

Please bring your hard copy of the Incubator Report.

M E M O R A N D U M

July 19, 2012

TO: Planning, Housing, and Economic Development Committee
FROM: Jacob Sesker, Senior Legislative Analyst 
SUBJECT: Status Report – Department of Economic Development (Incubator review)

Introduction

DED Director Steve Silverman will present a summary of current economic indicators, and an update regarding the status of ongoing initiatives. Topics could include status of unfilled positions, status of negotiations with Montgomery Business Development Corporation, website, and re-certification of the Workforce Investment Board.

Deputy Director Sally Sternbach will present a review of the Montgomery County Business Innovation Network (BIN) program and policy. She may be joined by Mike Knapp (Orion Ventures, LLC) and John Korpela (Montgomery County Business Innovation Network).

Background: The Business Innovation Network

The Department of Economic Development (DED) will provide a status update regarding its efforts to evaluate and enhance the BIN. DED retained Orion to review the BIN program and underlying policies, and to recommend potential alternatives for consideration. Orion's presentation slides are attached at © 2. The review of the BIN is part of a larger effort on the part of DED, at the request of the Council, to better align DED programs with policy goals to achieve results. This July 2012 update follows up on the Committee's July 2011 worksession to discuss the same topic.

The mission of the BIN is to support the growth and development of businesses in Montgomery County in the fields of biotechnology, information technology, international technology, professional services, and women- and minority-owned businesses. The incubators provide the BIN companies with flexible and short term lease agreements, as well as other services and programs to support the development of these firms (e.g., educational seminars and networking opportunities).

The BIN currently includes 5 incubators and a Virtual Incubator Program. A sixth facility, to be located in the White Oak area, is currently under consideration. In 1993, the County created its first incubator (the Montgomery County Technology Enterprise Center) at a leased site located at 2092 Gaither Road in Rockville (no longer operational). The Shady Grove Innovation Center was opened in 1999. Four incubators were subsequently added to the BIN (Silver Spring in 2004, Wheaton in 2006, Rockville in 2007, and Germantown in 2008). See © 1 (Montgomery County Incubator Network Overview and FY11 Costs). See also Orion Report, Appendix 8. At roughly 150,000 gross square feet, Montgomery County's BIN is one of the largest incubator networks in the nation.

The *Virtual Incubator Program* currently serves 15 companies. The program provides entrepreneurs, scientists and researchers with the use of facility resources such as access to conference rooms, fax and copy machines. These companies also have to access to the support and mentoring programs provided to all BIN tenants.

The *Shady Grove Innovation Center* currently serves 44 companies, 35 of which are biotechnology companies. The facility has 60,000 gross square feet (33,680 leasable square feet). The facility has 76 office spaces and 24 wet labs. The facility is owned by MEDCO, but the County can assume full ownership of the facility upon retiring the debt in 2019.

The *Silver Spring Innovation Center* currently serves 23 companies, of which 10 are information technology firms and 10 are consulting/professional services firms. The facility has 21,000 square feet in size (9,920 leasable square feet). The facility has no lab space. The County owns this facility, and all debt has been retired.

The *Wheaton Business Innovation Center* currently serves 21 companies, 19 of which are in consulting and service industries. The facility has 12,000 square feet (5,623 leasable square feet). The Wheaton facility is targeted at the support and growth of minority- and women-owned non-technology companies. The County leases the facility from Westfield Wheaton Shopping Center.

The *Rockville Innovation Center* currently serves 23 companies, 13 of which are information technology firms. The facility has 22,000 square feet (13,339 leasable square feet). The facility is owned by MEDCO, but the County can assume full ownership upon retiring all debt in 2032.

The *Germantown Innovation Center* currently serves 29 companies, 15 of which are biotechnology firms and 9 of which are information technology firms. The facility has 33,000 square feet (17,513 leasable square feet). In addition to offices, the facility has 9 wet labs. The County leases this facility from the Montgomery College Foundation.

Incubators in context

Business/entrepreneurial development is a core economic development function. The function is often wholly or partially performed outside of local government (e.g., by private sector business development organizations or by academic institutions). Business/entrepreneurial development strategies often focus on technology-led development, due to the opportunities for rapid growth¹ and because the jobs in high-technology industries pay well in comparison to jobs in other industries.

¹ Note that not all tech-led development results in rapid growth. Information technology, for example, has relatively shorter product development cycles and much of the early investment necessary is investment in people with ideas. By

One business/entrepreneurial development strategy is to create a nurturing environment for firms (generally referred to as an “incubator” or “technology development center”). The following represents a definition of “incubator”, according to a 2011 report² from the U.S. Economic Development Administration:

“Business incubation programs are designed to accelerate the successful development of entrepreneurial companies through an array of business support resources and services, developed or orchestrated by incubator management, and offered both in the incubator and through its network of contacts. A business incubation program’s main goal is to produce successful firms that will leave the program financially viable and freestanding. Critical to the definition of an incubator is the provision of management guidance, technical assistance, and consulting tailored to young, growing companies.

“In the practitioner’s lexicon, ‘business incubation program’ and ‘business incubator’ often are used synonymously. However, the research team for this project defined a business incubator as a multitenant facility with on-site management that directs a business incubation program, as defined above. Business incubation programs usually provide clients access to appropriate rental space and flexible leases, shared basic business services and equipment, technology support services, and assistance in obtaining the financing necessary for company growth. Business incubation programs may also provide business assistance services for non-tenant clients, also referred to as *virtual* or *affiliate clients*.”

According to Orion, the number of incubators nationwide has increased from 12 in 1980 to more than 1,100 today. Since 2000, the incubator model has been expanded to include “virtual incubators” (i.e., incubator programs that do not have a real estate component) and “accelerators” (similar to incubators, but tend to provide more mentoring over a shorter period of time to bring a company’s products to market in less than one year).

Policy considerations

According to the Orion report, the objective of the original Montgomery County Technology Enterprise Center (MCTEC) was to provide “low-cost rental space and support services for knowledge-based, technology-intensive start-up or early-stage information technology firms.” The current incubators (all opening in 1999 or later) came into being between 1999 and 2008; consequently, all were planned and/or opened during a period of economic growth and tight real estate markets. As such, an emphasis on meeting the real estate needs of BIN companies was appropriate.

The BIN has maintained a focus on providing ready access to space for emerging technology firms with flexible terms. According to the report, **“Current DED leadership identified three basic policy objectives for the BIN: 1) to provide below market rent; 2) to provide a short-term lease option to businesses; and 3) to provide lease options with no requirement for personal guarantees.”**

comparison, biotechnology has a much longer product development cycle and requires significant capital investment in the early stages of development.

²“Incubating success: incubation best practices that lead to successful new ventures.”

Over time, reviews of the incubator program have also given great weight to real estate objectives (e.g., number of tenants, occupancy rates). However, to focus on occupancy as a measure of success risks losing sight of bigger policy objectives and could potentially skew the selection of BIN companies to those that are capable of filling larger amounts of space and/or moving in sooner. The Orion report observes that, “[R]eporting on BIN occupancy rates...reduces what many people view as a key government program designed to develop exciting, high-quality technology businesses, to a somewhat less glamorous landlord/tenant relationship.”

Occupancy of the BIN facilities is tied not only to the objective of providing low-cost and flexible real estate to businesses in strategic industries but to a measure of self-sufficiency. The facilities generate more revenue as occupancy increases, and therefore require less operating subsidy. In FY11, the County’s debt service obligations equaled \$791,000, and the County made \$855,000 in lease payments. At the same time, the County still provided an operating grant of \$1.37 million (not including personnel costs). See © 1 (Montgomery County Incubator Network Overview and FY11 Costs).

Policy alternatives

The Orion report suggests that DED should shift away from measuring occupancy to measuring economic impacts. The report acknowledges, however, the challenge of measuring or quantifying impacts that can be directly tied to the BIN. The report suggests 5 specific policy alternatives tailored to achieve measurable outcomes.

Industry-specific innovation clusters. The policy goal of this alternative is to achieve strategic company creation and job growth in specific industry sectors that will be beneficial to Montgomery County’s economic growth and expansion.

- *Example outcome:* To achieve creation and growth of a specified number of new firms each year in the areas of health information technology (health IT), life sciences, software development, green technologies, and cyber security.
- *Benefits/key characteristics:* Industry-specific review committee improves applicant selection process; increases synergies among tenants; branding/marketing support for the County’s efforts in key industries.

Accelerator. The policy goal of this alternative is to cultivate and identify early stage companies with high growth potential and entrepreneurs that would benefit from rigorous guidance, seed funding, and space to create a strong entrepreneurial environment and cultivate capital partners.

- *Example outcome:* To create a new screening process for emerging business ideas that could be short-term incubator tenants, resulting in X new tenants annually.
- *Benefits/key characteristics:* Identify and quickly move opportunities out of an incubator stage into viable and investable opportunities; particularly well-suited for internet startups that can move to market more quickly with less required investment.

Venture-based public/private innovation center(s). The policy goal of this alternative is to create and grow companies that are able to attract funding by establishing public/private partnerships to provide more rigorous assessment of program applicants, establish venture capital relationships with firms entering the Innovation Centers, provide more industry specific management and implement industry best practices.

- *Example outcome:* To establish X revenue-generating partnerships between county government, tenant companies and established private sector firms, including venture capital, real estate, and technology developers, resulting in X increased local investment.
- *Benefits/key characteristics:* Multiple venture funds partner in a single facility and identify “backable” firms and provide them with investment and pooled management resources; only provides space to firms that have been approved for investment; builds cadre of local investment partners.

Federal and academic partnering with innovation centers. The policy goal of this alternative is to leverage Montgomery County’s BIN to accelerate tech transfer and commercialization efforts from local federal and academic research assets, in order to identify and develop new companies and products based on the ongoing research being undertaken in these institutions.

- *Example outcome:* To establish a mechanism to provide a pipeline of new commercial opportunities based on research activities at the partner institution to create X new companies.
- *Benefits/key characteristics:* Identify commercial partners who share a research interest with the federal/academic research institution; leverage research that is already taking place to create new commercial opportunities.

Refine existing BIN. The policy goal of this alternative is to build upon the success of providing low-cost flexible space for emerging and life science companies by providing more diligence, guidance, and management milestones in order to improve program efficiencies and foster a higher graduation rate.

- *Example outcome:* Establish company specific milestones for continued BIN occupancy to ensure Montgomery County resources are assisting companies most likely to succeed.
- *Benefits/key characteristics:* Improve real estate management; increase accountability of BIN tenants; aid staff to provide guidance and programming to meet each company’s needs; reduce operating subsidy.

Report conclusions and recommendations

Orion performed an exhaustive review of the history of the BIN and concluded that “The goal of providing space for emerging technology firms was and continues to be the BIN’s primary policy objective.” However, Orion suggests that, even if the goal remains the same, the program can be improved.

Orion makes several specific recommendations, as well as general recommendations, for improving the County’s BIN (see pages 43-47 of the report). The recommendations include improved tracking of BIN tenants and BIN graduates; more proactive development of milestones to ensure timely graduation; consolidation/restructuring to eliminate the Wheaton Innovation Center and re-allocate those resources either to other BIN functions or to reconfigure other BIN facilities in order to accommodate current Wheaton BIN tenants; and establishing an industry specific focus for each BIN facility.

Staff conclusions/recommendations

Staff notes that implementing Orion's recommendations will require an **action plan that addresses the transition from the status quo**. For example, if DED elects to refine or reconfigure the existing BIN, DED will need to develop an action plan for current tenants of the Wheaton facility. Similarly, if DED elects to establish a specific industry focus for each facility, then DED will need to develop an action plan that does so while continuing to serve BIN tenants regardless of whether they are currently housed in a BIN facility that is appropriate for their industry. **Staff recommends that the Committee request a report from DED outlining its action plan for implementation of Orion's recommendations. That report should take place this fall.**

Appendix 2 of the report includes an inventory of BIN tenants, graduates and terminations. **Staff recommends a review of the former BIN graduates that are no longer doing business in Montgomery County in order to determine why those firms relocated elsewhere.**

Staff also recommends a review of how BIN graduates are (or could be) more involved in BIN program operations. For example, BIN graduates should be involved in selecting BIN tenants, serving on peer review panels, and formal mentoring relationships.

Contents:

©	Item
1	Montgomery County Incubator Network Overview and FY11 Costs
2	Presentation slides

Montgomery County Incubator Network Overview and FY11 Costs

	Shady Grove	Silver Spring	Wheaton	Rockville	Germanatown	Total
Year opened	1999	2004	2006	2007	2008	
Facility Size	60,000 sq.ft.	22,000 sq.ft.	12,000 sq.ft.	24,000 sq.ft.	33,000 sq.ft.	151,000 sq.ft.
Present Ownership	MEDCO	County	County leases facility from Westfield	MEDCO	County sub-leases from College	
Ownership Condition	County can assume sole ownership upon retiring debt in 2019	None	10-year lease with 3% annual escalation until 2014	County can assume sole ownership upon retiring the debt in 2032	20-year lease with 3% annual escalation until 2027	
Total Project Capital Cost	\$9.45 million (\$850,000 in County funds)	\$2.5 million (\$900,000 in County funds)	\$300,000 (All County funds)	\$6.6 million (\$900,000 in County funds)	\$6.7 million (\$2.95 million in County funds)	\$25.55 million (\$5.9 million in County funds)
Outstanding Debt	\$2.7 million	None	None	\$4.3 million	None	\$7 million
FY11 Debt Service	Approx. \$391,000	None	None	Approx. \$400,000	None	Approx. \$791,000
FY11 Lease Payment	None	None	Approx. \$270,000	None	Approx. \$585,000	Approx. \$855,000
FY11 County Operating Grant	\$299,710	None	\$225,270	\$400,000	\$442,000	\$1.37 million
Recommended FY12 County Operating Grant	\$450,000	None	\$300,000	\$400,000	\$500,000	\$2.05 million
	Above amounts will be slightly adjusted to reflect the actual operating costs for each center for FY12.					
Recommended FY12 County Personnel Costs	\$118,898	One staff covers both centers: \$107,620		SGIC staff covers RIC as well	\$126,488	\$353,006

Montgomery County Business Innovation Network (BIN): Program and Policy Review



The Report Objectives

- ❖ Montgomery County DED is assessing programs for future economic growth. Assessment includes the review of the BIN.
- ❖ Orion retained to
 - review the existing program policies and objectives,
 - provide policy alternatives and recommendations for DED, and
 - create a comprehensive list of current BIN tenants.
- ❖ Intended audience for Orion's report - DED management team and County policymakers.
- ❖ Report provides review and sets stage for future policy decisions—it does not include an in-depth analysis of policy alternatives, comprehensive fiscal analysis, cost assessment of proposed policy options, or comparative review of other incubator-like systems.



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The Approach

- ❖ Provide an overview of the BIN, its existing programs and its characteristics.
- ❖ Lay out the policy objectives for the existing program.
- ❖ Provide a fiscal context for understanding the BIN.
- ❖ Identify policy alternatives and goals.
- ❖ Make recommendations.



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BIN Overview

- ❖ Discusses the characteristics of each innovation center.
- ❖ Outlines programs and services associated with the BIN.
- ❖ Provides addendum with a spreadsheet of all BIN companies (All data current as of March 1, 2012).



BIN Overview

Location	Year Established	# of Companies	FTE's at Program Admittance	FTE's at Present Time	Average Length of Time Current Companies Have Been in the BIN
Shady Grove	1999	44	66	165	3.41 years
Silver Spring	2004	23	104	151	3.31 years
Wheaton	2006	21	45	58	4.01 years
Rockville	2007	23	59	155	2.96 years
Germantown	2008	29	98	132	2.60 years

TABLE 1: Summary of Number of BIN Companies, FTES and Average Time in BIN, March 1, 2012

BIN Overview

Location	Biotechnology	Information Technology	Consulting/Services	Green Technology
Germantown	15	9	5	0
Rockville	5	13	4	1
Shady Grove	35	6	2	1
Silver Spring	2	10	10	1
Wheaton	0	2	19	0
TOTAL	57	40	40	3

TABLE 2: Summary of BIN Tenants by Industry Type

BIN Overview

Facility	Rental Income @ 95% Occupancy	Gross Area (Sq. Ft.)	Net Leasable Area (Sq. Ft.)	Average Income Per Leasable Sq. Ft.
Shady Grove	\$1,314,004	60,000	33,680	\$39.01
Silver Spring	\$ 292,618	21,000	9,920	\$29.50
Wheaton	\$ 166,268	12,000	5,623	\$29.57
Rockville	\$ 427,331	22,000	13,339	\$32.04
Germantown	\$ 652,073	33,000	17,513	\$37.23

TABLE 3: Summary of Leasable Area, Projected Rental Income and Average Income Per Square Foot

BIN Policy

- ❖ Montgomery County pursued an incubator approach as a way to grow technology based companies and jobs organically.
- ❖ During the more than 15 year span of the BIN, the primary objective has been to provide ready access to space for emerging technology firms with flexible terms as it assumed that this will spur on job creation.



Policy Considerations: Why is Policy Important?

- ❖ Policy determines how success is measured.
- ❖ Policy determines how funding is provided.
- ❖ Policy determines programs and activities.
- ❖ Policy provides cover.
- ❖ Policy determines support.



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Fiscal Context

Facility	Rental Income @ 95% Occupancy	Operating Grant	Operating Expenses	Debt Service/Lease Payments	Personnel
Shady Grove	\$1,314,004	\$ 200,000	\$ 958,504	\$ 440,000	\$ 58,692
Silver Spring	\$ 292,618	\$ 25,000	\$ 301,579	\$ 0	\$ 56,036
Wheaton	\$ 166,268	\$ 280,000	\$ 116,776	\$ 299,594	\$ 56,036
Rockville	\$ 427,331	\$ 610,000	\$ 586,303	\$ 410,000	\$ 58,692
Germantown	\$ 652,073	\$ 442,000	\$ 310,698	\$ 634,821	\$128,710
Total	\$2,852,294	\$1,557,000	\$2,273,860	\$1,784,415	\$358,166

TABLE 11: BIN Income and Expenses Across Facilities

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Policy Alternatives

- ❖ **Alternative 1—Industry Specific Innovation Centers**
 - Policy Goal: To achieve strategic company creation and job growth in specific industry sectors that will be beneficial to Montgomery County's economic growth and expansion.
- ❖ **Alternative 2—Accelerator**
 - Policy Goal: To cultivate and identify early stage companies with high growth potential and entrepreneurs that would benefit from rigorous guidance, seed funding and space to create a strong entrepreneurial environment and cultivate capital partners.
- ❖ **Alternative 3—Venture-based Public/Private Innovation Center(s)**
 - Policy Goal: To create and grow companies that are able to attract funding by establishing public/private partnerships to provide more rigorous assessment of program applicants, establish venture capital relationships with firms entering the Innovation Centers, provide more industry specific management and implement industry best practices.

Policy Alternatives

- ❖ **Alternative 4—Federal and Academic Partnering with Innovation Centers**
 - Policy Goal: To leverage Montgomery County’s BIN to accelerate technology transfer and commercialization efforts from local federal and academic research assets in order to identify and develop new companies and products based on the ongoing research being undertaken in these institutions.
- ❖ **Alternative 5—Refine Existing BIN**
 - Policy Goal: To build upon the success of providing low-cost, flexible space for emerging technology and life science companies by providing more diligence, guidance and management milestones in order to improve program efficiencies and foster a higher graduation rate.

General Recommendations

- 1) Establish a clear policy objective(s) to establish measureable outcomes and provide benchmarks for success.
- 2) Implement a clear, consistent and regular mechanism for tracking out-come measures and participating company data.
- 3) Focus BIN activities on industries where Montgomery County can achieve a competitive advantage, create jobs with salaries sufficient to allow employees of BIN companies to reside in Montgomery County and drive economic growth.



General Recommendations

- 4) Develop programming that is tailored to the specific activities/requirements of each Innovation Center.
- 5) Provide resources for Innovation Center tenants to address ongoing resource requirements in addition to providing access to space.
- 6) Proactively develop milestones for participant companies and more defined graduation criteria to increase likelihood of moving companies into locally owned commercial real estate.



General Recommendations

- 7) Develop a 'pipeline' of candidate companies to move into the BIN as firms either graduate, fail to meet their established milestones, or new facilities come on line.
- 8) Develop a detailed recommendation of staffing requirements to meet new programmatic needs or modifications.
- 9) Explore alternatives for reducing debt service associated with the BIN's capital expenditures.

Specific Recommendations

- 1) Restructure the existing BIN program to provide additional funding for new or ongoing programmatic efforts.
- 2) Establish a specific industry focus for each Innovation Center.
- 3) Establish formal commercialization relationships and strategies with key academic and federal research partners.
- 4) Establish an accelerator.



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Next Steps

- ❖ Develop a draft of BIN goals and a mission statement for the BIN.
- ❖ Work with DED staff to develop a draft strategic plan “straw man” for the BIN incorporating policy and programmatic objectives identified in the Report.
- ❖ Meet with key executive branch representatives, if appropriate, to present the draft proposal.
- ❖ Work with DED and BIN staff to implement program participant tracking using agreed upon metrics to support and reflect program objectives.
- ❖ Present Report and draft proposal to PHED Committee.
- ❖ Meet with other interested Councilmembers.
- ❖ Present report and proposal to other interested groups (i.e. Montgomery County Chamber, MBDC, others).

