



July 16, 2012

Mr. Carl Jordan  
Office of Size Standards  
U.S. Small Business Administration  
409 Third Street, SW  
Washington, DC 20416

Re: Comments of NSBA in Connection with the U.S. Small Business Administration's (SBA) Proposed Rule: *Small Business Size Regulations, Small Business Innovation Research (SBIR) Program and Small Business Technology Transfer (STTR) Program*; RIN: 3245-AG46

Dear Mr. Jordan:

The National Small Business Association (NSBA) is the nation's oldest nonpartisan small business advocacy organization, with more than 65,000 small-business members in every industry across the country. On behalf of the NSBA, I would like to submit the following comments on the U.S. Small Business Administration's (SBA) Proposed Rule: *Small Business Size Regulations, Small Business Innovation Research (SBIR) Program and Small Business Technology Transfer (STTR) Program*; RIN: 3245-AG46.

Having long advocated for the reauthorization of the Small Business Innovation Research (SBIR) Program, I would first like to thank you for the opportunity to comment on this public rulemaking and express our gratitude for the SBA's continuing effort to formulate a rule that reflects the unique needs and limitations of small business. That said, given the nature of NSBA and our very broad-base of industries represented by the association, we have some serious concerns with the SBA's proposed rule changes. Specifically, we are troubled by the proposed elimination of the restriction against foreign ownership of SBIR firms and an easing of the affiliation rules for large firms, both of which will create significant loopholes through which foreign and larger corporations can divert funding away from the intended recipients of these awards: small businesses.

Accordingly, in response to the SBA's request for comments on its proposed rule: *Small Business Size Regulations, Small Business Innovation Research (SBIR) Program and Small Business Technology Transfer (STTR) Program*; RIN: 3245-AG46, the NSBA is pleased to submit the following comments.

#### *Section 121.701 – Definitions and Programs Subject to Size Determinations*

Although NSBA appreciates the SBA's efforts to promulgate regulations that will promote and facilitate innovation, job creation, and sustainable economic growth for America's small business community, NSBA believes that the SBA's proposed definition of the term "domestic business concern" falls well short of these goals and fails to meet

SBA's statutory obligations as identified in the SBIR/STTR Reauthorization Act. NSBA further believes that the proposed definition is neither "straightforward" nor "easy to understand" as stated in the proposed rule.

Section 5107(c)(1)(C) of the Small Business Reauthorization Act (which was incorporated in the FY 12 National Defense Authorization Act) reads as follows:

It is the stated intent of Congress that the Administrator should promulgate regulations to carry out the authority under section 9(dd) of the Small Business Act, as added by this section, that... preserve and maintain the integrity of the SBIR program as a program for small business concerns in the United States by prohibiting large businesses or larger entities or foreign-owned businesses or foreign-owned entities from participation in the program established under section 9 of the Small Business Act."

SBA's proposes to define a "domestic business concern" as follows:

A 'business concern or concern' eligible for SBA's programs is one that is for profit, has a place of business located in the United States, and which operates primarily within the United States or which makes a significant contribution to the U.S. economy through payment of taxes or use of American products, materials, or labor. SBA proposes that a domestic business concern meet this definition.

However, SBA has proposed additional criteria that a 'domestic business concern' must meet. SBA has proposed that for purposes of the SBIR and STTR programs, the domestic business concern must also be created or organized in the United States, or under the law of the United States or of any State. (See Federal Register Vol. 77, No. 94 – 5/15/12.)

NSBA believes that the proposed definition fails to ensure that an eligible business is "truly a domestic concern." NSBA recommends revising the proposed definition to focus more on ownership and less on where it is created or organized or whether it makes a "significant contribution to the U.S. economy through payment of taxes or use of American products, materials, or labor." Based on the proposed definition, any number of foreign-owned businesses or entities can be "organized in the United States," or make a "significant contribution to the U.S. economy," but nothing ensures that truly American concerns are the ones actually benefiting from a program established on their behalf. (See Section 5017(c)(1)(C); "It is the stated intent of Congress that the Administrator should promulgate regulations... [that] preserve and maintain the integrity of the SBIR program as a program for small business concerns in the United States by prohibiting large businesses or larger entities or foreign-owned businesses or foreign-owned entities from participation in the program established under section 9 of the Small Business Act.")

### *Section 121.702 – Ownership and Control*

For the above-mentioned reasons regarding the definition of "domestic business concern" NSBA believes that the SBA's proposed rule changes fail to meet the statutory purpose and intent of the Act, specifically with respect to the proposed domestic ownership requirements of the applicant and ownership by other-than-small businesses.

NSBA further believes that the proposed rules fails to address the issue of foreign-owned or foreign-controlled venture capital operating companies (VCOCs), hedge funds or private equity firms. A failure to promulgate rules on this matter will allow foreign

interests to compete for and benefit from American taxpayer-funded research and development funding, all at a time when job creation and long-term economic growth remain a top priority for this country.

Under current law, “an SBIR awardee must be a business concern that is at least 51% owned and controlled by U.S. citizens or permanent resident aliens or at least 51% owned and controlled by U.S. citizens or permanent resident aliens.” Instead of retaining the current definition that is both “straightforward and easy to understand,” SBA proposed new regulations regarding eligibility for the program. Specifically, the SBA proposed that an SBIR/STTR applicant must be:

More than 50% owned and controlled by U.S. citizens, permanent resident aliens, or *domestic business concerns* [(emphasis added)]; or [m]ajority-owned by multiple domestic VCOCs, hedge funds or private equity firms.

This proposed rule change creates a scenario whereby an SBIR or STTR applicant is majority-owned by multiple VCOCs, hedge funds or private equity firms, who may be “created or organized” in the United States but whose investors are foreign-owned businesses or entities. Again, a critical issue when economic growth and job creation remain a top priority for our country.

While NSBA agrees with the SBA’s decision to not propose any changes to the 500-employee size standard, it does believe that the proposed rule change regarding domestic-owned applicants and domestic ownership by other-than-small businesses fails to meet the statutory obligations set-out in the SBIR/STTR Reauthorization Act and the Congressional intent underpinning this critical piece of legislation.

### *Section 121.703 – Affiliation*

NSBA disagrees with the SBA’s decision to propose amendments to the current affiliation provisions with respect to minority stock holdings and the current affiliation provisions regarding a company’s affiliation with other entities. Both efforts reverse course on established affiliation provisions that have focused on an ownership standard instead of the proposed management (or “board of directors”) standard. Furthermore, NSBA questions the SBA’s reasoning behind applying the proposed affiliation rules solely to the SBIR and STTR programs and not SBA as a whole.

NSBA believes that the proposed rule changes will not only cause confusion among members of the small business community, but may also allow foreign and large corporations or other entities to participate in the SBIR and STTR programs. Accordingly, NSBA recommends that the SBA continue to use the current affiliation provisions with respect to the SBIR and STTR programs.

### *Conclusion*

The SBIR program is the nation’s largest source of early-stage research and development funding. Providing more than 50,000 patents since its inception, SBIR has successfully harnessed the proven innovative power of small, technology-based businesses to meet the

nation's technology needs. On average, the SBIR program generates seven new patents per day - which is far more than all U.S. universities combined, at less than one-twelfth their level of federal research and development funding.

Small businesses are America's economic engine and are the most dynamic and innovative sector of the U.S. economy. They comprise 99.7% of all domestic employer firms, employ approximately 50% of all private sector employees, and have created roughly 65% of America's net new jobs over the past 17 years.

As the President has stated time and time again, small businesses are the backbone of our economy. Unfortunately, if the proposed rule is allowed to go into effect without significant revisions, this may no longer be the case. Again, we appreciate SBA's continuing effort to formulate a rule that reflects the unique needs and limitations of small business, and look forward to working with you as this process moves forward.

Sincerely,

A handwritten signature in black ink, appearing to read "Todd O. McCracken". The signature is stylized with a large, sweeping initial "T" and "M".

Todd O. McCracken  
President