July 17, 2024

The Honorable Sherrod Brown (D-OH)
Chairman
Committee on Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Tim Scott (R-SC)
Ranking Member
Committee on Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

cc: Members of the Senate Committee on Banking, Housing and Urban Affairs

Dear Chairman Brown, Ranking Member Scott, and Members of the Senate Banking Committee,

Thank you for your service to the nation at such a critical time in our nation's history. In particular, we thank you for your work to support America's entrepreneurs and startups. As leaders and supporters of the nation's innovation and entrepreneurship community of color, we write today regarding an issue critical to America's future as an innovation leader and to a stronger, more resilient, and inclusive U.S. economy. Specifically, we write to respectfully urge you to support two bipartisan bills – the **Community Development Investment Tax Credit Act** and **the Expanding American Entrepreneurship Act** – which will significantly improve access to capital for America's entrepreneurs of color by incentivizing increased private investment in CDFIs, and by expanding participation by accredited investors of color in funds that invest in new businesses.

A Stark Racial Divide Regarding Access to Capital

Launching a new business requires money. Entrepreneurs need money to pay expenses, develop their product or service idea, research the marketplace, develop and implement a strategy for identifying and targeting customers, and, hopefully, begin paying initial employees. Because such costs typically arrive long before the first dollar of revenue, capital and credit are the lifeblood of any new business.

Entrepreneurs of color have historically encountered profound race-based obstacles to securing the capital they need – and, unfortunately, such obstacles persist. Indeed, a 2022 analysis by the Joint Center for Political and Economic Studies found that six in ten business owners of color face major challenges securing capital. These findings echo the conclusions of a 2021 analysis by the Federal Reserve that found that entrepreneurs of color were less than half as likely as white entrepreneurs to be approved for bank loans – even when business owners of color have high credit scores compared to their white counterparts.

The Community Development Investment Tax Credit Act

Given such difficulties, an important alternative for new and small business owners of color are community development financial institutions. CDFIs are financial institutions that provide credit and other financial services to underserved markets and populations. CDFIs are funded by private investors and – once certified by the Treasury Department – become eligible for financial awards and other assistance from the CDFI Fund (administered by Treasury), which was created by the Riegle Community Development Regulatory Improvement Act of 1994 to promote economic development in distressed urban and rural communities. Since their establishment, CDFIs have become a vitally important source of capital for business owners of color and other underserved populations, with 1,271 certified CDFIs operating nationwide with total assets of $152 billion as of September 30, 2021.

On September 28, 2023, Senators Mark Warner (D-VA), Roger Wicker (R-MS), Chris Van Hollen (D-MD), Cindy Hyde-Smith (R-MS), Gary Peters (D-MI), and Jerry Moran (R-KS) re-introduced their bipartisan **Community Development Investment Tax Credit Act**. The legislation would create a new tax credit for private sector investors that make equity or equity equivalent investments in, or that provide long-term patient capital (i.e., loans with a minimum term of at least 10 years) to CDFIs. The bill would benefit CDFIs of all types – bank CDFIs, credit union CDFIs, venture capital CDFIs, and CDFI loan funds – and provide those institutions with the maximum flexibility and financial support they need to accelerate economic development and build wealth in low- and moderate-income communities.

The Expanding American Entrepreneurship Act

While many entrepreneurs rely on credit provided by banks or CDFIs, other entrepreneurs rely on investors who provide early-stage capital in exchange for an equity stake in the company. Unfortunately, at present the overwhelming share of equity capital goes to white entrepreneurs. Indeed, in recent years entrepreneurs of color have received less than 1 percent of total equity capital.

The inequitable distribution of equity capital is attributable to both explicit bias on the part of some investors, but also to unintentional bias. At present, most startup investors are white and male, with the predictable result that most of the startups in which they invest are launched by white male entrepreneurs – a phenomenon known as "homophily." In other words, who gets funding depends a great deal on who is doing the investing. Getting more capital to entrepreneurs of color, therefore, requires greater diversity among those who invest in startups. Indeed, research published in 2022 by Harvard entrepreneurship scholar Josh Lerner concluded that investment funds led by managers of color are three to four times more likely to invest in entrepreneurs of color.

On November 16, 2023, Senators Jerry Moran (R-KS), Mark Warner (D-VA), and Tim Scott (R-SC), introduced the **Expanding American Entrepreneurship Act**. The legislation would raise the cap on funds organized under a 2018 sub-category of section 3(c)(1) of the Investment Company Act of 1940 from $10 million to $50 million, and double the number of permitted investors from 250 to 500. Together, these changes will enable emerging fund managers to raise larger funds – a "bigger bat" to swing at the inequitable distribution of capital – and facilitate greater participation by accredited investors of color, diversifying the investor base and thereby directing more capital to entrepreneurs of color. Importantly, a higher number of permitted fund investors also means smaller average investments and smaller risk exposures, promoting investor protection.

We, the undersigned, are strongly of the view that the **Community Development Investment Tax Credit Act** and the **Expanding American Entrepreneurship Act** are vital to significantly expanding access to both debt and equity capital for the nation's entrepreneurs of color. We very much hope that you will support, and perhaps co-sponsor, both bills.

Again, thank you for your ongoing work on behalf of the nation's entrepreneurs of color.

Sincerely,

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