



May 8, 2019

The Honorable Maxine Waters
Chairwoman
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
4340 O'Neill House Office Building
Washington, D.C. 20515

Dear Chairwoman Waters and Ranking Member McHenry,

On behalf of our nation's venture capital (VC) investors and the entrepreneurs they support, I write to you regarding the *Corporate Transparency Act*. NVCA supports the goal of preventing exploitation of corporations and limited liability companies to shield criminal gains but has outstanding concerns over unintended consequences the language will have on the venture capital and startup community. We appreciate the willingness of the bill's sponsor and staff to consider the issues described below and look forward to continuing efforts to find solutions to these challenges.

Venture-backed startups generally receive equity investment from multiple venture capital partnerships during each stage of the company's growth, which in turn have their own investors, or "limited partners (LPs)." The required disclosure of "beneficial owners" with a 25 percent ownership interest could impose significant legal costs and compliance burdens on companies *at their earliest stages* to find and report information of each beneficial owner on an annual basis. Many young companies begin with investment from the friends and family members of the company founders before attracting angel investors (that sometimes act as a syndicate of many investors), then receive venture capital financing that often include more syndicates in multiple rounds. We urge changes to the *Corporate Transparency Act* that will ensure a minimum of disruption to this fragile process of company building that underpins U.S. economic growth and competitiveness. In fact, recent

studies have demonstrated that all net new job creation in the U.S. in the last 30 years has come from young companies as they scale and grow.¹

First, the *Corporate Transparency Act* should make clear that all investment funds which file Form ADVs with the Securities and Exchange Commission (SEC) are exempt from the disclosure requirements. The bill currently exempts a number of entities from being subject to reporting obligations, including investment advisors registered with the SEC. Dependent on an individual firm's investment activity, some venture capital firms are registered with the SEC as registered investment advisors (RIAs), while others are exempt reporting advisors (ERAs). Both RIAs and ERAs are required to report a variety of information to the SEC annually through Form ADV, including ownership details with a natural person's name, address, auditor name and location, broker name and location, custodian name and location, outside administrator name and location, information on assets, types of business activities, and criminal history. NVCA believes the legislation should provide clarity that this exemption applies to both RIAs and ERAs.

Second, language should be included to clarify that startups do not need to track down and disclose any LPs of an exempt investment fund. Interpretation of the legislation's definition of a "direct or indirect" beneficial owner of a company has the potential to apply to LPs of a venture fund, which would impose a complex burden on startups receiving venture funding. In fact, this requirement, which is subject to penalties and possible jail time, may be impossible for a company to meet since the limited partners of a VC fund are in most cases not known to the company. Limited partners of a venture capital fund do not make direct investments into venture-backed companies, gain access to sensitive information, or have any role in running the company, but do receive returns on their investment if the overall fund is successful. LPs include university endowments, foundations, pension funds, other venture capital funds, and family offices. The legislation should clearly establish that a company does not need to disclose the LPs of funds that invest in the company because 1) the LPs of venture funds are not generally public information, including to the startup; 2) the LP does not exercise control over a company, a qualification for how a beneficial owner is defined in the language; and 3) for funds which are considered exempt entities under the bill, their portfolio companies should not be required to find and disclose information that the investment fund is not even required to provide.

Third, additional measures to mitigate the regulatory impact of this bill on startups are needed. Startups are generally resource-strapped enterprises and frequently do not have in-house legal counsel to handle a regulation such as that proposed under the bill. When a startup raises capital in a fundraising round it is often for a specific purpose, like hiring new employees, conducting further research, or launching new product lines. The compliance cost created by *the Corporate Transparency Act* would draw resources away from those core economic activities.

¹ "The Importance of Startups in Job Creation and Job Destruction," Kauffman Foundation Research Series: Firm Foundation and Economic Growth," (July 2010), *available at* http://www.kauffman.org/~media/kauffman_org/research%20reports%20and%20covers/2010/07/firm_formation_importance_of_startups.pdf

This letter is intended to illustrate areas of concern with the legislation in advance of the committee's consideration. We appreciate the interest and willingness of the bill's sponsor and staff to address the specific provisions that could impact venture investors and their portfolio companies, and we look forward to working towards a resolution.

Sincerely,

A handwritten signature in black ink that reads "Bobby Franklin". The signature is written in a cursive, slightly slanted style.

Bobby Franklin
President and CEO