



Jackson Walker LLP

# PUTTING THE BUSINESS IN SBIR/STTR

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Chris Rourk and Erin Camp  
Jackson Walker LLP

<https://www.jw.com/sub-practice-areas/jw-startup/>

A wide-angle photograph of a city skyline at dusk or dawn, with various skyscrapers and buildings illuminated against a soft, colorful sky. The image serves as a background for the top portion of the slide.

# Presentation Overview



- **The business component for SBIR/STTR**
- Forming a business for growth
- What investors look for in a business
- Where to network for startup business hiring

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# The business of SBIR/STTR



- SBIR and STTR both require a domestic small business
- How small is small? That is defined by the Small Business Administration regulations at 13 CFR 121.101 et seq., which defines the number of employees (full time and part time) depending on the type of business.
- For example, a small business in Research and Technology in Nanotechnology can have 1000 employees max, whereas a small business in Record Production and Distribution can have 250 employees max.
- There are annual receipts limits for certain businesses
- Employees/receipts limits include any affiliates that have power to control or are controlled





# The business of SBIR/STTR



- Forming a business versus finding a small business partner
- Forming a business:
  - Pro – total control over team members, no conflicts
  - Con – time and money spent on formation, logistics, management
- Existing small business partner:
  - Pro – business already formed and in operation
  - Con – less control over team members and potential conflicts; deferred costs
- Key questions – what do you want to spend your time on? How important is it to trust your team?

A wide, low-angle photograph of a city skyline at dusk or dawn, with various skyscrapers and buildings silhouetted against a soft, colorful sky. The image serves as a background for the top portion of the slide.

# Presentation Overview

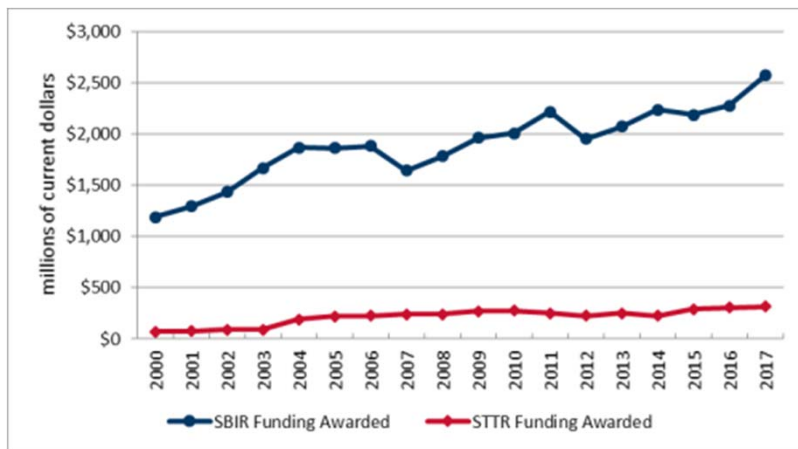


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# Forming a business for growth

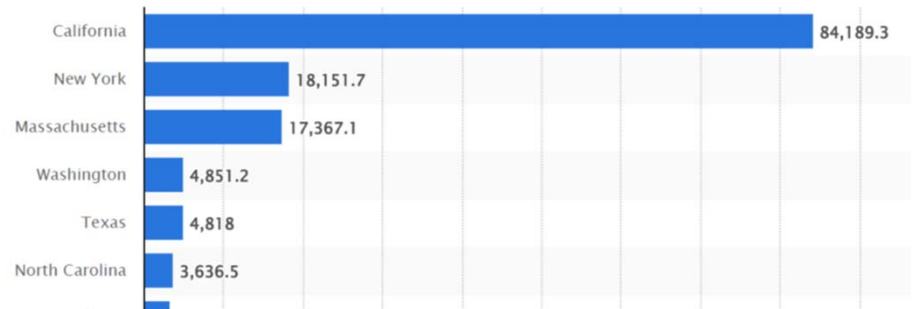


- Government versus private startup funding:



\$3+ billion nationwide  
Non-dilutive  
No loss of control

Value of venture capital investment in the United State in 2020, by state  
(in million U.S. dollars)



>\$100 billion nationwide  
Exchanged for equity  
Some loss of control

# Forming a business for growth



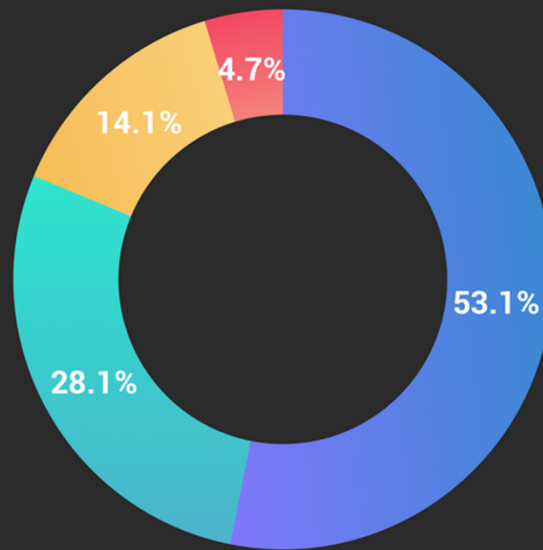
- Texas Venture Capital deals:

## Distribution Of Texas VC Deal Volume In Q1 '19

Based on data aggregated by metro area for venture rounds. Excludes PE.

- Austin
- Dallas
- Houston
- Other TX Metros

crunchbase news



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# Forming a business for growth



- Typical funding cycles of a startup:
  - Seed round –Basic research, basic product design, proof of concept. SBIR/STTR Phase I, maybe \$10K to \$100K other funding
  - Angel round –minimum viable product (MVP) prototype and revenue model. Typically \$100K to ~\$2 million investment round, also SBIR/STTR Phase II
  - Venture rounds – commercially validated MVP and revenues. Invest in rounds referred to as series A, B, C etc., typically >~\$2 million. Anti-dilution?
  - Mezzanine/bridge funding – usually for businesses that are generating substantial revenue (private contracts, SBIR/STTR Phase III?)
- It's never too early to talk to any level of investor, but most will only fund in their windows.



# Forming a business for growth

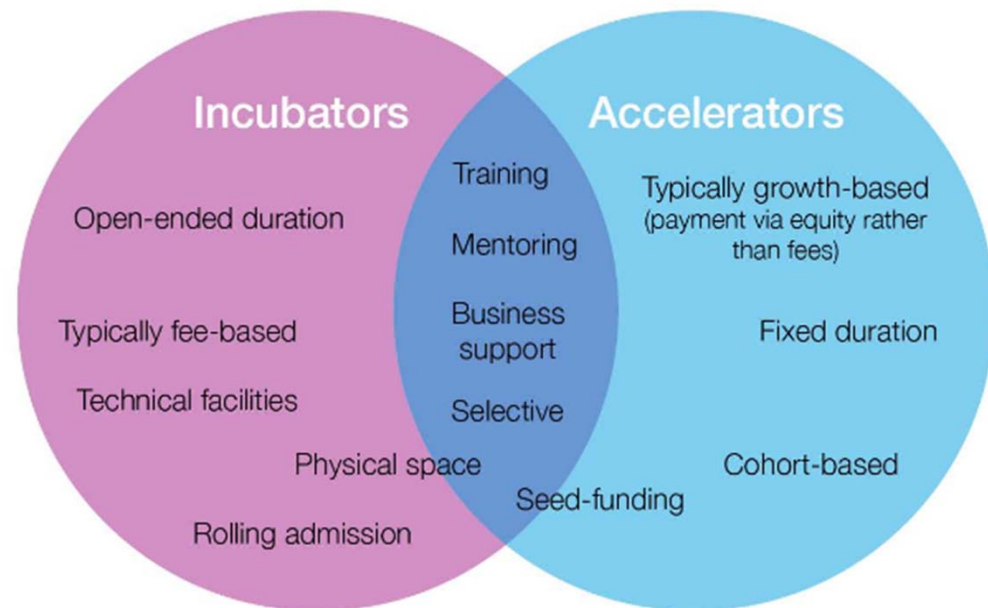


- Seed round – savings accounts, friend and family money. Considerations:
- Should you use your retirement funds to start up a company?
- What if you never pay back friends and family? Simple Agreement for Future Equity (SAFE)?
- Cost for legal, accounting advice, start work on MVP prototype, research
- Office space? Employees? Equipment?
- **How much does it cost to build a minimum viable product?**
- **What is the estimated market, sales channels?**
- Founders At Work – Stories of Startups Early\_Days -  
[https://www.academia.edu/download/56623151/Founders At Work -  
Stories of Startups Early Days - Jessica Livingston.pdf](https://www.academia.edu/download/56623151/Founders_At_Work_-_Stories_of_Startups_Early_Days_-_Jessica_Livingston.pdf)

# Forming a business for growth



- Incubators – pre MVP
- Accelerators – post MVP



Source:

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/608409/business-incubators-accelerators-uk-report.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/608409/business-incubators-accelerators-uk-report.pdf)



# Forming a business for growth



- Types of business entities
  - Sole Proprietorship
    - No separate business entity
  - Partnership
    - General Partnerships and Limited Partnerships
  - Corporation
    - “C” Corporations and “S” Corporations
  - Limited Liability Company
    - Simple, cost effective and flexible

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# Forming a business for growth



- **Sole Proprietorship**

- How many small/solo businesses operate
- Completely identified and intertwined with you, the entrepreneur
- No separate tax filings
- No limitation on liability





# Forming a business for growth



## • Partnership

- General Partnership – A “multi-person sole-proprietorship” with no limit on liability
- Limited Partnership – One or more general partners with control, and one or more limited partners with limited liability
- Ability to raise capital
- File a separate income tax return (Form 1065) but “bottom line” income and losses passed directly to personal income tax return
- Ability to set up “Special Allocations”
- If you go this route, should consult an accountant on tax issues and have an attorney draft a clear Partnership Agreement and other formation documents

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# Forming a business for growth



- “C” Corporation

- Ability to raise capital
- Shielded from liability
- “Double Taxation” issue
- No limit on number or type of shareholders
- File 1120 annually
- If you go this route, should consult an accountant on tax issues and have an attorney draft clear Bylaws and other formation documents

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# Forming a business for growth



- “S” Corporation

- Ability to raise capital
- Shielded from liability
- Similar to a partnership, has pass through taxation
- Limit on number and type of shareholders
- No Special Allocations
- File 1120S Form annually
- If you go this route, should consult an accountant on tax issues and have an attorney draft clear Bylaws and other formation documents

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# Forming a business for growth



- **Limited Liability Company**

- Ability to raise capital
- Shielded from liability
- The most flexibility: Can be taxed like a corporation or a partnership
- No limit on number and type of shareholders
- If you go this route, should consult an accountant on tax issues and have an attorney draft a clear Limited Liability Company Agreement and other formation documents





# Forming a business for growth



- Distribution of equity at formation
  - No “take backs”
  - Lack of equity and over-dilution of equity
    - Dilutes the rights of any current/founding equity holders and could be unattractive to additional investors
  - Benefits of a simple capitalization table
  - Assurance that the founder maintains the long-term control that they anticipate

A wide banner image at the top of the slide shows a city skyline at dusk or dawn, with various skyscrapers and buildings silhouetted against a soft, colorful sky. The title 'Presentation Overview' is centered over this image in a white, sans-serif font.

# Presentation Overview



- The business component for SBIR/STTR
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- **What investors look for in a business**
- Where to network for startup business hiring

# What investors look for in a business



- **Understandable minimum viable product (MVP) and value proposition (no research projects).**
- **Who are the competitors and what are the existing solutions? Why does your product/service beat them?**
- **Intellectual property protection that is aligned with MVP.**
- **Realistic revenue projections.**
- **Realistic company valuation.**
- Proper corporate structure.
- **Team members with a track record.**
- First to market.



“Fryergate”



# What investors look for in a business

- Team members:
  - **Chief Executive Officer – primary job is fundraising, forming partnerships, finding customers, running the company**
  - Chief Technical Officer – primary job is developing the MVP and additional products
  - Chief Accounting Officer – primary job is controlling cash flow
  - Chief Marketing Office – primary job is selling the product
  - Board members – should be people with relevant industry experience
- Do you need any of these? Not immediately for SBIR/STTR, but they are important for later funding rounds.





# What investors look for in a business

- Types of early stage financing
  - Debt financing
    - Borrowed money that must be repaid with interest on a certain timeframe
  - Equity financing
    - Money given in exchange for ownership interests in the company
  - Hybrid – Convertible Debt
    - Debt that can be (and is usually expected to be) converted to equity ownership in the company at a later date, instead of being repaid with cash
  - “Bootstrapping”
    - Founders putting in their own money, reinvesting profits into the business and operating lean to minimize funding needs

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# What investors look for in a business



- Debt Financing
  - Pros for startups
    - No dilution
    - Low interest rates means low cost of capital
    - Generally quicker and cheaper to get a small (less than \$5 million) loan than complete an equity raise
  - Cons for startups
    - Often very difficult for early stage companies to get traditional loans
    - Need some combination of a good credit rating, proven history, business or personal assets for collateral and/or personal guarantee
    - Will need to make regular payments (“debt service”)

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# What investors look for in a business



- Equity Financing
  - Pros for startups
    - Easier to get than bank loans because equity investors are more interested in potential for future growth than lenders
    - Entire ecosystem of professional investors focused on startups (angels, venture capital)
    - Professional investors can provide guidance and networking in addition to capital
    - No interest or principal payments, you get to keep the money
  - Cons for startups
    - Dilution and potential to lose control of the company
    - Generally more complicated and expensive process
    - Widely differing terms, need to “shop around”
    - Very early stage companies relegated to friends and family, angel investors will be interested later and venture capital is only looking for startups past the early stage



# What investors look for in a business



- Convertible Debt
  - Pros for startups
    - Unlike traditional bank loans, convertible debt is based on future potential of the company, not credit rating or historical results
    - Less dilution because no equity given right away, converts later at agreed upon conversion rates (usually a minimum rate and a rate based on future equity raises)
    - Unlike traditional debt, no interest or principal payments
    - Generally quicker and cheaper to issue convertible notes than complete an equity raise
  - Cons for startups
    - Dilution occurs upon conversion
    - A fairly complex process that will require involvement of lawyers and other professionals





# What investors look for in a business

- Bootstrapping

- Pros for startups

- No dilution
    - Maintain control
    - No time or money spent on completing equity raises or other financings

- Cons for startups

- Generally less capital available for growth
    - Founders will need to put in more “sweat equity” (time and effort) to do all the jobs they can’t afford to hire out
    - Will need revenue quickly and a strict budget to avoid a cash crunch (just a dry month or two can kill a startup)
    - No added experience or network from professional investors
    - Early stage equity incentives not worth as much

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# Where to network for startup business hiring

- Angel investors
  - Many are former C-level execs from startups that had an exit event (IPO, acquisition, merger), may be looking for their next one.
  - Angel investors usually want at least one board seat.
  - You may need to present to dozens of angel networks to get funded.
  - Show up early, stay late, talk to as many people as possible, exchange business cards, follow up.
  - Executive director of angel group can help to prepare you for presentation, may screen.
  - Usually a nominal fee associated with presenting to the group to screen out companies that are not ready or serious.
  - Don't need to be incorporated, but it helps to have good corporate formalities.



# Where to network for startup business hiring

- Angel Networks

- Aggie Angel Network <https://mcferrinrevventures.com/aggie-angel-network/>
- Central Texas Angel Network (Austin) <https://ctan.com/>
- North Texas Angel Network (Dallas) <https://www.northtexasangels.org/>
- Houston Angel Network <https://www.houstonangelnetwork.org/>
- Alamo Angels (San Antonio) <https://alamoangels.com/>
- Alliance of Texas Angel Networks <https://allianceoftexasangelnetworks.com/>
- Angel Capital Association (national) <https://www.angelcapitalassociation.org/>
- Angellist (national) <https://www.angellist.com/>



# Where to network for startup business hiring

- Incubators:
- at least 130 in Texas  
([https://gov.texas.gov/uploads/files/business/business\\_incubators\\_directory.pdf](https://gov.texas.gov/uploads/files/business/business_incubators_directory.pdf))
- Texas A&M incubators:
  - <https://engineering.tamu.edu/student-life/eep/engineering-incubator/index.html>
  - <https://tees.tamu.edu/research/facilities/clean-energy-incubator.html>
  - <https://energy.tamu.edu/research/initiatives/convergence-research-incubator-core/>



# Where to network for startup business hiring

- **Accelerators:**

- Startup Aggieland <https://mcferrin.tamu.edu/>
- Safe Tech <https://makesafetech.org/>
- Texas A&M Bioscience Business Accelerator ([https://vpr.tamu.edu/wp-content/uploads/2021/09/DOR\\_Fact\\_Sheet\\_BioscienceBusinessAccelerator.pdf](https://vpr.tamu.edu/wp-content/uploads/2021/09/DOR_Fact_Sheet_BioscienceBusinessAccelerator.pdf))
- Tech Wildcatters (Dallas) [www.techwildcatters.com](http://www.techwildcatters.com)
- Capital Factory (Austin) [www.capitalfactory.com](http://www.capitalfactory.com)



# Where to network for startup business hiring

- **Key networking points:**

- Ask questions – are you interested in startups? Are you interested in the field (of your startup)? Do you know anyone who is (if they are not)?
- Have an “elevator pitch” memorized – 30 second description of what your startup will do to make money.
- Listen – even when someone is not interested in your startup, they might know someone who is and not even realize it.
- Work the room – try to meet as many people as possible.
- Follow up – use Linked In or send an email.




Thanks!




**Chris Rourk,**  
Partner

Jackson Walker LLP  
2323 Ross Avenue,  
Suite 600  
Dallas, TX 75201  
V: (214) 953-5990  
F: (214) 661-6604  
[crouk@jw.com](mailto:crouk@jw.com)

**Erin Camp,**  
Senior Associate

Jackson Walker LLP  
112 East Pecan,  
Suite 2400  
San Antonio, TX 78205  
V: (210) 978-7746  
[ecamp@jw.com](mailto:ecamp@jw.com)  
 @TexasCorpLawyer

**Art Cavazos,**  
Partner

Jackson Walker LLP  
112 East Pecan,  
Suite 2400  
San Antonio, TX 78205  
V: (210) 978-7720  
[acavazos@jw.com](mailto:acavazos@jw.com)  
 @FinanceLawyer



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