STRATEGIC PLANNING

Forming an international biotechnology spinout: Is it worth it?

Substantial opportunities exist, but timing and communication issues must be carefully considered.

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Conventional wisdom would argue that the best opportunities for starting and developing biotechnology companies are in the US. The historical availability of capital, scientific and managerial personnel, favorable tax considerations, and the track record of many successful US biotechnology companies make such an assertion hard to deny. However, in the past two years, the opportunities for starting and running biotechnology companies in Europe have changed so dramatically that bioentrepreneurs must now reevaluate this US-centric vision of the field.

In our view, there is currently a major opportunity for US biotechnology companies to spin out existing technology into a stand-alone European counterpart that can benefit both the spinout and parent companies. From the perspective of Ribozyme Pharmaceuticals (RPI; Boulder, CO), it allowed us to accomplish our company's primary goal of developing novel therapeutics and at the same time accelerate development of a business that is a source of validated therapeutic targets and oligonucleotide leads. From the Atugen Biotechnology GmbH (Berlin) perspective—the company we helped spin out—they received a well-developed technology, extensive intellectual property, an existing customer base, and management advice to give them a competitive edge in the target-validation market (see "International biotechnology collaborations: Points to consider").

Creating this type of "win-win" deal was difficult to negotiate because it broke so much new ground. But, as the dust settles, it is apparent that the value to both companies is the leverage they provide each other in the rapid deployment of a novel technol-

ogy and the opportunity to increase value for their respective stockholders.

Overcoming preconceptions

Perhaps the greatest barriers to creating a Euro-American company are the preconceptions all parties initially carry to the

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negotiating table. For US bioentrepreneurs, the first preconception to overcome is that Europe is an extremely difficult place to grow a biotechnology business. While this may have been the case in the past, Europe has made a dramatic swing to a pro-biotechnology stance in human health. This has resulted in the availability of new capital sources and a "top-down" commitment to growing biotechnology companies from government officials, academic institutions, and many pharmaceutical companies. As part of this commitment, Europe is looking to the US for the skill set to make this happen quickly. Given the existing infrastructure of world-class science, this makes Europe an appealing venue for business development. Once one understands the potential of this opportunity, the next set of preconceptions that need to be overcome are objections from within your own company about entering into these kinds of negotiations.

Board members are likely to view the new enterprise as too great a drain on managerial and financial resources to justify the investment—regardless of the financial projections. Stockholders may express concerns over whether the stock price will increase or decrease as a result of the transaction—especially in the short term. And

employees will question what this means for their job security. These are all legitimate concerns.

Once you have convinced your company that this opportunity is worth looking into, you may next find yourself overcoming preconceptions held by the government agency responsible for the European initiative. Many times their greatest worry—based on either historical precedent or simply fear of change—is that a US company is simply trying to create a shell that will allow it to siphon funds back to the US. It is also likely that you will have to overcome the European investor's preconceptions that the mother company's management will either not spend sufficient time growing the new company or will dominate the management to the point where European managers will not be able to learn biotechnology-specific skills.

Unfortunately, all of these concerns are legitimate. Setting up a new company, you must take all of them into account and try to balance them appropriately. Perhaps the best advice is, "Get used to it." You are creating something for which there are no models. As part of the process you will necessarily be managing a diverse set of expectations. Focus on gaining the trust of the various negotiating parties from the outset. Find points of congruence in the differing agendas of all the players at the table and work to create a structure that includes them all. By keeping focused on the opportunities for all parties in making these negotiations work, these seemingly insurmountable differences will appear at the end of the day to be relatively minor frustrations.

Nuts and bolts

Overcoming preconceptions and managing expectations is only the first stage of building an international company. The next stage is bolting together an organization that takes into consideration the different ways that the two cultures do business, handle financial transactions, and offer legal

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protection. While this article can not hope to cover all these aspects, here is a sampling of what to expect.

The first issue is time. Bioentrepreneurs run on a different clock than government organizations and investors, whether in the US or Europe. In governmental organizations, timeliness is nearly always replaced by concerns that mistakes should be avoided. This usually translates into very long decision-making processes.

If the organizational representative believes that, "We have done it this way for years and the new company must abide by these rules," it is frequently difficult to make progress. Hierarchical organizations that employ linear decision-making processes can extend a process that could require only a few weeks into many months. This process is further extended by the necessity of managing it "long distance." The time losses encountered in travel necessitate fewer opportunities for face-to-face negotiations. Compounding this is the need to negotiate in multiple languages and multiple time zones—narrowing the window of what can be accomplished each day.

A second issue is defining the criteria of what constitutes a successful business. The traditional measurements of commercial success in Europe are much different from those of the US. In large part this is due to European unfamiliarity with entrepreneurial businesses. For example, in Europe a business has been required to be profitable historically to gain access to public markets. For a US biotechnology company—most of which go public years before they have a product to sell—this has been an unheard of requirement until quite recently. In addition, since there is no single European market for biotechnology IPOs such as NASDAQ in the US, how one plans the company's IPO becomes a strategic decision based on which of the many markets currently springing up will be the best place to leverage the company's value. While these issues are being re-thought in Europe, acceptance of alternative criteria is still slow in coming.

The differences in the legal systems between the two company's venues is also an issue that is likely to prove challenging. For example, a well-known US method of motivating performance is through stock option awards. The concept that an individual is willing to trade job security for substantial potential wealth through a stock-option award is well accepted in US entrepreneurial organizations. But this practice had no legal basis in German law until recently. Even now, programs of this type must be designed for the specific German state in which the company is

located—most states in Germany have no experience with this practice.

Growing an infrastructure

The third stage of building an international company is actually rolling up your sleeves and getting to work. One difficulty that makes initiation of a new kind of business in Europe very challenging is the shortage of experienced local management.

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minimized risk taking in business, academia, and government for decades. The result is that experienced biotechnology managers with local knowledge and language skills cannot be found, except for the rare individual who has been trained in Europe and has had entrepreneurial biotechnology experience in the US, and then wishes to return to Europe.

A related problem is that European recruiters generally have no experience in recruiting biotechnology management and so have few, if any, people of this type in their databases. This problem extends all the way to identifying potential board members for a new company. Finding people who have both relevant industry experience and entrepreneurial understanding is a real challenge, since most industry experience is not relevant to biotechnology company development.

A second problem is finding firms experienced in financing biotechnology. For example, venture capital sources have, with few exceptions, been established only recently. In addition, banks are unaccustomed to either the risk profile or the business model of biotechnology. Generally, they have limited, if any, experience in investment banking related to biotechnology. As a result, you may have to spend a long period of time educating nontraditional banking sources—such as government-backed commercial banks.

Finally, the lack of entrepreneurial experience in governmental agencies requires

patience in order to develop new structures appropriate to biotechnology companies. Each time the response of, "We can't do it this way" is encountered, an alternative needs to be created that allows the desired goal to be achieved through the creation of new or modified procedures and consensus building that is consistent with governmental policies and mandates. This is time consuming and challenging, both for the entrepreneur and government official.

Perhaps the best example of these financing issues is the "chicken-and-the-egg" problem Atugen encountered during its creation. Governmental agencies expressed enthusiasm for the proposed project, but indicated that their commitment would be contingent upon receipt of a commitment from venture capitalists. The venture capitalists indicated similar enthusiasm but insisted upon firm governmental commitments prior to closing their financial commitments. The obvious solution is to get all parties to commit separately, each contingent on the other parties' commitment. However, translating that solution into reality required enormous time and effort.

It is essential to have one or more persons or agencies "on the ground" in Europe to help expedite the company building process. Indeed, the RPI/Atugen story would not have been possible without it. The attention to detail, follow-up, local and state government connections, and knowledge of "how the system works" was provided by several economic development agencies in Berlin, as well as a consulting firm with extensive experience in Germany, each of which worked many months on this project.

Conclusions

Some critics will ask, "Why bother with Europe when you have everything you need in the US?" Part of the answer is that there are opportunities, both for individual companies and for the biotechnology industry, by accepting the challenge to create international biotechnology initiatives in Europe and elsewhere. This is not to say that it is easy. Transferring your biotechnology skill set to Europe requires careful consideration of the cultural, legal, and financial differences that need to be overcome to make an effective international organization.

In the final analysis, perhaps the most important question a bioentrepreneur can ask in deciding whether to look to Europe as a place to establish a spinout is, "Can my business be developed more rapidly and with greater stockholder value in Europe than in the US?" In our case, after all was said and done, the answer was clearly, "Yes." ///