



July 21, 2020

The Honorable Nancy Pelosi
Speaker
U.S. House of Representatives
H-232, The Capitol
Washington, D.C. 20515

The Honorable Mitch McConnell
Majority Leader
United States Senate
S-230, The Capitol
Washington, D.C. 20510

The Honorable Kevin McCarthy
Minority Leader
U.S. House of Representatives
H-204, The Capitol
Washington, D.C. 20515

The Honorable Charles E. Schumer
Minority Leader
United States Senate
S-221, The Capitol
Washington, D.C. 20510

Dear Speaker Pelosi and Leaders McConnell, Schumer, and McCarthy:

Domestic startups are struggling because of the pandemic, seeing traditional sources of financing and paths to revenue dry up – but startups are also uniquely positioned to make outsized contributions to our economic recovery, and it is essential Congress prioritize supporting them now so they remain viable and can create and maintain the jobs of the future. We urge Congress to ensure the next pandemic relief package helps this great sector of the U.S. economy. As a non-profit research and advocacy organization focused on promoting pro-innovation policies that support the growth of tech startups, Engine is uniquely situated to propose and develop policy solutions to support the startup community. Indeed, since the start of the COVID-19 pandemic, we have been in regular contact with our network of startups across the country as they navigate this economic uncertainty, and their lessons learned should inform future efforts.

While startup founders routinely face hurdles accessing the capital and qualified talent they need to grow, these things are much more challenging amidst a pandemic. Seed funding has already started to decline significantly this year,¹ and especially for companies that do not have established relationships with VC investors, deals are expected to continue to slow.² Female- or minority-founded companies are expected to face even higher funding hurdles.³ Moreover, many startups may be shut out of current federal relief programs – either because they are ineligible or because the existing relief programs are not suited to their financial needs. While the Paycheck Protection Program provided some relief to startups, issues surrounding the program's requirements, forgiveness process, and the implementation of SBA's

¹ Angus Loten, *Startup Funding Dwindles Due to Coronavirus Slowdown*, Wall Street J. (Mar. 25, 2020), <https://www.wsj.com/articles/startup-funding-dwindles-due-to-coronavirus-slowdown-11585175702>.

² Sophia Kunthara, *Vcs Share Thoughts, Advice on State of the Market During COVID Restrictions*, Crunchbase News (Apr. 13, 2020), <https://news.crunchbase.com/news/vcs-share-thoughts-advice-on-state-of-the-market-during-covid-restrictions/>.

³ See, e.g., Eliza Haverstock, *Female Founders Face Funding Hurdles Amid the Pandemic*, PitchBook (May 8, 2020), <https://pitchbook.com/news/articles/female-founders-face-funding-hurdles-amid-the-pandemic>.

affiliation rule, made it difficult for some startups to avail themselves of the loan program. It is integral Congress pass further relief measures to support startups so that they are able to survive the current economic downturn, maintain their current teams, and can expand and hire rapidly after the pandemic. Engine urges you to consider the following measures that would help startups throughout this challenging time.

Equity Investment. Congress should explore government involvement in equity investment. One option, the New Business Preservation Act (S. 3515, H.R. 6403), would create a joint public-private program to invest in new startups. The legislation is designed to incentivize private investment, to promote diversity, and to be self-sustaining because the government's returns will be reinvested in future startups. Moreover, as introduced, the bill focuses on funding female- and minority-founded companies and companies located outside of major VC sectors. Congress could alternatively consider something like the U.K. Government's 'Future Fund' program, which launched in May.⁴ This convertible loan program provides assistance via loans that convert to equity if not repaid. Finally, Congress could explore direct federal equity investment into startups, similar to assistance provided to private companies in previous recessions.⁵ Following the crisis, companies can buy out the government's stake.

Forgivable Loans. Congress should explore fixes to the Paycheck Protection Program while the program is still in effect, including expanded and simplified forgiveness, and targeted changes to the affiliation rule. Congress should further use lessons learned from the PPP in implementing new loan forgiveness programs, including forgiveness targeted directly at startups. Many VC-backed startups were excluded from the PPP program due to the SBA's affiliation rule. This rule is highly fact- and context-specific and can be difficult to apply. For many startups it is difficult to even determine if the affiliation rule applies to their business. Congress could amend and simplify the rule to waive it for (many) VC-backed startups, for example by narrowing the definition of affiliates to those that own more than 50% of a company at present, or by enacting H.R. 6751, the Caring for Startup Employees Act. Congress should also consider expanding the scope of forgivable purposes for PPP loans. For many early-stage startups, traditional payroll expenses are a very limited portion of their operating expenses. While Congress decreased the percentage businesses need to spend on payroll to receive forgiveness, having this limit at all precludes some startups from applying for PPP loans. Moreover, Congress should consider expanding the scope of costs and payments that are eligible for forgiveness. Additional forgivable purposes could include payments to 1099 contractors and more of a company's basic operating costs, such as cloud-computing contracts, accounting and bookkeeping services, marketing expenses, or attorneys fees. Congress could also consider establishing a startup fund, so that early stage ventures are not competing with established businesses for much needed relief.

Tax Credits. Congress should consider enhancing tax credits and could build on existing models to create new or expand current programs. For example, a number of states have enacted angel investor tax credits, through which the state government subsidizes and encourages individual investors by offering tax breaks for qualifying investments.⁶ Congress could enact a federal counterpart, allowing individual investors a credit of 20-50% of the amount invested in startups (e.g., new investments in recently established businesses with a smaller number of employees). Opportunity Zones provide another

⁴ *Apply for the coronavirus Future Fund*, Her Majesty's Treasury (April 20, 2020), <https://www.gov.uk/guidance/future-fund>.

⁵ *See, e.g., TARP Programs*, U.S. Treasury (November 15, 2016), <https://www.treasury.gov/initiatives/financial-stability/TARP-Programs/Pages/default.aspx>.

⁶ *Everything You Need to Know About Angel Investor Tax Credits*, Startups.com (July 3, 2019), <https://www.startups.com/library/expert-advice/angel-investor-tax-credits>.

model. Congress created this program to provide tax benefits to individuals or corporations that invest in financially distressed regions.⁷ The program could be expanded to either cover more areas or create a similar program to provide tax benefits to investors who invest in qualified startup incubators or accelerators. Congress could also look to expand R&D tax credits, to offset income and payroll tax liability for small businesses who spend on R&D. And Congress could also expand the definition of what counts as R&D to include common software development activities like user experience (UX) research and design.

Grants. Finally, Engine urges Congress to examine the use of grant programs in providing relief to startups. Congress could allocate additional funding to existing programs like SBIR/STTR or the NSF's I-CORPS and Congress could instruct the agencies to speed or streamline the review and approval process. Applying for grants is usually a lengthy and time consuming process, in which applicants are often competing for set amounts of money. This may not be suited to the startup lifecycle, where companies often need more flexibility and (a potentially smaller amount of) capital quickly. Lastly, the government could also provide funding to incubators, accelerators, and innovation intermediaries who have more familiarity with the startup ecosystem in their communities and the individual needs of the companies they serve. Those entities could in turn award funding directly to startups in their networks.⁸

The ability of our nation's startups to survive and thrive after the pandemic is crucial for the economic recovery of the United States on the whole. While the Paycheck Protection Program represented a good first step, more targeted relief efforts are needed to support the U.S. startup ecosystem. Thank you for considering the proposals detailed above. Engine is happy to serve as a resource to Congressional leaders on the state of startups in the United States and to make recommendations as to how to support startups going forward.

Sincerely,

Engine

cc:

Senator Marco Rubio (R-FL), Chairman, Senate Committee on Small Business and Entrepreneurship

Senator Ben Cardin (D-MD), Ranking Member, Senate Committee on Small Business and Entrepreneurship

Senator Charles Grassley (R-IA), Chairman, Senate Committee on Finance

Senator Ron Wyden (D-OR), Ranking Member, Senate Committee on Finance

Senator Mike Crapo (R-ID), Chairman, Senate Committee on Banking, Housing and Urban Affairs

⁷ *Opportunity Zones Frequently Asked Questions*, IRS, <https://www.irs.gov/newsroom/opportunity-zones-frequently-asked-questions>.

⁸ *See, e.g.*, Engine Letter to Members of the Subcommittee on Innovation and Workforce Development of the House Committee on Small Business (Feb. 27, 2020), <https://static1.squarespace.com/static/571681753c44d835a440c8b5/t/5e582a468fa56521103d6600/1582836294242/House+Small+Business+Committee+Feb+27.pdf>.

Senator Sherrod Brown (D-OH), Ranking Member, Senate Committee on Banking, Housing, and Urban Affairs

Representative Nydia Velázquez (D-NY), Chairman, House Committee on Small Business

Representative Steve Chabot (R-OH), Ranking Member, House Committee on Small Business

Representative Maxine Waters (D-CA), Chairman, House Committee on Financial Services

Representative Patrick McHenry (R-NC), Ranking Member, House Committee on Financial Services

Representative Richard Neal (D-MA), Chairman, House Committee on Ways and Means

Representative Kevin Brady (R-TX), Ranking Member, House Committee on Ways and Means