Testimony before the U.S. House Committee on Financial Services

"Innovation Revolution: How Technology is Shaping the Future of Finance"

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Chairman McHenry, Ranking Member Waters, and members of the Committee, thank you for the opportunity to appear before you today as an advocate for the innovation economy and the private capital that fuels it. My name is Henry Ward, and I am the CEO and co-founder of Carta—a privately held financial technology company that forms the infrastructure of the private capital ecosystem.

Startups, growth-stage companies, and the funds that back them create jobs, expand economic opportunity and growth, drive innovation, and ensure our nation's competitive advantage. Put simply, the private capital ecosystem is America's economic and innovation engine. Carta continues to invest in the infrastructure for private capital, and policy is part of that infrastructure. Our aim is to bolster private capital and broaden its impact to reach more investors, more entrepreneurs, more employees, more companies, and more communities.

We see these goals reflected in the work of Chairman McHenry, as well as many others on this Committee. Chairman McHenry has been a champion for the innovation ecosystem, working on a bipartisan basis to advance efforts to expand investor access, broaden capital formation for startups and growth-stage businesses, and help the U.S. maintain its competitive and innovative edge. But more than any specific legislative accomplishments, he has embraced the evolving technology landscape and adopted a policy approach designed to realize its opportunities. Chairman McHenry leaves a large legacy, but also a blueprint for how policymakers can operate to advance policies that unleash the potential of technology and private capital.

That approach is what continues to be required today. Bold, forward-thinking policy is crucial in the effort to keep America at the forefront of global innovation. My testimony today will highlight how private capital enables companies to launch and grow, how its unique model drives our country's growth, and how we can shape policy to broaden the reach of private capital to benefit more stakeholders.

Carta not only supports the private capital ecosystem but is itself a reflection of that journey and private capital's potential—funding an unproven concept to turn it into a company, and then helping that company succeed, scale, and mature.

Building Carta

Carta was born from the idea that it should be easier to track and manage equity in the private markets. By solving that problem, we could broaden the ownership economy and build the foundational infrastructure for expanded wealth and opportunity.

Unlike the public markets, there was no single source of truth in the private markets: Equity ownership was tracked through a fragmented network of spreadsheets and paper certificates. Carta digitized stock certificates and made it easier for companies to manage their equity, expand ownership, and help more of those owners—founders, employees, and investors—understand and maximize the value of that ownership.

Launching Carta and realizing this vision took capital. Like most founders, I was not able to self-finance this business and no bank would provide a business loan. I turned to venture capital—in exchange for equity in the company, investors gave me money.

We invested that capital to build. We built a capitalization table product and a related valuations business that streamlines how companies issue equity to employees and investors. We then turned to the investor segment and built a business that helps private funds with fund formation, administration, and valuations services.

This journey was not easy. Sixty investors told me "no." But we kept at it, and in January 2014, we opened our doors and onboarded our first customer. As an entrepreneur, you never forget the first time someone pays you for something you built. We earned $120 from our first customer in 2014. Today, Carta supports more than 40,000 private companies with over 2.4 million stakeholders and over $2.5 trillion in equity. We provide fund administration services for nearly 7,000 funds and fund vehicles, representing over $150 billion in assets under administration.

Today we are building toward our most ambitious goal: reinventing the infrastructure for private capital to unlock even greater potential in the private markets.

Carta is setting a new standard as the end-to-end platform connecting private capital—equity management and valuations for private companies, fund accounting and portfolio management for funds, and investor reporting and communications for limited partners. These tools bring transparency, accuracy, and timeliness to private markets, which often lack all three.

Private capital made this reimagining possible. And that is true at all stages of our lifecycle. Venture capital provided us the patient, risk-forward capital to launch our company and begin building. Venture capital invested more in Carta as we succeeded in the market and needed more capital to meet demand, grow the company, and tackle long-term, challenging problems. And these investors represented more than a check—they helped us shape strategy and products, introduced us to customers and partners, and helped raise more capital to scale the company. As we grew and matured, we expanded our investor base to include private equity funds that not only invested in us, but helped us refine our strategy, improve our operations, and mature as a company. This process fuels the innovation economy, and it made Carta possible.

Private capital drives America's innovation engine

Private capital—angel investors, venture capital, private equity, limited partners—serve as the lifeblood of startups and growth-stage companies at every stage of development.

Private capital provides patient, risk-forward funding to solve ambitious problems. This structure democratizes ingenuity, drives innovation and value creation, and promotes economic growth and job creation—all of which are critical to maintaining our nation's competitive advantage.

America's most transformative companies—Amazon, Apple, Genetech, Intel, LinkedIn, Moderna, Palantir, OpenAI, Stripe, and many that are not household names—would simply not exist without private capital. Venture-backed companies have disrupted almost every industry, changing how we learn, work, travel, heal, communicate, and so much more.

But private capital has done more than create successful companies—it has created jobs and economic opportunity. Startups and growth-stage companies backed by private capital are responsible for the bulk of net new jobs created in the United States. At its peak before the financial crisis, startups and growth-stage businesses accounted for approximately 3 million new jobs a year.[1] Since the

[1] Kauffman Foundation, The Importance of Startups in Job Creation and Job Destruction (July 2010), *available at* https://www.kauffman.org/wp-content/uploads/2019/12/firm_formation_importance_of_startups.pdf.

financial crisis, venture-backed companies still had employment growth 8% higher than traditional companies.[2] Private capital drives job creation.

It also drives economic value for its founders, investors, and employees. Of all initial public offerings since 1980, 40% were VC-backed companies; 13% were PE-backed companies.[3] Private capital is launching and helping companies grow into the public markets. Today, eight of the top ten publicly traded companies in the U.S. were venture-backed, accounting for more than $17.5 trillion in market capitalization and value to their investors and employee-owners.[4]

Private capital is America's innovation engine. America has driven every major technological innovation in the past 50 years and has started twice as many companies as the rest of the G7 countries combined.[5] This would not be possible without private capital. VC-backed public companies account for 46% of total R&D spending across governments, academic institutions, and private companies.[6] When you account for just commercial enterprises, companies that were initially backed by private capital and are either private or have gone public account for 92% of R&D investment.[7]

Right now, all across America, current and future founders are wrestling with the next idea that will be the defining product, market, or company in the next decade—if they can get the funding. That is the key to America's competitive advantage, and private capital makes it possible.

The capital structure to build

Like Carta in its early days, startups are often unable to access bank loans or traditional financing. Instead, they turn to friends and family, angel investors, or venture capital, which provide capital in exchange for equity ownership—and a piece of the uncapped potential. Venture capital democratizes ingenuity, enabling more people with ideas to pursue them. One no longer needs to be independently wealthy to finance their vision or bring their ideas into the existing, large incumbent companies at which they may work. Instead, venture capital broadens opportunity by empowering more entrepreneurs to transform ideas into reality.This is only possible with long-term capital that comes with greater risk tolerance.

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[2] *See* NVCA, Employment Dynamics at VC-Backed Companies in the United States: 1990 to 2020 (Feb. 2022), *available at* https://nvca.org/employment-dynamics/.
[3] Will Gornall and Ilya Strebulaev, The Economic Impact of Venture Capital: Evidence from Public Companies (June 2021), *available at* https://ssrn.com/abstract=2681841.
[4] *See* Stock Analysis, Biggest Companies by Market Cap (accessed Dec. 2, 2024), *available at* https://stockanalysis.com/list/biggest-companies/.
[5] Gornall and Strebulaev, *supra* note 3.
[6] *Id.*
[7] Kenan Institute of Private Enterprise, Enhancing the Resilience of Venture Capital (Apr. 10, 2024), *available at* https://kenaninstitute.unc.edu/kenan-insight/enhancing-the-resiliency-of-venture-capital/.

Launching a company that solves a complex problem, delivers a novel solution, or creates an entirely new market is hard. And it often has no roadmap. Founders and employees launch, learn, calibrate, build—they keep moving forward. Building something new often does not come with predictable quarterly results. Instead, founders seek some signal in the market that informs execution and sets them on a path toward longer-term innovation.

This is a key difference between private and public markets: Public markets index for predictable quarterly results, while private markets provide patient capital that allows the best ideas to take root and grow. Many companies may elect to stay private longer for a number of reasons—such as regulatory costs and burdens, or liquidity challenges with thinly traded securities—but the primary reason in my experience is that they are still building for long-term, rather than short-term, results.

Repeatable quarterly results and longer-term innovation are not mutually exclusive, but they can be hard to balance while a company is growing and maturing. Building is not a straight line and can be volatile. For instance, Carta spent more than three years building our fund administration business, during which time we have had to pivot and adapt. We adjusted, kept building, and today it is a key driver of our growth and a core part of Carta's future vision. Without patient, risk-forward capital, we could not have kept moving forward on this ambitious mission. This is what private capital and private markets facilitate.

Some startups and growth-stage companies will not just falter, but will fail. This is the reality of building to solve hard problems and shape the next chapter of American innovation. That is not a flaw; that is part of the dynamism of innovation. Our society should encourage such undertakings and our policy infrastructure should facilitate this ambition.

Private capital is at an inflection point—this is an opportunity

Private markets have grown exponentially over the past decade, and we expect this trend to continue.

Here's the problem: Without modernizing the policy infrastructure for private capital, the benefits will be limited to the fortunate few. And the gap will continue to widen as private markets continue to grow. The already-wealthy investor will be able to invest in the venture or private equity fund that is driving returns; the average American will not. The well-connected founder working in San Francisco or New

York will be able to raise capital; the budding entrepreneur in middle America with an idea and a dream, but no network, will struggle to fundraise.

We need to bolster private capital as the economic and innovation engine. But importantly, we need to broaden its reach.

The private capital landscape is evolving. This shift is driven by the increasing size and sophistication of the market, better technological infrastructure; industry and investor expectations; and increased policy scrutiny. These factors are changing how fund managers raise capital, identify and back entrepreneurs, and interact with their investors. This evolution is an opportunity. We can leverage this shift to align stakeholders on best practices and standards and modernize the infrastructure of private capital. This will bolster private markets, increase the trust in them, and help broaden the reach of private capital. Policy can help achieve this goal.

<u>Expand investor access to broaden its impact</u>: Private capital is a wealth and opportunity creator, offering diversification to its investors and delivering returns that historically outperform public markets.[8] But private market opportunities are largely reserved for institutional or wealthy investors. Policymakers should create more onramps for Americans to qualify as accredited investors and expand opportunities to invest in private fund vehicles.

The majority of Americans cannot invest in this country's most transformative and innovative companies because of regulatory constraints. Policymakers decided that private markets posed a greater risk than public markets because they are less transparent and less liquid. As a result, private market investment opportunities are largely limited to accredited investors—individuals who meet certain wealth- or income-based thresholds. The result: investor protection through investor preclusion.

The aim of investor protection is laudable, but the execution is problematic. And as companies stay private or wait longer in their lifecycle to go public, this means the bulk of Americans miss out on wealth creation and diversification in private markets.

The impact is not only on investors. Expanding investor access also increases the pool of capital that can fund founders. The primary avenue to raising capital requires entrepreneurs to have a pre-existing relationship with an investor. This rewards those who are in the club and excludes those who are not. Investor protection through preclusion will only lead to more inequality and widen the wealth

[8] *See* Cambridge Associates, US PE/VC Benchmark Commentary (Aug. 13, 2024), *available at* https://www.cambridgeassociates.com/wp-content/uploads/2024/08/2024-08-US-PE-VC-Benchmark-Commentary-CY2023_PUBLIC-1.pdf.

gap. Letting more people in the club enables more founders to raise capital and build.

Expanding private market investment opportunities should be done in a responsible manner that reflects unique but manageable risks posed by private capital. Expanding accredited investor onramps to reflect financial sophistication and enabling structured access to private market investments through professionally managed funds, where retail investors participate alongside and on the same terms as institutional investors, can democratize access while preserving important investor protections.

<u>Bolster fund managers to bolster the ecosystem</u>: To broaden the startup ecosystem, we must broaden the investor ecosystem beyond the traditional tech hubs. Regional growth and the diversification of private capital will be driven by emerging managers that identify and fund entrepreneurs across the country. Policy should lower barriers and help drive capital to this segment.

Emerging managers play a key role in supporting startups across the country that exist outside of traditional networks. Particularly at the earliest stages, many founders turn to their local communities for support to get their ideas off the ground. Emerging fund managers are more likely to participate in earlier rounds and invest in a more diverse pool of entrepreneurs located in their geographic area. These smaller funds also drive value—emerging managers often deliver superior returns compared to their larger counterparts.[9]

Despite their value, emerging managers' share of fundraising is declining, particularly as the economic environment has caused investors to revert to more established fund managers.

Policy should make it easier for emerging managers to raise and deploy funds. Adjusting venture capital fund parameters to permit fund-of-fund investments could help incentivize established funds to invest in emerging, regional funds, unlocking a significant source of capital for growing entrepreneurial ecosystems. Enabling secondary investments to be qualifying investments will facilitate greater value realization and recycle more funding into the system. Raising investor limits for venture capital funds could help smaller funds reach more investors with smaller check sizes, leading to the development of more localized networks.

[9] *See* Carta Policy Insights: Decoding the Data | Emerging venture capital managers (Sept. 10, 2024), *available at* https://carta.com/blog/policy-insights-09-2024/.

Modernize best practices and standards: Building a private capital regulatory framework that reflects the industry model, risk profile, and the needs of stakeholders in the ecosystem will unleash capital and broaden its impact.

Industry practices are changing. Part of this evolution includes investor access to information. Investors are demanding better, more timely information about the companies and funds in which they invest. And technology is enabling that. Carta helps investors better understand the market, manage their investments, and allocate capital. This will result in better decisions, better risk management, and better returns.

Appropriate, accurate information also helps private funds succeed by helping them allocate capital, support their portfolio companies, and communicate and deliver returns to their limited partners—the pension funds, charitable endowments, and others. If a fund knows how a company's fundraising levels and performance stack up against its peers, it can better support and guide the company to succeed. If a fund knows how other investors are valuing an illiquid holding, it can adjust to ensure it is reflecting the best thinking when communicating with its limited partners.

Industry is evolving to meet this opportunity, building best practices and standards with each new round raised and fund closed. Standardization can help lower barriers by creating clear industry-led expectations. This will reduce costs and friction points to form and operate funds, as well as facilitate practices around appropriate disclosures to the right stakeholders that lead to better risk-management, better capital allocation, and a more effective private capital ecosystem.

Policy can embrace this industry-led evolution. In so doing, it addresses the lack of transparency that some argue should restrict investor access. Modernizing such best practices can and should lead to broader investor access in this ecosystem, which will not only bolster this innovation and economic engine—but broaden it to more people, more companies, more communities.

That is the problem we are trying to solve. Modernizing the private capital infrastructure can help do it.

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Carta is proud to provide the infrastructure to support our innovators: the founders, investors, and employees who drive the innovation economy. Policy is part of that infrastructure—it affects nearly every aspect of the ecosystem and can drive innovation or bind its growth. Our goal is to ensure the private market infrastructure and regulatory framework helps expand access to capital, enables more investors to participate in private markets, and helps companies build along their lifecycle to prepare them to go public when they are ready. It is critical we have the right framework in place to ensure American innovation remains at the forefront, and that the American economy maintains its competitive edge.

I appreciate all the work that Congress is doing on that front, and we want to work with you to do that.

I look forward to your questions.