Commentary

The VC manifesto: Special pleading for a damaged cause: Commentary on Simon Witney interview

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First, the facts. Simon Witney's interview[1] starts from reviewing the British Venture Capital Association (BVCA's) *Venture Manifesto* (VM), and so we should start there too, distasteful as it is to wade through six pages of apologia for one of the less useful parts of the European economy. Nothing in the VM is obviously factually wrong (I hasten to say, as lawyers are eager in the wings). For example, the BVCA 'VM' states that many US companies, having gained initial funding in the United States, are moving to Europe. True, but this is to gain liquidity and funding on London Stock Exchange's Alternative Investment Market (AIM) or benefit from European grant schemes, and is nothing to do with European Venture Capital (VC). They say that 100 exits over £100 million have been achieved since 2004. True, but virtually all have been from companies receiving VC funds late in their development if at all, not VC-backed start-ups. £434 million was invested in what the BVCA describes as early stage start-ups in 2007, but what is early stage? What was invested in 2008, when they actually needed it more? (One 'early stage' BVCA investor member has turned down a 3-year-old biotech with strong animal Proof of Concept (PoC) data, good patents, world-class science and a signed pharmaceutical company development collaboration because they were 'too early.') And so on. In short, the tone of the VM is so completely at odds with what has been happening on the ground in biotech in the United Kingdom that one wonders what in decade the VM was written. I have described at far greater length what VC has really done to biotech in the United Kingdom,[3] as well as showing on the basis of more robust data than the BVCA is willing to release (and Witney is willing to discuss) how poorly biotech VC has performed in reality. If budding entrepreneurs want to know what VC really does, they should read that.

The manifesto echoes a lot of what the BioIndustry Association (BIA) has been saying. In 2003, the BIA was the principal member of a group called the Bioscience Innovation and Growth Team (BIGT). BIGT published *Bioscience 2015*, a report that laid out a plan to revitalize the United Kingdom's then ailing biotechnology industry, aided by substantial government money. The report's said that its goals were to achieve.

- A diverse, self-sustaining bioscience sector, with a core of large, profitable, world-class companies, second in size and achievement only to the United States.
- The most efficient and effective setting for conducting clinical trials in the world – a source of true distinctiveness.

- A health-care system, regulatory regime and business environment that support innovation in bioscience, delivering early access for patients.

David Cooksey said in his introduction to the original report '*The acid test for me is … whether the bioscience industry thrives in the UK. If the sector grows in line with the best of its overseas rivals, shows increased employment, increased profitability, an increased pipeline of new therapies and resilience in the face of intensifying international competition, I will count this a success.*'

Bioscience 2015 did some good. It brought the issue of economic terrorism masquerading as 'animal rights' into public awareness. It pushed for coordination of clinical trials which, if not achieved, at least raised the problem up the agenda and laid the seeds for today's interest in translational medical research.

But for the most part, exactly the opposite of the report's goals has happened, just as the reality is exactly the opposite of what the VM implies. The size, number and wealth of biotech companies in the United Kingdom has shrunk dramatically, start-up rates and employment have declined, there are now no independent, world-class biotech companies left in the United Kingdom (profitable or not), clinical trials have halved, and it is harder for UK patients to receive cutting edge medicines that ever before. Most particularly, the investment industry, which *Bioscience 2015* said was the mainstay of UK biotechnology and a part of the industry that the government should support energetically, has demonstrated failure to create or build companies, failure to invest and failure to make profits. And this is not just the 'credit crunch.' The decline started almost as soon as *Bioscience 2015* hit the government's desks.

When recently the BIGT has published *The Review and Refresh of Bioscience 2015,* many recommendations boil down giving more money to the same people as were asking for it last time, in tax breaks and cash.

It is not surprising that the BIA, whose agenda is based on a presumption that VCs are essential, should spend the whole of Chapter 3 of the new report on how government should support investors. It is not surprising that an organization whose membership has nearly twice as many consultants, lawyers and other advisors than actual biotechnology companies should suggest that the solution to the industry's woes lies in changes to laws and accounting rules that those accountants and lawyers advise on, and VCs use. It is not surprising that the BIA and others are clamoring for a billion-pound 'investment' (bailout, as we mere scientists would call it) for the VC industry. These are interest groups begging for power and money for their members. And obviously, the BVCA will ask for more tax breaks, incentives and so on for VCs. They would say that, wouldn't they?

But the reality is that VC investment in biotechnology in the United Kingdom has been a disaster to everyone except the VCs. Companies have been stunted, investors in the VC funds have lost money, entrepreneurs have been driven away[2] and opportunities for new drugs, new energy products, and new industrial technologies have gone overseas or, worst, allowed to disappear. Witney's comments at the start of his interview are simply not applicable to biotechnology. As an asset and investor class, the actual data show that VC has been positively toxic to UK biotech entrepreneurship.

One thing Witney has right is that the UK tax system is a mess. Tax changes are always driven by short-term political issues. Taxation is one of the few ways left to national governments to control their territory in an era of globalization. Much of the problem with UK taxation stems not from VC shareholding but from the labyrinthine rules around taxation. You have to spend days learning about the United Kingdom's R&D tax credits system *before* you start research, or you might find that your research is ineligible for an R&D tax credit because of something you should have done at the start, years before you claim the tax break, such as remove the word 'recharge' from your collaboration agreement or to file your draft patent the day before, not the day after, the postdoc started work. Similarly, small- and medium-sized enterprises (SMEs) have always been eligible to compete for public contracts, but the tender process is so bureaucratic and complex that they just do not have the time. The BVCA is not the right organization to lead this, however. VCs thrive on complexity as anyone who has read a VC term sheet or shareholder agreement will know.

And it is right that the tax rules around 'angel' investments are a bit of a mess and, more importantly, change faster than the companies in which angels invest.

But there are many other, bad suggestions in the BVCA manifesto, the various begging documents put out for more government to give more money to VCs, the BIA documents, and the many interviews and press releases that flutter around them including the Witney interview. It is not surprising that these interest groups are using the current crisis to improve their position. Alas, there is a risk, as Witney acknowledges, in these times of crisis, that governments grasping at fiscal straws agree with the interest groups' arguments and pour cash into the discredited VC business model. This would be a bad thing. To try to get more University spin-outs, more subsidized seed funding for those spin-outs and to suck angel investment into them prior to VC investment is unwise. This is just providing cheap feedstock for an already discredited VC business model, one based on using investee companies as fuel to be burned up, not as raw material from which to build winning products.

Who should benefit from government changes, largesse and support? Not the investment industry. It is time to stop propping up a fundamentally broken idea of how to support biotechnology in the United Kingdom through supporting VC investment, or the tax structures, accounting abnormalities and hidden subsidies that prop them up. The evidence is overwhelming: VC is not good for biotech in the United Kingdom.[3]

Possibly the University Challenge Funds could be vehicles, if liberated from the absurd rules that make them the whipping boys of the commercial investment industry today. Possibly Angel investment groups, who are motivated to grow companies (but how do you stop them becoming VCs?)

Possibly the R&D tax credit system, which gives cash to companies doing R&D. Making the scheme more generous and more targeted towards SMEs would help anyone investing in R&D in the United Kingdom.

And possibly – and here is a radical idea – we could support the scientists who create the ideas and run the science in academia and industry. Could we return to the idea that bright scientists are motivated to solve problems, and should be supported to allow them to do so? Paying scientists to solve problems just might solve those problems. Paying investment groups to make money for themselves, directly through bailout investments or indirectly by feeding them tax-breaks or cash-starved start-ups to chew up, certainly will not.

REFERENCES AND NOTES

1. VC Experts.com. (2009) The venture manifesto: Interview with Simon Witney, Partner SJ Berwin LLP on 18 February 2009, http://vcexperts.com/vce/news/interviews/interview_000011.asp.
2. There are so many ex-Pat Brits in the Boston biocluster that they not only have their own network organizations but their own branch of the Cambridge (United Kingdom) network as well.
3. Bains, W. (2008) *Venture Capital and the European Biotechnology Industry*. Basingstoke, UK: Palgrave Macmillan.

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