

A REVIEW OF THE SBIC PROGRAM

HEARING
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SUBCOMMITTEE ON ECONOMIC GROWTH,
TAX, AND CAPITAL ACCESS
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WEDNESDAY, OCTOBER 27, 2021

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
SUBCOMMITTEE ON ECONOMIC GROWTH,
TAX, AND CAPITAL ACCESS,
Washington, DC.

The Subcommittee met, pursuant to call, at 10:01 a.m., in Room 2360, Rayburn House Office Building, Hon. Sharice Davids [chairwoman of the Subcommittee] presiding.

Present: Representatives Davids, Newman, Bourdeaux, Chu, Mr. Kim of New Jersey, Meuser, Garbarino, and Van Duyne.

Chairwoman DAVIDS. All right. Good morning, everybody. I call this hearing to order.

Without objection, the Chair is authorized to declare a recess at any time.

I would like to begin by noting some important requirements. Let me begin by saying that the standing House and Committee rules and practice will continue to apply during hybrid proceedings. All Members are reminded that they are expected to adhere to these standing rules, including decorum.

House regulations require Members to be visible through a video connection throughout the proceeding, so please keep your cameras on. Also, please remember to remain muted until you are recognized to minimize background noise. If you have to participate in another proceeding, please exit this one and log back in later.

In the event a Member encounters technical issues that prevent them from being recognized for their questioning, I will move to the next available Member of the same party, and I will recognize that Member at the next appropriate time slot, provided that they have returned to the proceeding.

For those Members and staff physically present in the Committee room today, in accordance with the Attending Physician's most recent guidance, all Members and staff who attend this hybrid hearing in person will be required to wear masks in the hearing room. With that said, Members will be allowed to briefly remove their masks if they have been recognized to speak.

I will now begin with my opening statement.

Small businesses are the backbone of the American economy. They employ nearly half the private workforce and drive development through groundbreaking innovations. However, to be successful, they need capital.

Congress has long realized that funding on reasonable terms can be hard to come by for small firms. So, in 1958, Congress created

the Small Business Investment Company program at SBA, or the SBIC program. The goal was to bridge the gap between availability of venture capital and the needs of high-growth small businesses.

Under the SBIC program, SBA partners with private institutions to provide financing to small early-stage companies. Since its inception, the SBIC program has provided over \$100 billion in capital to entrepreneurs across the country. These funds have helped transform small firms into powerhouse job-creators. Early-stage small businesses that received SBIC investments include Apple, Costco, FedEx, and Intel.

In fiscal year 2020, SBICs financed 1,063 small businesses, with an average amount of just under \$2 million. These funds helped entrepreneurs acquire new companies, refinance debt, conduct R&D, purchase equipment, and generally operate their enterprise.

This is progress from the delays and mismanagement that has plagued the program in years past and our Committee has worked to correct. In fact, last year, the SBA licensed 26 new SBICs, which is up from 18. And, in 2021, they broke the record again, licensing 32 new SBICs.

Despite these successes, there are still issues with the program that the Committee must continue to address. One such problem is the lack of diversity both among investors and portfolio companies.

In 2007, the SBA acknowledged that women and minorities participated in the program at low rates. Today, the diversity numbers haven't budged. For example, in 2020, SBICs only made up around 5 percent of their total financing to minority-owned small businesses. The numbers were even worse for businesses owned by women and veterans.

After nearly 15 years of poor diversity metrics, we must get serious about increasing participation for women and minorities in the program.

So, today, I am looking forward to discussing ways that this Committee can further improve the SBIC program. I also look forward to learning from our witnesses who have extensive experience within this sector.

I would now like to yield to the Ranking Member, Mr. Meuser, for his opening statement.

Mr. MEUSER. Thank you, Chair Davids.

And thank you to all of our witnesses here today.

Mr. Mickelson, we appreciate you making the trip in from Iowa. Thank you very much.

So, Chairwoman Davids, thank you for calling this hearing to examine this important issue, the SBA's Small Business Investment Company program.

Before we delve too deeply into federal government investing programs, I want to touch on some of the realities on the ground that are facing small businesses nationwide, certainly in my district and throughout Pennsylvania.

Unfortunately, even with a high level of demand, it is a tough time for small business. After the devastating blows of COVID-19, particularly in certain States where arbitrary shutdowns were forced of various small businesses on a relatively random basis, the nation's job-creators are facing rising costs, spiking inflation, trou-

ble with finding workers, difficulty with keeping their shelves filled, for that matter.

With holidays approaching, these supply-chain issues are bottlenecking and potentially jeopardizing what could be a light at the end of the tunnel for many of these small businesses, which is certainly their hope.

Through all of this, the Biden administration and much of the Democrat leadership in the House do continue to threaten more government spending on the demand side of the equation, paid for by raising taxes on small businesses. This is a very, very self-defeating initiative.

In one of the latest regulations for small businesses, on September 9 of this year, the Biden administration announced a vaccine mandate for small businesses with 100 employees or more. There are many businesses with less employees than that that think, because the guidelines haven't been issued, that they will be affected as well. So it creates levels of uncertainty, which is the last thing a business wants.

To say the least, this announcement has left small business with numerous outstanding questions and concerns about retaining their employees, especially during such a severe labor crisis.

There is no doubt these are difficult times for small businesses. However, the nation's smallest firms are some of the most resilient. We don't have to look very far to find a small business that received a direct hit from COVID-19 but got back on their feet because of their perseverance and, yes, some government programs, such as the PPP. Many of these businesses did, in fact, reinvent themselves, while others simply were able to meet the demand where it was to be found.

We all, on this Committee, salute these businesses as they continue to work through the recovery. And they are what the recovery is all about.

In addition to the economic firestorms that small businesses are facing, they also struggle continuously with access to capital and financing opportunities to grow and expand their businesses. That is why the SBIC program has been an important resource in the Small Business Administration toolbox.

With the goal of injecting private equity into the small-business ecosystem, the SBIC program and other federal programs have the ability to reach down to businesses that might be geographically overlooked, including in my district in Pennsylvania.

Ensuring small businesses across our nation have access to these tools is important. Unfortunately, much of the investing is currently dedicated or siloed in certain areas of the country. Small businesses in rural areas often struggle with gaining access to capital. I am hoping that through this hearing we can develop pragmatic solutions to encourage more investment opportunities in worthy companies located particularly in rural America.

This Committee should work together through regular order, meaning examining an issue at a Committee hearing level, crafting legislation together and voting on it at the Committee level, and, if successful, moving it to the full House of Representatives. Unfortunately, that process was bypassed by my Democrat colleagues

when they drafted and took up the most recent budget reconciliation bill without Republican input.

I do look forward to discussing all of these issues this morning with our witnesses, as well as ensuring this program does reach its full potential. This program really should be studied and examined comprehensively. As Members of Congress and as Members of this Committee, it is important for us to exercise our oversight duty to explore how these programs are operating year-in and year-out.

The SBIC program has many layers, and it is worth examining thoroughly. I look forward to this conversation beyond this hearing. Again, I want to thank our witnesses for joining, and I yield back. Chairwoman DAVIDS. Thank you, Mr. Meuser.

The gentleman yields back.

I would like to take a moment to explain how the hearing will proceed. Each witness will have 5 minutes to provide a statement, and each Committee Member will have 5 minutes for questions. Please ensure that your microphone is on when you begin speaking and that you return to mute when you are finished.

With that, I would like to introduce—I will go through and introduce each of our witnesses, and then we will get started.

Our first witness is Ms. Holly Huels. Ms. Huels is the founder and managing partner of Holleway Capital Partners, which is an SBIC-licensed small-business investment company with offices in the district I represent, targeting small manufacturers in the greater Midwest and Southern U.S. Her insights will be critical for us to learn how SBA's SBIC program can play a role in helping finance the future of our domestic manufacturing base. She previously testified before the Committee in October of 2009.

So we are pleased to be able to hear from you again regarding SBIC program. Thank you for joining us today, Ms. Huels.

Our second witness is Ms. Carmen Palafox, a partner with MiLA Capital, a pre-seed and seed-stage investment fund based in Los Angeles. Thirty-two percent of MiLA Capital's portfolio companies are led by women CEOs, 58 percent are led by immigrants, and 42 percent address United Nations sustainable development goals. As a non-SBIC investment fund, she represents the type of investor who would be well-served by the Committee's recent efforts to expand licensing options within the SBIC program.

Ms. Palafox is also a founding board member of LatinxVC, a group of experienced investors working to engage and foster the Latinx venture capital ecosystem.

Thank you for joining us today, Ms. Palafox.

The Ranking Member, Mr. Meuser, is now going to introduce our third and final witness.

Mr. MEUSER. Thank you, Madam Chairwoman.

Our next witness is John Mickelson. Mr. Mickelson is a co-founder and managing partner of Midwest Growth Partners in West Des Moines, Iowa. Midwest Growth Partners is a private equity fund management firm that specializes in assisting and investing in underserved rural markets, including businesses in the food and agriculture, manufacturing, and distribution and logistics industries.

Mr. Mickelson has an extensive background in investing and finance and has an undergraduate degree, law degree, and MBA

from the University of Iowa and was also a Member of the school's Division I football team.

I don't know how they did that week, but maybe we will—or that year, but maybe we will get into it, while you were there.

Additionally, Mr. Mickelson is a former city councilman in West Des Moines, Iowa. I am looking to learning more about the strategic rural investing that Mr. Mickelson brings to his rural community.

I want to thank again all the witnesses for joining us today, for taking the time away from your busy schedules.

And I yield back.

Chairwoman DAVIDS. Thank you, Mr. Meuser.

And I appreciate all of you being here today.

And, with that, I will turn it over—Ms. Huels, you are recognized for 5 minutes for your testimony.

STATEMENTS OF HOLLY HUELS, FOUNDER AND MANAGING PARTNER, HOLLEWAY CAPITAL PARTNERS, LLC, ST. LOUIS, MO; CARMEN PALAFOX, PARTNER, MILA CAPITAL, CHATSWORTH, CA; AND JOHN MICKELSON, MANAGING PARTNER, MIDWEST GROWTH PARTNERS, WEST DES MOINES, IA

STATEMENT OF HOLLY HUELS

Ms. HUELS. Thank you, Subcommittee Chair Davids, Ranking Member Meuser, and Members of the Subcommittee.

My name is Holly Huels, founder and managing partner of Holleway Capital Partners. We are a small-business investment company headquartered in St. Louis, Missouri, with an office in Kansas City, Kansas. I am also a former Chairwoman of the Small Business Investor Alliance, a national organization that represents small-business funds and their investors in the lower-middle market.

Holleway Capital focuses on investing in small manufacturers and distributors throughout the Midwest, High Plains, Rocky Mountains, and Southern regions of the United States. Our investment strategy targets small businesses with annual sales between \$10 million and \$75 million.

Holleway specializes in working with small-business owners who want to sell, most commonly because they want to retire. We help these sellers align with buyer management teams to tailor an ownership transition and investment structure to each company's needs, market position, and future opportunity.

With Holleway as a partner, the business has the capital and management to update technology, purchase capital equipment, and expand into new markets. Without our capital, many of these businesses would simply shut down or have their operations consolidated into another company.

We are proud that we help these businesses remain independent, modernize, grow, and build a brighter future for their employees and communities. I have highlighted the success of two of our recent SBIC portfolio company investments in my written statement.

I am happy to report that the SBIC program is fulfilling its mission. As this Subcommittee knows, the program had several years

of suboptimal management, but, thanks in part to bipartisan congressional oversight, this SBIC program is helping more small businesses than ever before. On behalf of the SBICs across the nation, thank you for your critical and ongoing oversight role.

The SBIC program, administered by the U.S. Small Business Administration, is largely working well. But I would like to point out, as with any federal program, targeted improvements can help strengthen the program's ability to expand the benefits of free enterprise to more people and places.

First, SBA's SBIC information technology needs an investment upgrade. This is a \$34 billion program essentially running on Microsoft Office software. SBA's limited IT technology cripples productivity and creates unnecessary taxpayer risk. SBA has an incredible amount of data but cannot convert it into useful information to make informed decisions or to educate Congress.

Second, SBIC's primary regulators are called Operations Analysts, who are supposed to carry 10 to 12 SBIC funds per analyst. Staffing shortages currently have individual Analysts juggling as many as 50 SBICs. Regulated entities do not normally ask for more regulators, but we are. SBA needs the resources, both human and technological, to ensure SBA can run this successful program, provide necessary oversight, and remain responsive.

Last, small businesses need access to more equity capital because it is the most patient form of capital. It is also a critical resource for domestic small businesses to keep U.S. businesses competitive and to strengthen supply chains. If the SBA had the tools to allow SBIC equity investment, this would be an incredible advantage to small businesses experiencing high growth or surviving the bumps that they face.

I would also like to add that, since I last testified before this Committee in 2009, there has been a meaningful increase in women SBIC fund managers. Our trade association has 11 women on the board. And, while I was the first to Chair the board, several women have also served as Chair behind me, and several more are in line to serve as Chair in the years to come. Thanks to Congress, the SBIC program is serving as a great program for women fund managers to thrive.

Thank you for the opportunity to testify on the state of the SBIC program and offer recommendations to help maintain the program's critical role to provide much-needed capital to domestic small businesses.

I am happy to answer any questions you may have.

Chairwoman DAVIDS. Thank you, Ms. Huels.

And the Chair now recognizes Ms. Palafox for 5 minutes.

STATEMENT OF CARMEN PALAFOX

Ms. PALAFOX. I appreciate the opportunity to testify before you today.

I dedicate a lot of time and effort to expanding economic growth and capital access. I founded 2045 Ventures in 2020 to fill persistent gaps in the market for underrepresented founders and invest in sectors that will drive our future, including climate tech, fintech, and health tech.

I serve on the National Venture Capital Association Board of Directors, and I am a founding board Member of LatinxVC. As a founding board Member at LatinxVC, I focus on creating opportunities for emerging fund managers like me.

I was born and raised in San Diego, California, and moved to Los Angeles to study economics at the University of Southern California. I spent 15 years at Dimensional Fund Advisors, a global asset management firm, and gained deep appreciation for capital markets.

I left Dimensional in 2011 to pursue an executive MBA at Berkeley Haas. There, I was immersed in venture capital and startups and recognized the industry's increasing importance to our economy.

After graduating from Berkeley Haas in 2014, I wanted to launch a fund to invest in underrepresented founders, but I was too early. The ecosystem supporting women and underrepresented founders and emerging managers wasn't as robust as it is today.

So, instead, I joined two business partners and launched a venture capital fund, an accelerator, and innovation lab to invest in hardware technology startups. Our firm reached entrepreneurs in 70 countries and 33 States. We invested in 22 startups across sectors including ed tech, digital therapeutics, climate tech, and space tech. And some of our startups were beneficiaries of government grants and R&D scale-up manufacturing.

In October 2020, I launched 2045 Capital to fill gaps in the market. 2045's thesis is that diverse teams outperform, a view supported by data. The data shows that startups with ethnically diverse teams return 30 percent more capital to investors and startups with at least one female founder outperform all-male teams by 63 percent. And a quarter of all our U.S. science and technology firms are founded by immigrants. So 2045's objective is to invest in startups where at least one founder is a woman, an immigrant, or a founder of color.

So, in terms of the state of venture capital, it continues to be a powerful industry. The most recent third-quarter 2021 PitchBook and NVCA Venture Monitor reports that venture-capital-backed startups are at the top of the public markets. VC-backed IPOs accounted for more than two-thirds of the total U.S. listings year to date. In addition, 2021 is on a track record for another breaking year for venture investment, exit activity, and fundraising, with a total of \$238.7 billion.

The VC ecosystem is thriving for most, but not for women and minorities. This inequity is unsustainable when you consider the changing demographics of our nation. The Census predicts that by 2045 there won't be a racial majority in the United States, which is the case in five States today. Already, there isn't a racial majority for youth under 18, and 25 percent of Gen Z are Latinx.

In L.A., where I reside, 45 percent of the population is Latinx, but only 2 percent of VC capital investment goes to Black female founders and 3 percent to Latina founders. Furthermore, there is only less than 1 percent of female check-writers like myself in Los Angeles.

So programs such as SBIC can help women and underrepresented fund managers grow their presence, activate more invest-

ment into startups, and generate other benefits to society. Women and underrepresented managers are more than two times as likely to invest in female and underrepresented fund entrepreneurs—

Chairwoman DAVIDS. Thank you. Thank you, Ms. Palafox. We will return to you for questions after we yield to Mr. Mickelson for 5 minutes.

STATEMENT OF JOHN MICKELSON

Mr. MICKELSON. Thank you, Chairwoman and Ranking Member, and thank you, distinguished Members of the Subcommittee.

My name is John Mickelson, and I am the co-founder and managing partner of Midwest Growth Partners, located in West Des Moines, Iowa, with an additional office in Omaha, Nebraska. Midwest Growth Partners is a USDA-licensed Rural Business Investment Company, or an RBIC, and we raise dollars from the private sector to make succession planning and growth investments in food and agricultural, manufacturing, and distribution businesses in rural communities across the U.S.

Like the SBIC program, RBICs make investments in small businesses where institutional capital is scarce, particularly in non-coastal communities. Our investors include Members of the Farm Credit System, rural electric co-ops, ag trade organizations such as the Iowa Corn Growers, and commercial banks.

Starting with 7 after our first acquisition in 2014, Midwest Growth Partners' portfolio companies have over 2,600 employees today, employed in and often living in rural communities. These jobs all pay above the living wage, provide benefits, and generated more than \$7 million in federal, local, and state withholding taxes in 2020.

While we are proud of the impact these portfolio company jobs provide, we are just as proud knowing that many of the jobs provide off-farm income, allowing one spouse to remain farming while the other spouse secures benefits for the family.

Since inception, Midwest Growth Partners has grown the employment at its portfolio companies by 25 percent, on average, from the date of its original investment by making 19 investments in rural areas totaling more than \$100 million of much-needed private capital.

A real-life example of Midwest Growth Partners' capital at work is our investment in Fast Ag Solutions, located in Windom, Minnesota, population 4,400. Fast Ag manufacturers sprayers and liquid fertilizer applicators. Midwest Growth Partners partnered with the Fast Ag management team to purchase the company in the fall of 2020, and we have grown full-time employment from 52 to 73 since then.

This type of economic development in rural areas would not be possible without programs like the RBIC, but more can be done. Examples include: providing support for the Rural Capital Access Act, which would enable RBICs to utilize leftovers funds from the SBIC program; the creation of a Micro-SBIC license, which will create a more inclusive pool of talented entrepreneurs to invest in underserved communities; the creation of an SBIC working group to increase the number of SBIC applicants, specifically those located

in underserved communities and underlicensed States; and, finally, the creation of an SBA Office of Rural Affairs.

Unfortunately, all the success that has been made and the promise of the critical programs mentioned above could be muted because of current issues facing small businesses. PPP was a critical lifeline during the COVID-19 pandemic in 2020, but now businesses are facing a new set of challenges in 2021.

Our portfolio companies are facing 30- to 40-percent price increases in raw materials used to make goods, and that is if they can even secure the materials at all. Supply-chain constraints are having a direct impact on sales and profit margins, which constrict the ability to reinvest in our business and hire more employees.

The prospect of higher taxes of all forms is delaying business decisions necessary for long-term business planning. Midwest Growth Partners has experienced these challenges daily in the work we do in rural communities with small businesses.

On the passthrough income tax side, these proposals aren't impacting only billionaires but small-business owners, who, when faced with the prospect of a tax increase, will forego the hiring of additional workers, even one or two, or an investment in capital goods, such as something as simple as a forklift.

Possible increases of capital gains rates or to the 1202 Code have already created unnatural business outcomes, as owners and investors accelerate or indefinitely delay decisions related to their personal succession planning and growth investment strategy. Possible changes to the carried-interest model will disincentivize fund managers from making investments in all areas, including rural and other underserved communities.

Businesses in rural areas, and small businesses generally, already face a scarcity of capital access, negatively impacting the lives of millions of Americans. As we near the hopeful end of the COVID-19 pandemic, these businesses are optimistic to grow and create prosperity for their employees and communities.

Small and rural business owners and investors are used to facing headwinds. No day is ever easy. But adding additional regulatory and cost burdens is not in their best interest and definitely not in the best interest of the communities they operate in and the millions of employees who provide goods and services which make our country the land of opportunity.

Thank you, and I would welcome any questions that you have.

Chairwoman DAVIDS. Thank you, Mr. Mickelson.

I will now recognize myself for 5 minutes for my first question.

Ms. Huels, your fund invests primarily in manufacturing companies throughout the Midwest, including from one of your offices in Overland Park, Kansas, which is in the Third District.

This Committee passed a section of the Build Back—I can take my mask off. This Committee passed a section of the Build Back Better Act which included funds for the SBIC program to provide capital for underserved markets and small manufacturers.

Can you speak to the challenges that small manufacturers face in accessing capital and what more the SBIC program could be doing for these small businesses? I know you made a few recommendations related to information technology, the number of op-

erations analysts and equity investments, and I would be curious if you want to go into any more detail about that.

Ms. HUELS. Well, we invest primarily, as you said, in manufacturers and distributors in the middle part of the country, and we really see two broad trends.

Companies are coming back from COVID, and they are in need of growth capital to respond to the marketplace. And, as Mr. Mickelson said, there are challenges with regard to that with employees and supply chain.

But then there is also this acceleration of baby boomers who are late in their career and they are looking for what they are going to do with their business in order to retire.

So we are managing the portfolio companies that we have, as well as the substantial amount of need for capital, which is—you know, there is a very strong demand for capital in the market for both growth and for transition as people are trying to get in front of any kind of capital gains tax change that may happen in the future.

I hope that answers your question.

Chairwoman DAVIDS. Yeah.

And then I am curious—just a quick followup, and then I will move on to the next question—about the ways that—because the pandemic has exacerbated various issues, when we are thinking about some of the considerations, whether it is the capital gains, this sort of thing, how has the pandemic, like, either highlighted or maybe brought to the forefront the way that folks are thinking about that?

Ms. HUELS. Well, the pandemic—I agree with Mr. Mickelson, the PPP was an incredible resource to keep our companies and many, many companies viable through the pandemic. Now that they have survived that, the next big issue is the supply chain and lack of talent in the market, lack of employees in the marketplace.

So I would say probably the biggest struggle of most of our companies at this point—and we have companies in places like Wichita, Kansas, and Montgomery, Alabama. These are small-market-type businesses that are really struggling to, you know, fix supply-chain issues and find talent, employees.

Chairwoman DAVIDS. Okay. I appreciate that.

And then I guess my next question really has to do with—you know, we held a hearing in the last Congress to review the management of the SBIC program and had heard a lot of concerns about delayed processing and inefficiency. And I am curious if you have seen in the last 2 years any improvements or what your experience and what you have seen with that program.

Ms. HUELS. Yes, candidly, as you are aware, the program was struggling for several years. And I can say that the program is back. The management is excellent. The career folks at the SBA are excellent and do a fantastic job. And the management of SBA is doing—or the management of the OII and the SBIC program are in a great place now. Really happy with the improvements. So thank you.

Chairwoman DAVIDS. I am glad to hear that, and just would also encourage you and other folks who are participating in the SBIC program to, you know, keep the lines of communication open.

Let us know if you continue to see issues with the program, because we want to make sure it is running well.

And, with that, I will yield and recognize the Ranking Member, Mr. Meuser, for 5 minutes.

Mr. MEUSER. Thank you again, Chair Davids.

Thanks again to our witnesses.

So what I would like to try to get through in my 5 minutes here is, what can we do for you? And then let's talk about what you can do for us, as far as legislation or strengthening the SBA, the SBIC, the RBIC as well, overall.

So, Mr. Mickelson, I will start with you. You stated that there are various businesses that are underserved by institutional capital. You initially thought there would be 100 opportunities, and turned out there were many more that you are evaluating, 230 or so, and you might have the capacity that there may be far more than that.

So let's just talk about what—and Ms. Huels mentioned about the IT systems, which I know usually government agencies could use some real upgrades there.

So give me a little bit more on what you would need from the SBIC or, Mr. Mickelson, in your case, the RBIC that would be helpful to you—and, Ms. Huels, I am going to follow up with you, as well, on the same question—for the rural communities.

Mr. MICKELSON. Yeah, thank you, Ranking Member.

As you mentioned, when we got started in 2013, we told our investors that we hoped to see 100 opportunities a year, because they were concerned in rural areas there wouldn't be enough investment opportunities. In the first full year of operation, we saw over 230. And, for this year, 2021, we will evaluate over 800 investment opportunities.

And so there are a ton of wonderful businesses out in the rural areas. And because capital is concentrated in places other than those rural areas, it is a tremendous opportunity for us and other participants in the RBIC program. And I think there should be more funds. When we went through our licensing process for the RBIC in 2018, we were the fourth fund to fully go through the process, and now I believe there are 10, but there could be several more.

So one of the things that I think would be helpful for RBICs would be additional support. Similar to what we have heard on the SBA side, the USDA has wonderful people that are working there and overseeing the program. However, there are not many of them. And as I think there is more need for capital in these rural areas, I think there will need to be more oversight and funding for that program.

I mentioned in my remarks the Rural Capital Access Act. Right now, the RBIC program does not have access to leverage, like the SBIC program does. And if a fund like us had that tool, we could deploy additional capital into rural markets. And, as I have stated earlier, there is definitely a need for it, and there are not a lot of institutional capital providers like us that are focused on that area.

Mr. MEUSER. You mentioned to me earlier it is successful, it is working out well, your returns are pretty good—or very—you know,

what you anticipated, because you are a smart investor. And the SBIC—

Mr. MICKELSON. Thank you.

Mr. MEUSER. Well, yeah. The RBIC—you are as good as your last deal, as it says, right? The RBIC is a good partner for you. Do you focus on startups? I mean, the risk factor would be a little bit more there, but give me 20 seconds on how you relate with startups.

Mr. MICKELSON. Yeah, yeah, we don't. We focus on food and agriculture, manufacturing, and distribution. Part of that is our collective background as a management team, and then part of it is just the part of the country that we are in. And so, in these rural markets, you don't see a lot of startup tech funds like you would see on the coasts.

Mr. MEUSER. Okay.

Mr. MICKELSON. And so we are well-suited, uniquely qualified to chase the market that we chase. We would not be as well-suited to go after the technology companies.

Mr. MEUSER. Okay.

Ms. Huels, same question, and maybe you could answer something related to startups. We are looking at how we can expand, right, in a market-oriented, relatively risk-free manner that your organizations seek, right? So, please, Ms. Huels, if you would respond.

Ms. HUELS. Yeah, I think the SBA does a pretty good job with dispersion of SBICs and diversity, but it is always something that needs focus, needs improvement, as more fund managers gain experience within a fund or in some other job experience and to be able to bring that into a fund management.

I think there needs to be continued focused from the SBA to find small fund managers in geographies that are less served than the large markets. And I know it is definitely part of their criteria that they look at, as new fund managers are coming into the market. But supporting emerging fund managers, you know, is definitely—you know, there is a risk and a reward to that, and the SBA can manage that risk by allowing smaller, diverse management teams into the program and metering out the amount of leverage that they give those fund managers as they create a track record within the SBIC program.

You know, they have to be able to raise private capital, but to be able to supplement that with SBA debentures is a very powerful way to get capital to small markets, especially if the investor is in that small market. They have a tendency, as we do as well, to—

Mr. MEUSER. Excuse me. Thank you, Ms. Huels. We ran out of time, but we will—

Ms. HUELS. Okay. Sorry.

Mr. MEUSER.—cover this, perhaps, later.

Thank you, Madam Chair. I yield back.

Chairwoman DAVIDS. Thank you.

The gentleman yields back.

The Chair will now recognize Ms. Newman.

Ms. NEWMAN. Thank you, Madam Chair, and thank you, Ranking Member, for putting this on today.

So I would like to ask a couple questions. One is to Ms. Palafox and then to Ms. Huels.

So, Ms. Palafox, thank you so much for your data in your testimony. I would like to share one of your pieces of testimony, because it is very concerning to me, and I also experienced it.

I will raise the analysis from reports that 64 percent of VC firms in the U.S. with more than \$25 million in assets under management have zero—I will quote again—zero female check-writers and, of the women that became investors in 2020, only one self-reporting as African American and zero as Latinx.

So, quick aside: I twice have been involved in startups where, in fact, there was—on the folks that were assessing our businesses, there was not one female and not one person of color. And I pitched my business to over 75 VCs, PE, and early-stage investors and angels. So I can attest to that personally.

So my question for you is, what can Congress do to change that horrifying statistic?

Ms. PALAFOX. Thank you for that question. I represent 0.1 percent of the whole market as a Latina investor, and so I do recognize the issue. It is a big problem. And 2020, as you mentioned, was a backslide for many of us, as a lot of institutional investors fled to traditional names.

I do invest in startups. I invest early. I invest pre-revenue, pre-product. I am willing to take those risks. And I don't do so just geographically in California; I do that across the United States.

One of my recommendations for the program is that you focus on outcomes. So, if you want to move the needle in terms of having more representation of women and minorities, then you have to focus there and be intentional about it.

I would say that you also have to just take out a lot of the requirements that prevent, for example, solo managers for accessing these capital—for SBIC. There are many female solo managers. SheVC has done a great job of highlighting managers, female managers, that start their own funds independently. Often, these managers raise \$5 million to \$25 million in private capital. They have diverse backgrounds, coming from investment banking or, like me, asset management, and they invest with intention.

Ms. NEWMAN. That is fantastic.

Do you have any other ideas about how we can bring more not just female and people-of-color investors into the fold but how we can make that known to them?

So things like raising the cap on some of the funds, I think, helps a lot, but what do you think are some ways that we can work with this community to make sure that they have equal representation in the investment community and through the SBIC?

Ms. PALAFOX. Right. So, since 2015, there are many organizations that support female and underrepresented managers. I have named and listed many of them in my written testimony. These include All Raise, which is focused on female founders and funders; Women in VC, which was established in 2015; Transact, which is a group of female general partners established in 2018; LatinxVC; BLCK VC; and Venture Forward, which is a part of the NVCA.

Ms. NEWMAN. Outstanding. Thank you for your very helpful answer.

And then I will turn my attention to Ms. Huels.

A similar question to you, but I will focus it on your organization.

So, understanding you work directly with SBIC and can certainly—we know some of the things that we have to do, but what could your organization do to make sure that not only there are more investors that are women and people of color in your programs but also that women and people of color are recipients of your investments?

Ms. HUELS. Well, I have been active in the SBIC program for over 25 years, and when I first joined the SBIC program, I was with a different fund, and I am proud to say that I gained a lot of experience during my time with that fund. But I used that experience and relationships, and a former partner and I broke away to be able to form a women-owned SBIC, but we had to get that experience to get into the program. It is a long track—you know, it took a long time to get a track record.

So I think one thing that could be done is to have the SBA consider investors like myself but maybe with a slightly shorter track record to get more entrants into the program, people of color and women.

And I would say, what my fund specifically is doing——

Ms. NEWMAN. Thank you, Ms. Huels. I am so sorry.

Ms. HUELS. Okay, that is fine.

Ms. NEWMAN. I yield back.

Sorry, but thank you very much for your answer, Ms. Huels.

Ms. HUELS. No problem.

Chairwoman DAVIDS. Thank you.

The gentlelady yields back.

And the Chair now recognizes Rep. Garbarino from New York for 5 minutes.

Mr. GARBARINO. Thank you, Chairwoman, and thank you, Ranking Member, for hosting this hearing.

Thank you to the witnesses for being here.

My first question is for Ms. Huels.

I was reading through your testimony, and you state that your firm specializes in working with small-business owners that are interested in selling. Can you expand on this?

Ms. HUELS. Sure. Businesses go through a continuum. They start with Carmen and early-stage investing and getting a company started. And then, you know, we are focused on manufacturing and distribution companies; they go through a lifecycle of growth and meeting market demands. But, ultimately, an owner or founder or a couple of founders have to decide what they are going to do with that business at the end of their career, and that is really where we can step in.

That owner has a couple of choices. They can liquidate that investment and turn their life's work into cash by selling the assets. They could sell it to a corporate buyer, who may or may not leave the company in their current location; it may get absorbed into another facility. Or they can work with their management team to create a transition to keep the company in its current location, keep the employees, and find new markets to grow that business.

And that is really when Holleway steps in, to partner with those management teams to give the capital to the retiring owner and

allow, you know, growth in the business, purchase of capital equipment, and growth into new markets where they might not have been able to go with their former owner.

So there are needs for capital across the continuum. We, because of our background and experience, serve the later-stage-type businesses that are going through that kind of transition.

Mr. GARBARINO. That is fascinating. I appreciate your answer there.

And just turning to something else, you said you have been with SBIC or you have been part of the program for over 25 years now. How do you think it is running now compared to—you know, there have been some hiccups along the way, but, I mean, is it working well? What could we do better, if we are not doing something better?

Ms. HUELS. Well, I will just take the time to say that the career staff is excellent. They do a fantastic job working with the fund managers, licensing new funds. You know, the career staff does great.

There have been periods of time where leadership of the office has been fantastic, and then there have been times where it has been suboptimal, as I said. And, thankfully, right now we are in a period where the program is really running strong, I am happy to say.

Mr. GARBARINO. So is this something that we should just leave alone, since it is running well now, and just let it take its course?

Ms. HUELS. Well, new licensing is running well. There is definitely room for—a need for new or additional operations analysts. I think they are swamped. The number of new fund managers and just the staffing is short-staffed. I definitely think that is something that could be fixed.

As I said, the technology element is definitely something that needs some focus and investment. You know, the SBA has a lot of portfolio companies under their domain, and I think being able to gather data would, frankly, give folks like yourself more information about how many companies and how successful the program is. It is hard for them to gather that data using their current systems.

Mr. GARBARINO. I appreciate that.

I can testify, myself, to the staffing level. I had a breakfast—I think it is just short everywhere. I had a breakfast this morning with a bunch of equipment salesmen, and they were just saying, between the supply chain and staffing, you know, it is just very hard for them to grow. And they said, even if supply-chain problems didn't exist, they wouldn't have the staff to take care of it.

Are you hearing that from your small businesses? You discussed staffing, supply-chain issues, and, I guess, costs as well. And if those are problems, you know, would we want to add new taxes onto that now? I know there are discussions about possible new taxes coming on businesses. You know, would that add to part of the problem that we are seeing right now with some of the growth of small businesses?

Ms. HUELS. Certainly raising taxes discourages investment into long-term, illiquid investments, which is what we do—long-term, illiquid investments. And capital gains rates increasing could deter,

will deter, investors from investing in long-term asset classes like ours for sure.

Mr. GARBARINO. Yeah.

Ms. HUELS. And in terms of the employees, employees and supply chain are the two things we hear from our portfolio companies every day.

Mr. GARBARINO. I appreciate your answers.

And I only have 10 seconds left, so I yield back, Madam Chair.

Chairwoman DAVIDS. Thank you.

The gentleman yields back.

The Chair will now recognize Ms. Chu from California for 5 minutes.

Ms. CHU. Ms. Huels, thank you so much for mentioning my bipartisan legislation, the Investing in Main Street Act, which has been favorably reported by this Committee for the past three Congresses and has actually passed out of the House in past Congresses.

And what it does is increasing the amount of capital that could be invested in the SBICs, particularly from banks. Under current law, the Small Business Investment Act of 1958 prohibits SBICs from taking investments from banks that have over 5 percent of their capital invested in SBICs already.

But bank regulations already permit the exact same institutions to invest up to 15 percent of their capital and surplus into SBICs. So this bill would simply align the outdated small-business investing law with current banking law and unlock up to three times as much investment capital for SBICs at no additional cost.

So what impact would this policy change have on the SBIC program and institutions such as yours?

Ms. HUELS. Representative Chu, I agree with you, there is a regulatory mismatch between the banking regulations and the SBIC regulations. I think bringing them into parity would be supported and would definitely bring more capital into the market—it would provide clarity to investors of how much they can invest into SBIC funds, which would allow more capital to flow to fund managers, which would ultimately allow more capital to go to small business.

I think it is definitely a regulatory mismatch that should be fixed. Thank you for supporting it.

Ms. CHU. Thank you so much.

Ms. Palafox, your story is so impressive. And as a Representative of the Los Angeles area myself, I am so glad that you came before the Committee today to tell your story.

As you know, the SBIC program has historically struggled to reach underserved businesses and to license funds operated by women and people of color. CRS research finds that SBICs provide about 5 percent of their total funding to minority-owned businesses, about 3 percent to women-owned businesses, and less than 1 percent to veteran-owned small businesses.

These low numbers led SBA to have the Library of Congress research this issue, and they found that racially diverse SBICs make more investments in minority-led and minority-owned portfolio companies, as well as in women-led and women-owned businesses, than non-racially-diverse SBICs.

So, to address the lagging diversity in the SBIC program, the House Small Business Committee's section of the Build Back Better Act includes almost \$10 billion in investments in the SBIC program, largely to ensure that it reaches more underserved businesses.

It would establish a new Venture SBIC program to provide capital to underserved markets and small manufacturers, create an Emerging Managers Program to help less experienced fund managers get an SBA license, and implement a new MicroCap SBIC license subprogram to increase SBIC diversity.

So can you talk about the challenges that somebody from an underserved group would have to get this venture capital and how these particular kinds of programs in the Build Back Better Act could address this?

Ms. PALAFOX. Thank you for that question.

You know, Los Angeles is the third-largest tech ecosystem in the United States, but, as I mentioned, it is not working for women and underrepresented minorities, and that is because there is this funder-founder gap. We don't have enough women check-writers. We don't have enough minority check-writers.

And so we do need to act quickly. We need to issue licenses quickly, and we need to allocate the billions of dollars that you talk about. As I mentioned in my statement, \$238 billion was invested in venture capital year to date. That is just year to date.

So, in order to have meaningful progress, we need to move quickly. We need to work with organizations that are supporting women and emerging managers. There are so many out there now, today, that can be helpful in this process to reach these communities.

I, myself, am considered a first-time manager, but I have invested in over 25 startups at day one. These companies have gone on to raise over \$210 million and are doing meaningful work for our country.

Ms. CHU. Thank you.

I yield back.

Chairwoman DAVIDS. Thank you.

The gentlelady yields back.

The Chair will now recognize Rep. Van Duyne, the Ranking Member of the Subcommittee on Oversight, Investigations, and Regulations, for 5 minutes.

Ms. VAN DUYNE. Thank you very much. I really appreciate you having this hearing today.

I do have a question for Mr. John Mickelson.

First of all, I want to thank you for your work as a city council Member. I, too, served on city council for 6 years. I think you will agree it is one of the hardest jobs that we have had but also one of the most personal and meaningful. As a result, I am sure you had opportunities to talk to business owners and employees in your city to figure out what their needs are and can tell about that firsthand.

One of the SBIC program goals is to improve and stimulate the national economy and the small-business segment in particular. I would be remiss if, while discussing how to stimulate our economy, we didn't touch on the current economic situation for small businesses.

Record inflation and hiring shortages are severely impacting our small businesses. NFIB reports that 51 percent of small businesses have employment openings that they can't fill and 90 percent of small businesses are experiencing supply-chain troubles.

And this doesn't make light of the fact that small businesses are also awaiting potential tax hikes and increased regulatory burdens that this administration is pushing. So, when considering the success of small businesses, do you find that this current business environment, primarily due to an overactive administration, is more challenging than it needs to be?

Mr. MICKELSON. Thank you, Congresswoman, for the question. And thank you for your comments on the city council. It was a good, wonderful time in my life.

Yeah, there is no question that the current challenges facing small businesses—as I mentioned in my remarks, inflation, a hiring shortage, the potential for a vaccine mandate which will impact companies with more than 100 employees, and then uncertainty around tax, both for passthrough businesses but then also on the capital gains side—is really just creating uncertainty. And uncertainty is bad when planning a business.

So, this time of year, all of our businesses are going through a budget process to plan for 2022 and what kind of investments they can make in people and in capital goods. And because so many of these things are sort of in flux, it is very hard to plan. And that makes it very inefficient to run and operate a business.

Ms. VAN DUYNE. Okay. I appreciate that.

I have spoken to businesses of all sizes, and a common concern that they have shared with me is the upcoming vaccine mandates that are being imposed by the Biden administration.

While we are experiencing, as I just mentioned the numbers, a significant labor crisis, how do you think that the vaccine mandate will affect small businesses' ability to be able to manage their current staff, to hire, and to grow?

Mr. MICKELSON. Yeah. Thank you for the question.

You know, in rural communities and predominantly blue-collar environments, there is a lot of hesitancy as it relates to getting the vaccine. And, whether that is right or wrong, that is just the facts that we are dealing with today.

And I know several business owners, including our portfolio companies, that are concerned, should this pass—I think it was announced on September 9, and we haven't been given a lot of guidance since then—but, should this become law, they will have up to 50 percent of their workforce leave and go find jobs elsewhere.

And so the business owners are concerned that the obligations that they have made to fulfill contracts for things that they have agreed to build or to do in their business for customers they won't be able to do, because they just simply won't have the people there to do that.

So, at a minimum, providing some further information, some guidance for businesses, would be extremely helpful for small businesses.

Ms. VAN DUYNE. In representing a rural district, I have had a lot of opportunities to speak with folks who actually are in the shipping area. And I am assuming a lot of your small businesses

are relying on that. Part of this vaccine mandate is going to definitely affect pilots of shipping for supplies.

So, given the fact that we already have such a supply-chain shortage now and issues with that, do you see the vaccine mandate being able to hurt small businesses, specifically in the rural areas, because of the hiccup in transportation?

Mr. MICKELSON. Yes. The definition of “social distancing” would be being by yourself in a semi truck, hauling goods and services—or hauling goods for customers.

And so I know that many of these trucking companies have more than 100 drivers and they have a chronic shortage of drivers. And so, to the extent that they lose, you know, up to half of those drivers overnight, it will have catastrophic impacts on getting raw materials to manufacturers, like the ones that we are invested in, to go and build further products.

Ms. VAN DUYNE. I appreciate that. And, actually, I think it was UPS, as well, that said they were going to have a dramatic impact on the commerce in the United States if this mandate were to go through as well.

I appreciate your time.

And I yield back.

Chairwoman DAVIDS. Thank you.

The Chair now recognizes Rep. Bourdeaux for 5 minutes.

Ms. BOURDEAUX. Thank you, Chairwoman Davids and Ranking Member Meuser.

In this committee, we frequently hear from small-business owners and advocates dealing with issues of accessing capital. Access to capital is very much at the top of the list in terms of issues that I hear about when I talk to small businesses in my community. And the SBIC program really does offer a vital source of capital for these folks. In Georgia alone, SBICs have invested more than \$1.7 billion in 332 small businesses since 2011.

Just a couple of questions.

Ms. Huels, I noticed that you got cut off when you were answering Congresswoman Newman’s questions about getting more women involved in the SBIC program, and would love to take a minute, just if you could flesh out some of your ideas there about how to do that.

Ms. HUELS. Thank you for circling back. I appreciate that.

What I was really just going to say is, we, as a fund, have taken the challenge of getting more women into the program very personally. My partner and I have been—or, we have two analysts—we are a firm of five people, and myself and our associate and senior associate are all women. We are trying to, you know, use our little corner of the world to try to support more women coming into the program and getting experience.

As a check-writer, as Carmen has said, as a check-writer in the program and becoming a qualified investor, you need to get experience hopefully early in your career. So we have done that by using the two positions that we have, and both of them are women, and we are really happy about that.

Ms. BOURDEAUX. Okay.

You mentioned something about, you know, should we think about adjusting the standards; we want to make sure that women

are in there, that they are qualified, though, when they do it; and, you know, shortening the time where, you know, women are, you know, learning the ropes, as it were.

Is there anything like that that we should just think about?

Ms. HUELS. Well, there are qualified women out there who may not have exact SBIC experience, and I think and I am hopeful that the SBA takes that other experience into account as they are looking at these emerging managers.

So to give someone a license either with no leverage or limited leverage as they learn the program, make investments, and build a track record, I think, is definitely something the SBA could look at or look at further, if they are not already, to be able to manage taxpayer risk by metering leverage, the amount of leverage, to the smaller or emerging fund managers who may not have quite as much experience.

Ms. BOURDEAUX. Okay. Thank you so much on that.

And then one other issue really of interest to me is around manufacturers—

[Audio interruption.]

Sorry about that. We have all sorts of internet problems. I think I froze there for a second.

Interested in the manufacturers. And you said about a third of all program funds are invest in small manufacturers.

What makes the SBIC program well-suited to investing in manufacturing firms? And what can we do to make it more attractive to continue and build those investments in the small manufacturers?

Ms. HUELS. Did you direct that question toward me? I am sorry.

Ms. BOURDEAUX. That was—yes, yes.

Ms. HUELS. Oh, okay.

Ms. BOURDEAUX. Sorry. It might have gotten lost in the gap.

Ms. HUELS. No, that is okay.

Yep, manufacturing companies are the heart of what we—our entire investment thesis and strategy is around manufacturers and distributors, in the middle part of the country specifically. We are, as I mentioned, going to places like Wichita and Montgomery, Alabama, and other, sort of, off-market places, and there are a lot of really great manufacturing firms that are in this transition phase that I have mentioned a couple of times.

And the way to support them with growth and capital is to allow them to transition away from a retiring owner, give that person the value of the business, but backing the management team to continue to operate in the locality that they are and grow with additional capital to support the additional markets. It is a really important source of capital that many SBIC fund managers—

But the definition of—we are a debenture fund, so we need interest income, so these need to be cash-flowing, typically later-stage business that have cash flow available to pay interest so that we can pay the SBA debentures. So a more equity-oriented investment needs a different kind of a tool than what the SBA structure is currently—debenture program is currently structured to support.

Ms. BOURDEAUX. And what would be a more equity-oriented-type program? What would that look like?

Ms. HUELS. There are several equity-oriented programs on the, you know, docket that are being looked at that would use the SBIC

infrastructure to make longer-term investments in companies that may not yet have the cash flow available to serve this interest but take a more equity-oriented longer term to give companies time to create cash flow.

Ms. BOURDEAUX. Okay. Got it. Thank you so much.

And I yield back.

Chairwoman DAVIDS. Thank you.

The gentlewoman yields back.

Well, first of all, I want to say thank you to all of our witnesses again for being here today. Your testimony is certainly critical as our committee takes steps to enhance not just the SBIC program but other areas where we can increase access to capital, particularly in rural areas, as we heard today, and then, of course, build on years of success that the SBIC program has seen.

This program is essential. It is providing billions of dollars to small businesses seeking investment capital, facilitating economic growth, and helping to create jobs in that process. And it is why we have to address the program's shortcomings and ensure that it is operating as efficiently as possible as well.

You know, by making critical reforms, we can expand licensing options to investors funding the 21st-century entrepreneurs, facilitating more small-business growth. And I am definitely looking forward to collaborating with Committee Members to reach this goal.

And, with that said, I would ask unanimous consent that Members have 5 legislative days to submit statements and supporting materials for the record.

Without objection, so ordered.

And if there is no further business to come before the committee, we are adjourned. Thank you.

[Whereupon, at 11:08 a.m., the Subcommittee was adjourned.]

A P P E N D I X

U.S. House Small Business Committee

Subcommittee on Economic Growth, Tax, and Capital Access

Review of the Small Business Investment Company Program

Statement of

**Hollis A. Huels, Founder and Managing Partner
Holleway Capital Partners**

October 27, 2021

Subcommittee Chair Davids, Ranking Member Meuser, and members of the Subcommittee, thank you for inviting me to testify on behalf of the Small Business Investor Alliance (“SBIA”) at this oversight hearing. I am Holly Huels, Founder and Managing Partner at Holleway Capital Partners, a Small Business Investment Company —or SBIC— headquartered in St. Louis, Missouri, with an office in Kansas City, Kansas. I am also a former Chair of the SBIA, the national organization that represents small business funds and their investors in the lower middle market.

Holleway Capital focuses on investing in small manufacturers, and distributors throughout the Midwest, High Plains, Rocky Mountains and Southern regions of the United States. Our investment strategy targets small businesses with annual sales between \$10 million to \$75 million, and annual earnings before interest payments, taxes, depreciation and amortization, or “EBITDA” of between \$2 million to \$10 million. Holleway specializes in working with business owners who want to sell. We help these small business sellers align with buyer management teams to tailor an ownership transition and investment structure to each company’s needs, market position, and future opportunity. With Holleway’s investment, these small businesses are able to modernize, grow, and build a brighter future for their employees and communities.

I am happy to report that the SBIC program is fulfilling its mission. As this Subcommittee knows, the program had several years of suboptimal management, but thanks, in part, to bipartisan congressional oversight and a new Associate Administrator, the SBIC program is helping more small businesses than ever before.

On behalf of SBIA’s membership, thank you for your critical role.

I hope my testimony today demonstrates that the SBIC program, administered by the U.S. Small Business Administration (“SBA”), is largely working well. But I would also point out, as with any federal program, targeted improvements can help strengthen the program’s ability to expand the benefits of free enterprise to more people and places. Three potential areas include:

- Information Technology (IT) is in need of investment. This is a \$34 Billion program running on Microsoft Office (Excel and Access).
- SBICs’ primary regulators are called “operations analysts”. These analysts are supposed to handle 10-12 SBIC funds. Staffing shortages currently have analysts juggling as many as 50 SBICs.
- Small businesses need access to more of the most patient form of capital – equity. Access to equity capital is critical for domestic small businesses to keep the U.S. competitive and strengthen supply chains.

An SBIC Success Story - Holleway Capital

SBICs are an American success story and example of a successful federal public policy that aligns the power of private markets with the public interest of job creation and economic growth.¹

The principals managing Holleway have more than 60 years of combined experience investing in and working with private companies. Over the last 20 years Holleway's principals have partnered with family and entrepreneurial-owned companies, completing over 40 transactions all through the SBIC program. Holleway prefers investments in product-oriented small businesses that manufacture niche, proprietary industrial products or provide value-added distribution. Our team members bring strategic experience and creative thinking, cultivated from years of working with and advising leaders to solve the many challenges entrepreneurs face while growing their companies.

Congress declared in its original authorizing legislation that the SBIC program should "stimulate and supplement the flow of private equity capital and long-term loan funds which small business concerns need for the sound financing of their business operations" while also stimulating the national economy and growth.² Holleway Capital is a new SBIC fund, and we have made some exciting investments that have indeed helped stimulate job and economic growth and support the initial mission of the SBIC program.

Let me highlight a couple of investments we've made in the last three months:

- **Panek Precision Products** in Northbrook Illinois is a precision metal machining company that manufactures tens of millions of parts annually for many US-based customers. Holleway partnered with the Panek family as they were, in part, seeking a financial partner to help shoulder the financial investment in capital equipment and other resources needed to help grow the Company. As a result of the growth the company is experiencing, Panek is currently seeking to add over **20** full-time employees, which is a daunting challenge in today's labor market.
- **T-TEK Material Handling** in Montgomery Alabama is a manufacturer of high-speed palletizing and de-palletizing equipment used primarily by beverage and other companies producing high volumes of canned products. The founders of T-TEK chose to work with Holleway, in part, to help finance the investments required in people, facilities, and equipment necessary to achieve the growth the company is currently experiencing. T-TEK is currently seeking to add over **10** full-time employees as soon as possible.

¹ An independent study prepared for the Library of Congress found that SBIC-backed small businesses created almost 3 million new jobs and supported an additional 6.5 million jobs over the 20-year period of their study. The average administrative cost was approximately \$35 per job created, and about \$11 per job created or sustained." *Paglia and Robinson, Measuring the Role of the SBIC Program in Small Business Job Creation, Report for the Library of Congress, at 4 (January 2017)* <https://www.sba.gov/sites/default/files/articles/SBA_SBIC_Jobs_Report.pdf>.

² Small Business Investment Act of 1958, Pub. L. 85-699 (Aug. 21, 1958). 15 U.S.C. 661.

Demand for investments from licensed SBICs was very strong throughout fiscal year 2021, which ended on September 30. This was the first year in the program's history that its annual authorized leverage maximum of \$4 billion was reached. As the nation emerges from the pandemic-induced economic downturn, the SBIC program provides a lifeline that helps many domestic small businesses not only survive but thrive. SBIA encourages Congress to consider raising the annual \$4 billion authorization limit for SBIC leverage in anticipation of continued SBIC program growth.

Coming out of the massive economic disruptions caused by the pandemic, small businesses need capital to recover and grow. The SBIC program is doing what Congress tasked it to do and everyone should be proud of the way the program is being run. At the end of FY 2021 there were over \$34 Billion in assets in the program – all of which is for capitalizing American small businesses. The amount of private capital, from Limited Partners, hit an all-time record validating the private market's support for small businesses and the SBIC program. SBICs made over \$7 Billion in investments into small businesses– another record. SBA licensed 32 funds in 2021, 12 of which were first-time funds. When the SBA hit the \$4 Billion annual leverage cap for the first time ever, it represented a 90% increase year over year. Congress should raise this cap to ensure it is not hit again in 2022. Despite being an extraordinarily challenging year, zero SBIC Debenture or Non-Leveraged SBIC funds entered the “office of liquidations” the equivalent of a bank's “workout” group. The program is doing what it was designed to do and small businesses across the country are benefiting. These investments are in real companies with real staying power and real growth potential.

SBA Staffing and IT Technology

The Office of Investment and Innovation (OII) staff that regulate the SBIC program did a remarkable job during the pandemic. As we emerge from the pandemic, small businesses will look for an effective SBA to continue to provide the help they need to grow. As is the case throughout the US economy, OII staffing shortages are severe, and this staff shortage may pose a risk to expanded capital access to small businesses and healthy oversight of the SBIC program.

For example, frontline SBIC regulators typically monitor and regulate about 10-12 SBIC funds per regulator because of the unique nature of each fund. Today, however, the SBA is so short-staffed that the ratio between Office of Investment and Innovation regulator and regulated SBICs is reported at a level of nearly 50 SBICs per operations analyst. Regulated entities do not normally ask for more regulators, but we are. SBIA encourages Congress to provide the necessary resources, both human and technological, to ensure SBA can run this successful program, provide necessary oversight, and remain responsive.

The OII staff have helped deliver strong results for the SBIC program during the pandemic despite using outdated technological tools. While the SBIC program involves capital levels in 2021 that reached \$34 billion, its OII regulators are saddled with rudimentary IT technology that cripples productivity and creates unnecessary risk. SBA has incredible amounts of data but cannot convert it into useful information.

Everyone in the private sector has IT technologies that can give them investment and risk management information with just a few clicks of a mouse. These same tasks can take the SBA

weeks or months to replicate. a challenge that Congress can help alleviate with adequate funding to SBA for IT technology upgrades.

At Holleway we, provide long-term patient capital to small businesses. This longer-term strategy is an incredible advantage to small businesses in surviving the bumps, sometimes jarring bumps, that small businesses face. But SBA discourages equity strategies in large part because the SBA does not have tools tailored specifically for equity investing. We would be able to provide more equity capital to more small manufacturers if the SBA had the tools to allow more equity investing.

Let me also add that the SBIA reiterates its long-standing support of the *Investing in Main Street Act*, a bill designed to increase bank investments in SBIC funds, which was introduced by Senators Duckworth and Young in the Senate and Reps. Chu and Garbarino in the House. The bill currently has passed the House Small Business Committee and awaits a vote by the full House chamber.

This proposed legislation would amend the Small Business Investment Act of 1958, which currently restricts SBICs from taking capital investments from banks that have more than five percent (5%) of their institution's capital and surplus invested in SBICs. Bank regulations currently permit these same banks to invest up to 15 percent of their capital and surplus (with regulatory approval) in SBICs.

This simple change would create symmetry between statute and bank regulation and would increase the amount of capital that banks can deploy into SBICs. Increasingly, SBIC funds are encountering smaller banks who have hit the five percent (5%) statutory cap but want to invest more in job creation that is a hallmark of the SBIC program.

Conclusion

Let me end where I began. The SBIC program is working well. But there are always occasions for improvements.

On behalf of Holleway Capital and the SBIA, thank you for the opportunity to present observations about the state of the SBIC program and recommendations on maintaining the program's critical role to provide much needed capital to domestic small businesses.

I am happy to answer questions from the Subcommittee.

###

**Committee on Small Business Subcommittee on Economic Growth, Tax, and Capital
Access Hearing**

A Review of the SBIC Program

Carmen Palafox Founder & Managing Partner, 2045 ventures

October 27, 2021

Introduction

I appreciate this opportunity to testify before the Committee on Small Business Subcommittee on Economic Growth, Tax, and Capital Access Hearing. I dedicate lots of time and effort to expanding economic growth and capital access. I founded 2045 ventures in 2020 to fill persistent gaps in the market for underrepresented founders and invest in sectors that will drive our future, including climate tech, fintech, and health tech. I serve on the National Venture Capital Association (NVCA) board of directors and am a founding board member of LatinxVC. As a founding board member at LatinxVC, I focus on creating opportunities for Emerging Fund Managers.

I will share my personal story, along with my experience as an Emerging Fund Manager and my thoughts on how women and minority fund managers are critical to the ongoing success of our venture capital industry and our economy.

I was born and raised in San Diego, California, and moved to Los Angeles to study economics at the University of Southern California. I spent 15 years at Dimensional Fund Advisors, a global asset management firm, and gained a deep appreciation for capital markets. I left Dimensional in 2011 to pursue an Executive MBA at Berkeley Haas. There I was immersed in venture capital and startups and recognized the industry's increasing importance to our economy.

After graduating from Berkeley Haas in 2014, I wanted to launch a fund to invest in underrepresented founders. I was too early. The ecosystem supporting women and underrepresented founders and Emerging Managers wasn't as robust as it is today, so instead, I joined two business partners and launched a venture capital fund, an accelerator, and an innovation lab to invest in hardware technology startups. Our venture capital firm reached entrepreneurs in 70 countries and 33 states. We invested in 22 startups across various sectors and industries through our first fund, including companies building EdTech, Digital Therapeutics, Climate Tech, Immersive Computing, Advanced Manufacturing, and Space Tech. Some of our startups were beneficiaries of government grants for R&D and scale-up manufacturing.

In October 2020, I launched 2045 Capital to fill gaps in the market. 2045's thesis is that diverse teams outperform, a view supported by data. The data show that startups with ethnic teams return 30% more capital to investors, and startups with at least one female founder outperform all-male teams by 63%. 2045's objective is to invest in startups where at least one founder is a

woman, an immigrant, or a founder of color. I have a successful track record of reaching this audience through personal investments and fund investments: 63% have a founder of color, 41% have at least one female founder, and an immigrant founder founded 60%.

Current State of Venture Capital

Pitchbook and the NVCA's Venture Monitor¹ reports on the state of the industry including capital investments, exit values, and new fundraises. The most recent third-quarter 2021 report shows that venture capital backed startups are at the top of the public markets. VC-backed IPOs also accounted for more than two-thirds of the total US listings year-to-date. In addition, 2021 is on track for another record-breaking year for venture investment, exit activity, and fundraising with a total of \$238.7 billion invested year-to-date.

Underrepresentation

The venture capital ecosystem is thriving for most, but women and minorities are underrepresented. This inequity is unsustainable when you consider the changing demographics of our nation. The census predicts that by 2045 there will not be a racial majority in the United States, which is the case in five states today. Already there is not a racial majority for youth under 18. And 25% of Gen Z are Latinx.

In Los Angeles, where I reside, 45% of the population is Latinx. And 35% of the University of California's student population is Latinx. Los Angeles's venture ecosystem is thriving and the third largest in deal count and value behind the Bay Area and New York. But in Los Angeles, women and underrepresented founders are lagging in funding. PledgeLA, where I am on the advisory board was launched by the Mayor's Office and the Annenberg Foundation to foster an inclusive startup and venture capital ecosystem. The organization measures and reports venture capital allocation across gender and race. From January 2016 to December 31, 2020, PledgeLA reports that Latina founders received 2% of venture capital investment and Black female founders received 3% of venture capital investment.²

Furthermore, there is a lack of female checkwriters in Los Angeles, the third largest technology ecosystem in the US. [According to All Raise and Crunchbase only .61% of female checkwriters are based in Los Angeles.](#)

SBIC

Programs such as the SBIC can help women and underrepresented fund managers grow their presence, activate more investment into startups, and generate other benefits to society. For example, women and minority fund managers are more likely to invest in women and underrepresented founders based on their networks and sourcing methods.

Why Now: the growing gap and founders seeking diverse investors

¹ Q3_2021_PitchBook-NVCA_Venture_Monitor, available at https://nvca.org/wp-content/uploads/2021/10/Q3_2021_PitchBook-NVCA_Venture_Monitor.pdf

² ■ 6. PledgeLA 2021 VC Portfolio Diversity by Race & Gender.pdf

All Raise analysis of 2020 data shows that the pandemic year precipitated a backslide for female founders' access to funding — as well as those writing the checks.³ All Raise also reports that 64% of VC firms in the US with more than \$25M in assets under management have zero female checkwriters. And of the women that became investors in 2020⁴ only one self-reporting as African American and zero as Latinx.

Furthermore, there is a growing trend of founders recognizing the benefit of having women and minority investors. [The Cap Table Coalition](#), of which I am a member, has successfully deployed \$16 million into high tech startups in partnership with entrepreneurs seeking female and minority investors.

Program Recommendations

If our goal is to build back better, we need to quickly empower talented women and other socially disadvantaged managers to deploy capital, including firms with solo emerging managers.

Women and Emerging Managers have many resources at their reach to help them grow their firms, get advice, and source opportunities. These include nonprofit organizations such as All Raise (established in 2017), Women in VC (established in 2015), Transact (established in 2018), LatinxVC (established in 2019), BLCK VC (established in 2018), Venture Forward (established in 2020). And data exist to support the [outperformance of female managers](#) and [first time managers](#).

Solo Emerging Managers do not present a greater risk to investors and should not be excluded from programs meant to jump-start innovation. The market has embraced Solo Managers for many reasons, including their unique geographies, networks, diverse backgrounds, and ability to move quickly. Furthermore, fund formation documents address the succession of Managers should the case arise. Excluding Solo, Managers would eliminate qualified women and minority managers. And according to Rob Freelen, Head of VC Relationships at Silicon Valley Bank, [Solo General partners are raising funds larger than some established funds](#).

Conclusion

I am grateful for this committee's attention to the SBIC program. Venture capital is and will continue to fund transformative startups. Government programs such as the SBIC can play a critical role in closing persistent gaps in venture capital and accelerating the inclusion of women and minorities. The beneficiary of this increased inclusion at the investor level will fuel more jobs and accelerate pay equity for all Americans.

³ 2020 Was a Tough Year for Female and Non-Binary Founders & Funders
<https://medium.com/allraise/2020-was-a-tough-year-for-female-and-non-binary-founders-funders-87b6876a4a0d>

⁴ <https://allraise.org/assets/all-raise-annual-report-2020.pdf>

When we build back better, we must focus on outcomes that close persistent gaps in the underrepresentation of women and minorities. Building an inclusive ecosystem starts with greater representation at the investor level. With outcomes in mind we can build startups that are rooted in Diversity, Equity, and Inclusion.

Government programs such as the Micro SIBC and Emerging Manager Program, should have the broadest aperture and should be built to drive a more inclusive ecosystem for an ever-increasingly multicultural society.



Testimony of John Mickelson

Co-Founder and Managing Partner of Midwest Growth Partners

BEFORE THE HOUSE COMMITTEE ON SMALL BUSINESS SUBCOMMITTEE ON ECONOMIC GROWTH,
TAX, AND CAPITAL ACCESS HEARING ENTITLED "A REVIEW OF THE SBIC PROGRAM"

Rayburn 2360

Wednesday October 27, 2021 10AM EST



Good morning, distinguished members of the subcommittee, my name is John Mickelson and I am the Co-founder and Managing Partner of Midwest Growth Partners, located in West Des Moines Iowa, with an additional office in Omaha, Nebraska.

Midwest Growth Partners is a USDA licensed Rural Business Investment Company ("RBIC") and we raise dollars from the private sector to make succession planning and growth investments in food & agricultural, manufacturing, and distribution businesses in rural communities in the United States. Like the Small Business Investment Company program, Rural Business Investment Companies make investments in small businesses where institutional capital is scarce, particularly in non-coastal communities. Our investors include members of the farm credit system, rural electric co-ops, ag trade organizations such as the Iowa Corn Growers, commercial banks, and successful private citizens – most of whom own businesses involved in food & agricultural production.

Rural businesses are underserved by institutional capital for succession planning and growth capital and that fact was the core thesis when founding Midwest Growth Partners in 2013. At the time, potential investors asked if there would be enough opportunities to evaluate for investment and we hypothesized that we would see 100 opportunities each year and likely execute on one or two. In our first full year in business, we evaluated 230 investment opportunities, validating our thesis of rural and non-coastal communities needing an institutional capital source, and that number has continued to grow each year. This year we will evaluate more than 800 opportunities. All told, we have made 19 investments in rural areas, deploying more than \$100 million of much needed private capital that has been used to grow businesses and provide a next generation future of ownership.

Starting with seven after our first acquisition in 2014, our portfolio companies today have over 2,600 employees employed in and often living in rural communities. These jobs all pay above the living wage, provide benefits, and generated more than \$7 million in federal, local, and state withholding taxes for their local communities in 2020. While we are proud of the impact our portfolio company jobs provide, we are just as proud knowing that many of the jobs provide off-farm income, allowing one spouse to remain farming, while the other spouse secures benefits for the family and additional income. Since inception, Midwest Growth Partners has grown the employment at its portfolio companies by 25%, on average, from the date of its original investment.



A real-life example of Midwest Growth Partners capital at work is our investment in Fast Ag Solutions located in Windom, Minnesota, population 4,400. Fast Ag manufactures sprayers and liquid fertilizer applicators from its 100,000 plus square foot facility in Windom. Midwest Growth Partners partnered with the Fast Ag management team to purchase the company from the previous owners in the fall of 2020 and have grown full-time employment from 52 to 73 during that time, all of which are working overtime.

This type of economic development in rural areas would not be possible without programs like the Rural Business Investment Program, and more can be done. Since the great recession in 2008, rural job creation has contracted by 4.2%. According to the USDA, metropolitan areas, where most institutional investment capital is concentrated, has poverty rates of 12.6% compared to 16.1% in rural areas. With 19% of people in the US living in rural areas, this shortage of capital is critical for millions. Providing support for the Rural Capital Access Act, which would enable Rural Business Investment Companies to utilize leftover federal funds from the SBIC program, is one clear path to ensuring improved the lives of these 19%. The Rural Capital Access Act would put additional capital into experienced fund managers hands who live in, are from, and are operating their businesses near the rural areas that so desperately need investment capital. Other policy enhancements that would improve rural and underserved investment areas within the structure of the successful existing SBIC program include the creation of a MicroSBIC license, which will create a more inclusive pool of talented entrepreneurs to invest in underserved communities, the creation of a SBIC working group to increase the number of SBIC applicants, specifically those located in underserved communities and underlicensed states, and the creation of the SBA office of Rural Affairs.

Unfortunately, all the success that has been made and the promise of critical programs mentioned above to accelerate that success could be muted because of current issues facing small business. PPP was a critical lifeline during the COVID-19 pandemic in 2020, but now businesses are facing a new set of challenges in 2021 and 2022.

Our portfolio company partners are facing 30-40% price increases in raw materials used to make goods – and that is if they are able to secure the materials at all. Existing supply chain constraints are having a direct impact on sales and profit margins, which constrict the ability to reinvest in our businesses and hire more employees.



Attracting and retaining talent, which was already difficult, has become a crisis as uncertainty looms surrounding vaccine mandates. Many companies are facing the realization that they could lose up to 50% of their workforce overnight and will not be able to fulfill the orders and contracts they have already agreed to.

The prospect of higher taxes, of all forms, is delaying business decisions necessary for long-term business planning. Midwest Growth Partners has experienced these challenges daily in the work we do in rural communities with small businesses. On the pass-thru income tax side, these proposals aren't impacting only billionaires, but small business owners, who when faced with the prospect of even a small tax increase will forgo the hiring of additional workers, even one or two, or an investment in capital goods, such as something as simple as a forklift. Possible increases to capital gains rates or changes to the existing 1202 code have already created unnatural business outcomes as owners and investors accelerate or indefinitely delay decisions related to their personal succession planning or growth investment strategy. Possible changes to the carried interest model will disincentive fund managers from making investments in all areas, including rural and other underserved communities.

Businesses in rural areas, and small business generally, already face a scarcity of capital access, negatively impacting the lives of millions of Americans. As we near the hopeful end of the COVID-19 pandemic, these businesses are optimistic to grow and create prosperity for their employees and communities. Small and rural business owners and investors are used to facing headwinds in their business – no day is ever easy – but adding additional regulatory and cost burdens is not in their best interest and definitely not in the best interest of the communities they operate in and the millions of employees who provide goods and services which make our country the land of opportunity.

Thank you and I would welcome any questions you have.



November 2, 2021

The Honorable Sharice Davids
Chairwoman, Subcommittee on Economic Growth,
Tax, and Capital Access
U.S. House Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515

Re: A Review of the Small Business Investment Company Program –Statement for the Record

Congresswoman Davids,

First, thank you for holding this very important and timely hearing. As we finally exit what has been one of the darkest periods in our country's history, with a once in a generation pandemic that disproportionately ravaged communities of color, to historic levels of social unrest in the aftermath of the tragic murder of George Floyd, our nation must do better to empower diverse communities.

Founded in 1999, the New America Alliance (NAA) is a national organization of Latino business leaders dedicated to advancing the economic development of the American Latino community. Our members leverage their success and influence as leading money managers to increase the availability of investment capital for women and minority-owned firms, and to accelerate diverse leadership in entrepreneurship, corporate America, and public service.

We firmly believe access to investment capital for women and minority-owned businesses is one of the last frontiers of the civil rights movement. The availability of capital means the difference between a community that can build both individual and community wealth through flourishing businesses and job opportunities, and those communities that stagnate, with ever higher levels of poverty and lack of opportunity.

In many ways, the COVID-19 pandemic amplified many of the social inequities access to capital for women and minority-owned businesses could help address. Ethnic communities, where a historic lack of economic opportunities and investment have defaulted entire populations into "essential" work, vastly increased the incidence of infection, severity and lethality of the virus.

The truth is our country will never have shared success without shared opportunity and achieving that goal will require us to take a serious look at why initiatives like the Small Business Investment Company (SBIC) program have performed so poorly partnering with funds led by women or diverse managers. While we support a more formal, rigorous standard for requiring the SBIC to license more women and diverse managers, we appreciate the political climate makes it unlikely, so we are ready to partner with you in rolling up our sleeves to assess and identify the process at SBIC that are driving this outcome.

Over the next several days, we will be meeting with our members that have operated successfully as SBIC managers, and a few that have either failed to get an SBIC license or never applied because of concerns with how the program is operated. We will compile their experiences into implementable recommendations for the Committee to consider as you work to improve the SBIC program's performance partnering with women and diverse fund managers.

Respectfully,

Respectfully Submitted,



Solange Fernández Brooks,
Chief Executive Officer,
New America Alliance


Bank

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TD Bank, N.A.

 2005 Market Street, 2nd Floor
 Philadelphia, PA 19103

OCTOBER 27, 2021

Chair Davids (D-KS) Ranking Member Meuser (R-PA) Members of Committee – my name is Carl Kopfinger. I am a Senior Vice President with TD Bank, and I am based in Philadelphia, Pa. TD Bank, America's Most Convenient Bank, is one of the 10 largest banks in the U.S., providing more than 9.6 million customers with a full range of retail, small business and commercial banking products and services at more than 1,100 convenient locations throughout the Northeast, Mid-Atlantic, Metro D.C., the Carolinas and Florida. In addition, TD Bank and its subsidiaries offer customized private banking and wealth management services through TD Wealth®, and vehicle financing and dealer commercial services through TD Auto Finance. TD Bank is headquartered in Cherry Hill, N.J.

I am responsible for the Bank's investments in Small Business Investment Companies (SBICs) within our regional footprint. We are currently managing more than 75 SBIC investments, including both levered and unlevered venture capital, senior credit, mezzanine, and lower middle market buyout funds. The Small Business Administration's (SBA) SBIC program is an important component of TD's efforts to support small businesses and job creation.

Our role in the small business investment ecosystem system is to serve as a Limited Partner (LP) in SBIC funds, meaning that we invest the bank's capital into SBIC funds, which, in turn, benefit small businesses in the United States that are in need of long-term capital. LPs are the backbone of the SBIC program, which is a market-driven collaboration of public and private funding. The SBIC program works as an amplifier of private investments into small businesses. If LPs do not invest their private capital into SBIC funds, then U.S. small businesses would not receive needed growth capital through the SBIC program. The key to the success of the SBIC program is that an SBIC fund manager must first raise private LP capital commitments, followed by submitting a material assessment questionnaire (MAQ application) to the SBA. If approved, the fund manager is licensed to operate as an SBIC. The MAQ application also provides for the SBIC fund to apply for leverage from the SBA in the form of SBA debentures, which is a low-cost method to increase the size of the SBIC fund and magnify the capital impact for U.S. small businesses. The rationale behind the SBIC program is a linking of the need from U.S. small businesses for growth capital and a real investment opportunity for the private LPs. The SBA's leverage magnifies the capital impact. As a result, more capital is being provided for expansion of U.S. small businesses, creating more jobs and economic expansion – a real win-win situation. At TD, we are proud of the role we play in this successful program.

Emerging from the massive economic disruptions caused by the global Coronavirus pandemic, U.S. small businesses continue to need capital to recover and grow. As tasked by Congress, the SBIC Program is delivering capital to small business. At the end of FY 2021 there were over \$34 billion in assets in the program – all of which capitalized American small businesses. The amount of private capital from LPs, like TD Bank, hit an all-time record, validating the private market's support for small businesses and the SBIC program. The SBA licensed 32 funds in 2021, 12 of which were first-

time funds. And the SBA reached the \$4 billion annual leverage cap for the first time ever, representing a 90% increase year-over-year. Furthermore, SBIC funds financed more than \$7 billion in investments into U.S. small businesses— another record. Despite being an extraordinarily challenging year, zero SBIC Debenture funds and Non-Leveraged SBIC funds entered the “office of liquidations”, the equivalent of a bank’s “workout” group. The program is working.

TD is particularly proud of the impact of our SBIC fund investments. Over 99% of the small businesses in our SBIC portfolio, financed by our SBIC fund clients, survived the global pandemic despite it being a brutal year for small businesses. Our SBIC fund clients invested capital into 110 low- and moderate-income areas (LMI), including 27 new LMI investments since the beginning of the pandemic. Additionally, 30 of our LMI investments are in below poverty LMI census tracts. Therefore, access to patient capital and supportive SBIC fund managers was a powerful lifeline for the recovery of these U.S. small businesses while saving many communities from further economic damage.

The existing SBIC program, for both Debenture funds and Non-Levered funds, is an important positive economic tool. But even good programs can be improved.

TD's investment allocation to all SBICs continues to be dependent upon current market and regulatory conditions. I don't see TD's allocation changing in the near term so long as SBIC funds remain a permissible investment under banking laws and regulations.

Venture and SBICs

For more than two decades, including through economic downturns, TD Bank remains committed to the SBIC program and continues to actively invest. Presently, 19 of the 75 active SBIC funds in our current investment portfolio are venture capital SBIC funds. At our peak, we managed approximately 40 SBIC venture funds, which are the foundation of small business formation and job creation in the United States. The venture funds we have supported and continue to support are generally less than \$125 million in fund size. These fund managers invest patient equity capital in both technology-enabled businesses and life science companies nationally. The investments span seed/early stage through growth equity/late stage business concerns. Most SBIC funds are not venture funds but rather are lower middle market mezzanine funds because the leverage provided by the SBA is limited to small businesses that are already cash flow positive and generally later stage. Most SBICs that are venture-oriented are “non-levered” which makes early investing a challenge.

The following theme presents an opportunity for the SBA to improve its licensing and back-office processes to attract venture funds to the SBIC program.

One of our early-stage venture funds, based in NYC, has invested in four infrastructure companies addressing current needs as well as three niche healthcare companies addressing the needs of an aging population. Additionally, their fintech investments have focused on the needs of Americans who have less than \$1,000 in their bank accounts or have amassed too much household debt. This is the type of venture fund that should be retained in the SBIC program.

This NYC-based fund manager experienced interruptions in the SBIC licensing process due to delays by the SBA's field audit operation department, which could not schedule the SBA's routine annual exam for 4-6 months. In fact, despite taking no SBA leverage, this applicant could not advance in the licensing process until the audit was scheduled, completed, and a no findings letter issued. The fund had reached the end of its investment period in the prior fund and thus was not able to make any additional capital investments in small businesses in NY state until the new fund was licensed by the SBA. The most expedient solution for the fund manager was to leave the SBIC program, operate as a non-SBIC fund and close on the private LP capital raised from their investor base.

Unfortunately, the Volcker Rule prohibits TD Bank from investing in all non-SBIC funds. Another one of our SBIC fund clients, an early-stage healthcare venture fund in Boston had a similar experience and also decided to leave the SBIC program after previously managing three unlevered SBIC funds.

In hindsight, it is likely that neither the NYC or Boston based venture funds would have left the SBIC program if the SBA was able to arrange for a speedy field audit and expedite the subsequent licensing process. The corollary is that unpredictable regulatory delays, high compliance costs and program fees are impactful for funds participating in the SBIC program, especially small unlevered venture funds. The country would benefit from having more small venture funds in all regions of the country.

Over the last decade or more, TD Bank has seen an increase in awareness, interest and investment consideration by banks, university endowments, charitable foundations, and SBIC fund-of-funds investors attracted to the strength of SBIC program and the fund managers participants. While the two fund managers I previously discussed were unlevered venture funds, existing SBIC program investors understand the power of SBA leverage with mezzanine funds because of the benefit of low-cost SBA leverage on investment returns. Similarly, I believe the SBIC program would benefit from a venture-specific equity program and produce a substantial economic impact if the venture equity program is properly aligned with private LP investor equity, like a TD Bank. Said differently, it is my hope and expectation if the venture equity SBIC program (VSBIC) is implemented that the SBA's capital will be *pari passu* with the private Limited Partner's capital and not senior to the equity of the private LPs in the capital stack. If the SBA VSBIC terms are appropriately structured, I believe the current base of private investors in SBIC funds would support the VSBIC program, specifically the formation of smaller venture funds across the country. Similarly, the VSBIC program should flourish if the money is deployed by responsible venture fund managers whose investment focus is directed towards disadvantaged individuals and companies in underserved markets, veterans, small manufacturers, and critical infrastructure businesses.

In conclusion, TD Bank makes SBIC investments for both Community Reinvestment Act credits as well as for the economic returns. We focus on strong investment managers who have a dependable track record of delivering solid performance results, returning capital to its Limited Partners, treating entrepreneurs with respect, and growing U.S. small businesses that we can all be proud of. We have seen firsthand the job creation, job retention, and revenue growth that our fund partners have achieved with their portfolio companies. This revenue growth has a rippling effect on tax revenues generated in the states and local communities in which these companies operate.

Thank you again for your time and allowing me to present an LP's perspective on the important role the SBIC program plays and the VSBIC program could play in funding small businesses and generating jobs, tax revenue, and investment returns.

Respectfully submitted,

Carl Kopfinger
Senior Vice President
TD Bank, N.A.

