November 8, 2021

Senator Amy Klobuchar
425 Dirksen Senate Building
Washington, DC 20510

Senator Tom Cotton
326 Russell Senate Office Building
Washington, DC 20510

Dear Senator Klobuchar and Senator Cotton:

On behalf of our nation's venture capital (VC) investors and the entrepreneurs they support, I write to express our opposition to the *Platform Competition and Opportunity Act of 2021* (S. 3197). The U.S. economy is the most dynamic in the world in large part due to our vibrant entrepreneurial ecosystem. We appreciate that a goal of your legislation is to increase competition against incumbent technology platforms. However, we believe S. 3197 will unfortunately harm startup activity in our country.

For entrepreneurs, an acquisition of their company is the most common liquidity opportunity and one that motivates founders to launch new companies. Barring acquisitions of companies by select acquirers would close the door to this opportunity and therefore provide a significant disincentive for new company formation, job creation, and innovation.

Background on VC and the importance of acquisitions

Venture capital is the fuel for high-growth startups that have transformed the world.[1] Recent examples include Moderna and Zoom, and past examples include Genentech, eBay, and SpaceX. VCs partner with entrepreneurs to build companies. This includes incubating a company within a venture firm, investing in a founder with merely an idea and a business plan, or providing capital and expertise to propel a company as it grows.

For venture-backed companies there are effectively three outcomes: standalone company (often via initial public offering, or IPO); merger or acquisition; or bankruptcy. Company failure is the most common outcome, but the success stories are often hypergrowth companies with a big impact. Many entrepreneurs and their investors begin the company building process with the

[1] VC funds make equity investments in a company and makes the longest-term investment of any asset class. The company's stock is generally illiquid until a company matures after five to fifteen years and as a result there is little actual value until a company goes public or is acquired.

hope of creating a standalone, public company. However, in most cases an IPO is not possible, and the preferred exit opportunity becomes an acquisition by another company, with 58% of startups expecting to be acquired.[2]

Some have incorrectly argued that acquisitions of VC-backed startups have become more common place; in fact, the opposite is true and must be recognized by policymakers. Over the last decade, the average annual ratio of VC-backed acquisitions to IPOs is approximately 13:1.[3] There are less acquisitions today relative to IPOs, with 886 venture-backed companies having been acquired in 2020, whereas 103 went public.[4]

These acquisitions contribute to the health of the startup ecosystem, as entrepreneurs who realize liquidity through the sale of their company regularly go on to found new, innovative companies, and often invest in other startups as angel investors or VCs. Furthermore, acquisitions help power the returns of VC funds, thereby supporting the pensions, endowments, and foundations that invest their capital in venture funds. In addition, acquisitions allow VCs to raise new investment funds and partner with the next generation of entrepreneurs. This "recycling effect" is one of the key drivers of dynamism in our economy.

These acquisitions are incredibly important to the startup ecosystem because in recent years it has become challenging for small capitalization companies to go public. The data bears out this reality in stark terms. The number of IPOs per year post-2000 has dropped by more than half relative to the preceding two decades. Companies going public are older than they used to be—the average age of a company undergoing an IPO in the last decade was around 10.7 years as compared to 7.5 years in the 1980s and 8.5 years in the 1990s. Far fewer small capitalization companies go public: between 1980-2000, companies with less than $50 million in annual sales made up about 50 percent of IPOs; post-2000 that number has dropped to about 35 percent. [5]

The reality is most young companies cannot realistically achieve the size and scale necessary to survive in the public markets of today. It has become more expensive and significantly more challenging to manage public companies. Much of the infrastructure that supported small companies going public has disappeared and the public markets have unfortunately become more short-term in nature. The frustrating result is that the U.S. now has roughly *half* the total number of public companies than there were twenty years ago.[6] Acquisition activity for most of these companies represents their only realistic chance of success. Yet S. 3197 would disrupt many of these transactions.

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[2] "2020 Global Startup Outlook," Silicon Valley Bank (2020) at 7, available at https://www.svb.com/globalassets/library/uploadedfiles/content/trends_and_insights/reports/startup_outlook_report/suo_global_report_2020-final.pdf.

[3] "NVCA Yearbook," National Venture Capital Association (2020) at 37-29, https://nvca.org/wp-content/uploads/2021/03/NVCA-2021-Yearbook.pdf.

[4] Id.

[5] "Initial Public Offerings: Updated Statistics," Professor Jay Ritter, University of Florida, available at https://site.warrington.ufl.edu/ritter/files/IPO-Statistics.pdf.

[6] *Capital Formation, Smaller Companies, and the Declining Nature of Initial Public Offerings,* Jeffrey M. Solomon, available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/jeffrey-solomon-presentation.pdf.

Specific concerns with S. 3197

The *Platform Competition and Opportunity Act* is effectively a ban on acquisitions by companies with a market capitalization of $600 billion or more that have at least 50 million U.S.-based monthly active users or at least 100,000 U.S.-based monthly active business users. Specific concerns with S. 3197 include:

•Had S. 3197 been in place, it likely would have barred the acquisition of at least 100 venture-backed companies in just the last five years.[7] This harsh penalty would be applied without any analysis of the benefits of the acquisition.

• S. 3197 would disproportionately impact startups in emerging ecosystems. In recent years, startup and venture capital activity has seen impressive growth in the middle of the country, thereby spreading entrepreneurial activity into new pockets.[8] But because companies in these regions do not tend to grow large enough to go onto the public markets, acquisitions are the far more common exit opportunity for entrepreneurs. S. 3197 would endanger the recent growth in emerging ecosystems by closing off potential acquirers of startups and disincentivize investment in new companies in these regions.

• S. 3197 would make it harder for startups to be acquired by reducing the number of potential acquirers. The impact of this is considerable: fewer potential acquirers would mean a reduced sales price for the company due to less bidders, resulting in less profitability for the entrepreneurs. This reduced profitability will make new company formation less attractive than it currently is relative to other opportunities, thereby negatively impacting employment, wages, and innovation.

•An unintended consequence of this dynamic is that many startup founders are former employees at large technology companies, and if entrepreneurship is less attractive then these individuals are far more likely to remain employed at established companies, thereby strengthening the hand of the very companies that S. 3197 is designed to curtail.

•Serial entrepreneur Bettina Hein has elaborated on how S. 3197 will backfire:

> By dramatically raising the regulatory hurdles and compliance costs of acquisitions, the act would benefit large incumbent companies that have money and teams of lawyers to navigate the new legal landscape. Smaller companies would be shut out. In this way—ironically—the bill would likely deepen and widen the competitive moat protecting large incumbent companies from smaller, more innovative challengers.[9]

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[7] Source: Pitchbook data

[8] "How Policymakers Can Capitalize on Two Geographical Trends in the Startup Ecosystem," Jeff Farrah (NVCA), *available* at *https://nvca.org/how-policymakers-can-capitalize-on-two-geographical-trends-in-the-startup-ecosystem/*.

[9] "Lawmakers Plan to Tank the Startup Economy, Bettina Hein (*Wall Street Journal*), *available at* https://www.wsj.com/articles/lawmakers-plan-to-tank-the-startup-economy-acquisition-antitrust-ipo-11634592207.

• S. 3197 is effectively a ban on acquisitions by certain companies because its exclusions are so challenging to meet. For example, one exclusion is that the acquiree does not "compete with the covered platform or with the covered platform operator for the sale or provision of *any product or service*."[10] The companies subject to S. 3197 are large, multi-faceted enterprises that arguably "compete" with vast amounts of smaller companies outside the core business of the acquirer, thereby nullifying this exception. Another exclusion is that the acquiree does not "constitute nascent or potential competition to the covered platform [.]"[11] In most cases, this is impossible to determine, especially for the government which is not a market participant and therefore does not have the relevant experience or expertise to make judgment calls on which companies may compete years down the road. Ultimately, the exclusions within S. 3197 are not exclusions at all, which makes the bill an effective ban on acquisitions without any analysis of the competitive effects of the transaction.

•Because S. 3197 bars the purchase of "the whole or *any part of the stock or other share capital*," the bill goes beyond restricting acquisitions and appears to bar even minority, non-controlling investments into startups by certain companies. Corporate Venture Capital (CVC) is the practice of investments by existing corporate entities into startup companies. CVC activity has been a growing and important source of capital for startups in recent years. In addition to providing capital to startups, CVCs also serve as important business partners as the new company scales. But S. 3197 would cut off this source of capital even though an acquisition has not occurred.

Thank you for your consideration of our views.

Sincerely,

Bobby Franklin

Bobby Franklin
President & CEO

CC: Chair Dick Durbin
Ranking Member Chuck Grassley

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[10] *See Platform Competition and Opportunity Act of 2021*, section 2 (b)(3)(a) (emphasis added)
[11] *See Platform Competition and Opportunity Act of 2021*, section 2 (b)(3)(b)