



Hearing Testimony
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US Department of Treasury

Proposed Regulations on Internal Revenue Code Section 409A
Application to Nonqualified Deferred Compensation Plans

Private Company Stock Options Valuation Reform

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Good Morning. My name is Larry Tamarkin. I am the President and Chief Executive Officer of CytImmune Sciences Inc. CytImmune is a small privately-held biotech company in the field of Oncology. We specialize in the utilization of colloidal gold tumor-targeting nanotechnology that focuses on the next generation of anti-cancer therapies.

On behalf of CytImmune and the Biotechnology Industry Organization (BIO)¹, we appreciate this opportunity to testify today about our concerns over the proposed regulations under the Internal Revenue Code (IRC) Section 409A, and more specifically, regarding the valuation of stock options for private companies.

CytImmune is a small independently owned private company formed in 1988 with a focus on the development of clinical diagnostic tools for monitoring immune systems. In 1996, we restructured CytImmune's focus into a bio-therapeutic company using colloidal gold nanoparticles to target drug delivery of cancer therapies. All of our research and development are home grown with committed investors, management, and staff who worked together throughout the years to realize our current status as one of the innovators in the field, making an impact on medicine and the quality of life for millions of cancer patients in the United States.

¹ BIO represents more than 1,100 biotechnology companies, academic institutions, state biotechnology centers and related organizations in 50 U.S. states and 31 other nations. Majority of BIO member companies are small, private, research- and- development oriented companies that are eager to attract scientific talent, investment, and corporate partners to grow into the next generation of Fortune 500 firms.

As creators of new therapy technologies, risk is high for the investors, management, and the employees in our industry. Although CytImmune is able to generate enough revenues to sustain itself, we are heavily reliant on federal grants and private equity investors to further develop our cutting edge technologies. Given the high risks, stock options have provided the needed incentive to attract the best talent and maintain the commitment of our employees, critical to CytImmune's success. In fact, we currently provide stock options to all of our employees and during the early years, stock options were provided in lieu of high salaries, 401 (k) company matches, and pension plans. Given our situation, we fear that without the ability to maintain such incentive plans, we will not be able to maintain the workforce necessary to remain competitive.

The implications of section 409A, which imposes income tax liability and penalties on the employees who presumably receive below fair market value stock options, will have a negative impact on the industry's ability to innovate and invest in the future, if not implemented correctly.

To that end, I would like to discuss the need for **Clarity and Certainty** in private company stock option valuation standards in the current proposed rules and provide CytImmune's perspective on their impact.

1) The rules should provide, through examples, that a company's financial official or its board of directors qualify as having "significant knowledge and experience" to do the valuations. Given the event-driven nature of the biotech industry and the huge volatility in the industry's external valuation models, it is critical that the fair market valuations are performed by those who have the requisite knowledge and experience with the industry and the company and by those who have the ability to weigh the factors that determine the fair market value of private company options.

Over the course of seventeen years in the biotechnology business, I have presented the company to many sophisticated investors such as venture capitalists. On numerous occasions, such investors have strongly disagreed with our valuation of the company. In particular, during our transition years from a diagnostic company to a therapeutic company, such potential investors have flatly said that they simply could not value the company at all. On the other hand, the management and our board always knew where we were going and the value of our technology.

2) The Rules should be further clarified to definitively state that no independent appraisal is required. Although the current rules provide a safe harbor from section 409A if a company has received an independent appraisal, given the volatility and the lack of external valuation standards for private company stock, I believe that company officials or the members of the board are in the best position to determine the fair market value of my common stock. Hiring an external appraiser would not only be costly, it may also cause more confusion since there are no existing guidelines on who may qualify as an "independent" appraiser and what valuation standards the appraiser should use.

Most critically, there have been times, as I have kept my dream alive, that money was very, very tight. During those times, I have had to ask my staff to sacrifice personally to keep the company going. In appreciation for their commitment, CytImmune has granted them stock options. If I

was required to seek an outside appraisal to set the value of those options, I would have been out of business, and my dream would have died. Now my company is poised to bring our revolutionary cancer drug into clinical testing. I assure you, this could not have happened if we had to bear any additional costs.

3) The proposed rules regarding the reasonable expectation of a change in control or public offering should be clarified. The presumption of reasonableness and good faith valuation may be subject to question only if a company has entered into a definitive agreement or filed its registration statement with the SEC at the time of the valuation or within 15 -30 days of the valuation.

Similar to many early stage biotech companies, we have had the opportunity to discuss partnering deals with mature biotech and pharmaceutical companies. Under the current rules, the impact of such a deal coming to fruition would trigger section 409A since it would create an expectation of change in control. Unfortunately, we have had situations where such partnering deals have fallen apart at the 11th hour, after all of the due diligence was already finalized. This demonstrates the volatility of such transactions in our industry. Therefore, a clear action triggering event such as a formal agreement or filing of a registration statement with the SEC, which is not withdrawn or cancelled, would provide much needed certainty and clarity on when the presumption of the valuation could be questioned.

4) The application of section 409A should be prospective and all options granted by a private company based on a good faith valuation prior to the final rule publication date should be exempted from 409A.

Given the volatility and the lack of industry standards on the valuation of private company stock and the lack of formal guidance on such valuations, it is critical that all options granted by a private company prior to the date of the final rule publication be exempted from section 409A. Having the rules apply retroactively, where no clear guidance was provided, would unfairly punish companies and employees who have played by the rules and have made good faith efforts to comply without settled guidance.

Thank you for the opportunity to testify today. I appreciate your consideration of the recommended changes and I look forward to your questions.