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Race and Equity in the Age of Unicorns

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This Article critically examines startup culture and its legal predicates. The Article analyzes innovation culture as a whole and uses the downfall of Theranos to illustrate the deficiencies in Silicon Valley culture, centering on race and class. The Article demonstrates that the rise and fall of the unicorn startup Theranos and its founder, Elizabeth Holmes, is emblematic of the problem with the glorification and pursuit of the unicorn designation for startup ventures. The examination of the downfall of Theranos exposes how investors, founders, and others in Silicon Valley engage with each other in the context of pursuing unicorn status. The saga of Theranos lays bare how the wealthy and the privileged control the private financial markets and underscores the structural inequities within the startup ecosystem. Such a structure promotes certain types of entrepreneurs to the exclusion of others. Diverse and nontraditional entrepreneurs in the startup world face tremendous hurdles to securing financing, mentorship and media exposure. In stark contrast, founders like Holmes benefit from a perception of worthiness drawn from factors such as race, socioeconomic status, pedigree and social connections. This Article examines how the culture of creating the next unicorn has ramifications beyond fraud and risk, but also socio-economic consequences.

[†] Clinical Professor of Law, Columbia Law School. This Article is based on a presentation given at the ComplianceNet 2019 Conference on Business Ethics, at the Villanova University Charles Widger School of Law. It was presented at the 2019 Clinical Law Review Writers' Workshop at New York University Law School and the 2019 Biennial LatCrit Conference at the Georgia State University School of Law. I thank the facilitators and participants at each workshop for their insightful comments and suggestions. For additional helpful comments and suggestions, I would like to thank Deborah Archer, Alina Ball, Priya Baskaran, Stephanie Charles, Jennifer Fan, Gautam Hans, Jennifer Olivas, Lauren Rogal, Colleen Shanahan, and Erika Wilson. For truly exceptional research assistance, I thank Dola Adebayo and Anisha Mohin.

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INTRODUCTION

The holy grail for a startup is the achievement of the unicorn moniker: the billion dollar valuation on the private market.[1] Silicon Valley is ground zero for the creation of a unicorn because of the number of influential investors, innovators, and businesses in the region, which is home to thousands of startup companies and the country's largest technology corporations.[2] The amount of wealth in Silicon Valley is astounding.[3] Silicon Valley has multiple definitions—the tangible geographic one, defined as the southern part of the San Francisco Bay Area, and the metaphorical one that refers to the U.S. high tech economic sector and other comparable sectors around the world.[4] The geographic region accounts for nearly half of all the venture capital in the United States.[5] Because of its influential investors and gatekeepers, the metaphoric region represents a powerful private market for capital raises.[6]

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1. The term "unicorn" was coined by Aileen Lee as a term for startups valued over $1 billion. Aileen Lee, *Welcome to the Unicorn Club: Learning from Billion-Dollar Startups*, TECHCRUNCH (Nov. 2, 2013, 11:00 AM), https://techcrunch.com/2013/11/02/welcome-to-the-unicorn-club. Market research firm CB Insights found that there are now over 600 private companies valued at $1 billion. *$1B+ Market Map: The World's 600+ Unicorn Companies in One Infographic*, CB INSIGHTS (Mar. 24, 2021), https://www.cbinsights.com/research/unicorn-startup-market-map/.

2. *See* Shobhit Seth, *Why Is Silicon Valley a Startup Heaven?*, INVESTOPEDIA, https://www.investopedia.com/articles/personal-finance/061115/why-silicon-valley-startup-heaven.asp (June 25, 2019); *see also* Kimberly Amadeo, *Silicon Valley, America's Innovative Advantage*, BALANCE, https://www.thebalance.com/what-is-silicon-valley-3305808 (Nov. 27, 2020).

3. According to the Brookings Institute, the metropolitan area of San Jose, California, has the third-highest GDP per capita in the world (after Zurich, Switzerland, and Oslo, Norway). Gina Hall, *San Jose Area Has World's Third-Highest GDP Per Capita, Brookings Says*, SILICON VALLEY BUS. J. (Jan. 23, 2015, 3:34 PM), https://www.bizjournals.com/sanjose/news/2015/01/23/san-jose-has-worlds-third-highest-gdp-per-capita.html. According to the research institute Wealth-X, the percentage of "ultra high net worth individuals" (assets worth at least $30 million) in the San Francisco Bay Area has continued to grow each year, with an increase of 16.6% of ultra high net worth individuals between 2018 to 2019. WEALTH-X, WORLD ULTRA WEALTH REPORT 2020, at 2 (2020), https://thehometrust.com/wp-content/uploads/2020/10/Wealth-X_World-Ultra-Wealth-Report_2020.pdf.

4. Troy Segal, *Silicon Valley*, INVESTOPEDIA, https://www.investopedia.com/terms/s/siliconvalley.asp (Oct. 27, 2020); *Silicon Valley*, DICTIONARY.COM, https://www.dictionary.com/browse/silicon-valley (last visited May 21, 2021).

5. Richard Florida & Karen M. King, *Spiky Venture Capital: The Geography of Venture Capital Investment by Metro and Zip Code*, MARTIN PROSPERITY INST. (Feb. 22, 2016), http://www-2.rotman.utoronto.ca/mpi/content/spiky-venture-capital/ (showing that San Francisco, California, accounts for 25.26% and San Jose, California, accounts for 14.51% of venture capital in the United States); Richard Florida, *The Extreme Geographic Inequality of High-Tech Venture Capital*, BLOOMBERG: CITYLAB (Mar. 27, 2018, 7:43 AM), https://www.bloomberg.com/news/articles/2018-03-27/the-extreme-geographic-inequality-of-high-tech-venture-capital ("Silicon Valley . . . currently accounts for nearly 45 percent of total venture capital investment in the entire United States.").

6. Jim Yu, *The Unforeseen Challenges of Raising Capital*, FORBES (Dec. 16, 2013, 9:30 AM), https://www.forbes.com/sites/groupthink/2013/12/16/the-unforeseen-challenges-of-raising-capital/#1e7c2a496989; *see* Ray Hennessey, *Elitism Has No Place in Entrepreneurship*, ENTREPRENEUR (Sept. 18, 2015), https://www.entrepreneur.com/article/250831 ("[E]litism is found too often among entrepreneurs, particularly in tech startups. The myopia, the drive that fuels people to take risks, often creates great companies and great products, but it also cultivates a solipsism that assumes the work the entrepreneur is doing, and the way in which that work is being done, is the only important undertaking in the world.").

The paradox of Silicon Valley is that it is a community built on the ideals of pursuing innovation and of challenging the status quo, but in reality, the practices and culture of Silicon Valley are stagnant in key ways that further entrench the status quo. Further, Silicon Valley purports itself to be the ultimate meritocracy, but in reality, the culture reproduces and reinforces racial and gender inequities.[7] In Silicon Valley, indeed, startup success tracks dominant cultural norms found in larger society. While the ideas, inventions, and companies purport to disrupt and innovate, the ecosystem of Silicon Valley values dominant race and class-based indicators of success and worthiness to the detriment of "nontraditional" and minority entrepreneurs. Examining the decade-long fraud of Theranos with a critical lens, the company's story provides an example of the paradoxical values of Silicon Valley and their ultimate harm to companies, investors, and customers.[8] The Theranos saga demonstrates the dysfunction and the systemic problems associated with the entrepreneurial process. This Article describes the pervasive structural racism and inequality in place that created an environment where a fraud of such magnitude was hidden for so long.

Theranos, the former blood-testing technology company, is notable for its meteoric rise, emblematic of the culture of creating a Silicon Valley unicorn company, as well as its disastrous fall from grace.[9] It is an unraveling that lost investors' money and endangered the health of its clients. The company garnered attention because of its claims that its innovative and proprietary technology could perform over 200 medical tests with a single drop of blood, at low cost, thereby revolutionizing the medical industry.[10] Given what is now known about the massive fraud and deception, the unbelievable ten-year growth and financial

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7. Safiya Umoja Noble & Sarah T. Roberts, *Technological Elites, the Meritocracy, and Postracial Myths in Silicon Valley*, *in* RACISM POSTRACE 113 (Roopali Mukherjee, Sarah Banet-Weiser & Herman Gray eds., 2019).

8. *See* Erin Griffith, *Theranos and Silicon Valley's 'Fake It Till You Make It' Culture*, WIRED (Mar. 14, 2018, 3:12 PM), https://www.wired.com/story/theranos-and-silicon-valleys-fake-it-till-you-make-it-culture (finding that in the so-called "age of unicorns," startups can raise large sums of capital from private investors and become sizable businesses without the scrutiny, onerous disclosures, and strict regulatory compliance of being a public company).

9. "'Unicorns' are private companies with valuations of a billion dollars or more. As their name indicates, unicorns were originally so rare as to be almost mythical." Jennifer S. Fan, *Regulating Unicorns: Disclosure and the New Private Economy*, 57 B.C. L. REV. 583, 583 (2016). Theranos raised more than $700 million from venture capitalists and private investors, resulting in a $10 billion valuation at its peak in 2013–2014. *See* Roger Parloff, *This CEO Is Out for Blood*, FORTUNE (June 12, 2014, 4:37 AM), https://fortune.com/2014/06/12/theranos-blood-holmes.

10. In fact, the two key pieces of the Theranos technology, the "Edison" and the "Minilab," were found to be unreliable. Lisa Eitel, *Theranos—And the Satisfaction of How Engineering Doesn't Lie*, DESIGN WORLD (Apr. 23, 2019), https://www.designworldonline.com/schadenfreude-for-theranos-and-satisfaction-in-how-engineering-doesnt-lie/. It was discovered that rather than using its own technology, the company often relied on the equipment of its competitor, Siemens, to perform certain blood tests. *See id.* Further, Theranos offered lower prices than its competition not because of the low cost of its product, but because the company was burning up cash raised from venture capitalists. *See* Zaw Thiha Tun, *Theranos: A Fallen Unicorn*, INVESTOPEDIA, https://www.investopedia.com/articles/investing/020116/theranos-fallen-unicorn.asp (Aug. 27, 2019).

success of Theranos is worthy of a close examination. The story of Theranos' rise demonstrates how structural, economic, and social forces play out in the startup context to favor certain actors and reward certain behaviors, to the detriment of others. In this Article, I suggest that such examination reveals the structural bias and inequality that is woven into the current system of private capital raising for startup entities. The broader impact of the revelation is that seemingly more than any other factors, race, class, and education are strong indicators of startup success. The story of Theranos, its founder Elizabeth Holmes, its former company president Ramesh "Sunny" Balwani, and the company's path to startup success reveals inequity rampant in the traditional canons of how to achieve entrepreneurial success.

Elizabeth Holmes launched the blood-testing startup in Silicon Valley in 2003 at the age of nineteen.[11] Beyond Theranos' claims and mission, much was made of Holmes as the young, "genius" founder of Theranos.[12] This "rising star" and "young genius" narrative is central to American legend making in business and entrepreneurship.[13] Historically, individual success and glory is celebrated and canonized.[14] For example, many historical figures, often referred to as robber barons, became wealthy through individual entrepreneurship efforts.[15]

Holmes made for a compelling founder. She was described as magnetic with an inspiring, idealistic vision for her company.[16] She is white and from an affluent family. She was well-educated; she went to a well-known prep school in Houston, Texas,[17] and after graduating, she matriculated to Stanford University in 2002.[18] She dropped out of Stanford during the fall of her sophomore year and used an education trust set up by her parents to start her

11. Lydia Ramsey Pflanzer, *The Rise and Fall of Theranos, the Blood-Testing Startup That Went from Silicon Valley Darling to Facing Fraud Charges*, BUS. INSIDER (Apr. 11, 2019, 8:55 AM), https://www.businessinsider.com/the-history-of-silicon-valley-unicorn-theranos-and-ceo-elizabeth-holmes-2018-5.

12. Avery Hartmans & Paige Leskin, *The Rise and Fall of Elizabeth Holmes, the Theranos Founder Whose Federal Fraud Trial Is Delayed Until 2021*, BUS. INSIDER (Aug. 11, 2020, 11:14 AM), https://www.businessinsider.com/theranos-founder-ceo-elizabeth-holmes-life-story-bio-2018-4 (stating that Holmes was hailed "as a genius who styled herself as a female Steve Jobs").

13. *See generally* Yiren Lu, *Silicon Valley's Youth Problem*, N.Y. TIMES MAG. (Mar. 12, 2014), https://www.nytimes.com/2014/03/16/magazine/silicon-valleys-youth-problem.html (articulating the concern about tech being "increasingly youth-fetishizing").

14. *See* Noam Scheiber, *Google Workers Reject Silicon Valley Individualism in Walkout*, N.Y. TIMES (Nov. 6, 2018), https://www.nytimes.com/2018/11/06/business/google-employee-walkout-labor.html ("For decades, Silicon Valley has been ground zero for a vaguely utopian form of individualism—the idea that a single engineer with a laptop and an internet connection could change the world, or at least a long-established industry.").

15. *See* Gus Lubin, Michael B. Kelley & Rob Wile, *Meet the 24 Robber Barons Who Once Ruled America*, BUS. INSIDER (Mar. 20, 2012, 9:56 AM), https://www.businessinsider.com/americas-robber-barons-2012-3.

16. JOHN CARREYROU, BAD BLOOD: SECRETS AND LIES IN A SILICON VALLEY STARTUP 7, 151 (2018).

17. Reed Abelson & Julie Creswell, *Theranos Founder Faces a Test of Technology, and Reputation*, N.Y. TIMES (Dec. 19, 2015), https://www.nytimes.com/2015/12/20/business/theranos-founder-faces-a-test-of-technology-and-reputation.html.

18. CARREYROU, *supra* note 16, at 12.

company.[19] At that time, the company was called Real Time Cures and it was based on her idea to develop a wearable patch that could adjust the dosage of drug delivery and notify doctors of variables in patients' blood.[20] She began developing lab-on-a-chip technology for blood tests, changed the company name to Theranos, a combination of the words "therapy" and "diagnosis," and pursued a new strategy for the company that would make testing cheaper, more convenient, and accessible to consumers.[21] Although she was heavily engaged with chemical engineering classes while on campus at Stanford, she had no medical or otherwise relevant scientific training.[22] Despite her lack of experience, she was at the helm of a company that would go on to raise hundreds of millions of dollars in private capital. Her rapid ascent is a racial reality unheard of for entrepreneurs of color because entrepreneurs of color are not only questioned with more rigor, but they typically have to demonstrate expertise and a viable product in order to access capital, and they also are unlikely to have trust funds to back them.[23]

Up until Holmes and her company were exposed as fraudulent in 2015, she had clearly mastered fundraising in Silicon Valley. Successful and famous venture capitalists, such as Tim Draper and Steve Jurvetson, founders of famed venture capital firm, Draper Fisher Jurvetson, were early investors in Theranos.[24] Famed power brokers, such as the former Chairman of Oracle, Don Lucas, and a former Secretary of State, George Shultz, were investors and served on the Board.[25] The endorsement of these notable kingmakers within Silicon Valley's ecosystem ensured that Holmes and Theranos gained the necessary visibility and buzz essential for unicorn status.

As she built Theranos, and started to achieve success with investors, Elizabeth Holmes was featured on the cover of multiple tech and industry magazines.[26] The media described her as a bright young star in the male-

19. Caitlin Roper, *This Woman Invented a Way to Run 30 Lab Tests on Only One Drop of Blood*, WIRED (Feb. 18, 2014, 1:30 PM), https://www.wired.com/2014/02/elizabeth-holmes-theranos/.

20. Megan Liscomb, *Elizabeth Holmes: The Making of a Scam*, FINANCE 101, https://www.finance101.com/elizabeth-holmes/ (Nov. 10, 2020).

21. CARREYROU, *supra* note 16, at 15.

22. Her chemical engineering professor, Channing Robertson, was a paid advisor to Theranos until 2012 when he gave up a tenured position and an endowed chair in Stanford's engineering department to join Theranos as an employee. *See* Tom Relihan, *4 Red Flags That Signaled Theranos' Downfall*, MIT SLOAN: IDEAS MADE TO MATTER (Oct. 29, 2018), https://mitsloan.mit.edu/ideas-made-to-matter/4-red-flags-signaled-theranos-downfall.

23. *See* Bärí A. Williams, *I Can't Wait for There to Be a Black Elizabeth Holmes*, FAST CO. (Mar. 16, 2018), https://www.fastcompany.com/40545503/i-cant-wait-for-there-to-be-a-black-elizabeth-holmes; *see also* James Norman, *A VC's Guide to Investing in Black Founders*, HARV. BUS. REV. (June 19, 2020), https://hbr.org/2020/06/a-vcs-guide-to-investing-in-black-founders.

24. *The Inventor: Out for Blood in Silicon Valley* (HBO documentary broadcast Mar. 18, 2019).

25. Roger Parloff, *A Singular Board at Theranos*, FORTUNE (June 12, 2014, 4:40 AM), http://fortune.com/2014/06/12/theranos-board-directors.

26. Katie Thomas & Reed Abelson, *Elizabeth Holmes, Theranos C.E.O. and Silicon Valley Star, Accused of Fraud*, N.Y. TIMES (Mar. 14, 2018), https://www.nytimes.com/2018/03/14/health/theranos-elizabeth-holmes-

dominated tech industry and some described her as "the next Steve Jobs."[27] A professor of Holmes, Channing Robertson from Stanford's engineering department, described Holmes as "a once-in-a-generation genius," comparing her to Newton, Einstein, Mozart, and Leonardo da Vinci.[28] Forbes Magazine referred to her as "the youngest self-made woman billionaire."[29] President Obama appointed her to be a U.S. ambassador for global entrepreneurship, and Harvard Medical School invited her to join their Board of Fellows.[30] The extensive media attention helped propel her fundraising.[31]

Inevitably, the fictions of Theranos unraveled as former employees blew the whistle and told their story to John Carreyrou, an investigative reporter for the *Wall Street Journal*. Carreyrou wrote about the myriad of lies and discrepancies at Theranos' lab, resulting in regulatory, civil, and criminal actions against Holmes and Balwani.[32] In 2016, Theranos was sanctioned by the Centers for Medicare and Medicaid Services.[33] The Securities and Exchange Commission (SEC) accused the company, its founder and CEO, and its former president of engaging in an elaborate fraud, alleging that Theranos, Holmes, and Balwani had made false statements about the company's technology, business, and financial performance.[34] Theranos and Holmes settled the SEC charge for an amount of $500,000 in addition to other penalties.[35] As of the writing of this Article, the charges against Balwani have not been settled. In September 2018,

fraud.html ("[Holmes] became an overnight celebrity, featured on magazine covers and richest-woman lists and in glowing articles.").

27. Parloff, *supra* note 9 (providing a statement from Holmes' former professor Channing Roberts) ("I realized that I could have just as well been looking into the eyes of a Steve Jobs or a Bill Gates . . . .").

28. CARREYROU, *supra* note 16, at 211.

29. In 2015, at the age of thirty, Holmes debuted on the Forbes 400 List. *See #435 Elizabeth Holmes*, FORBES, https://www.forbes.com/profile/elizabeth-holmes/?sh=7b447be647a7 (last visited May 21, 2021).

30. Sarah Buhr, *Elizabeth Holmes Quietly Stepped Down from Obama's Business Ambassador Program*, TECHCRUNCH (Aug. 2, 2016, 4:38 PM), https://techcrunch.com/2016/08/02/elizabeth-holmes-quietly-stepped-down-from-obamas-business-ambassador-program; Steve Tobak, *After the Theranos Mess, Can We Finally Quit Idolizing Entrepreneurs?*, Fortune (May 27, 2016, 6:00 AM), https://fortune.com/2016/05/27/quit-idolizing-entrepreneurs/.

31. Press Release, SEC, Theranos, CEO Holmes, and Former President Balwani Charged with Massive Fraud (Mar. 14, 2018), https://www.sec.gov/news/press-release/2018-41 ("The complaints allege that Theranos, Holmes, and Balwani made numerous false and misleading statements in investor presentations, product demonstrations, and media articles by which they deceived investors into believing that its key product—a portable blood analyzer—could conduct comprehensive blood tests from finger drops of blood, revolutionizing the blood testing industry.").

32. In 2015, the *Wall Street Journal* published an investigative story raising doubts about the company's blood-testing technology and the veracity of its financial performance. *See* John Carreyrou, *How Startup Theranos Has Struggled with Its Blood-Test Technology*, WALL ST. J. (Oct. 16, 2015, 3:20 PM), https://www.wsj.com/articles/theranos-has-struggled-with-blood-tests-1444881901.

33. John Carreyrou, Michael Siconolfi & Christopher Weaver, *Theranos Dealt Sharp Blow as Elizabeth Holmes Is Banned from Operating Labs*, WALL ST. J. (July 18, 2016), https://www.wsj.com/articles/u-s-regulator-bans-theranos-ceo-elizabeth-holmes-from-operating-labs-for-two-years-1467956064.

34. Press Release, *supra* note 31. The SEC referred to Theranos as an "elaborate, years-long fraud" in which Holmes and Balwani "exaggerated or made false statements about the company's technology, business, and financial performance." *Id.*

35. *Id.*

after defaulting on a $65 million loan, Theranos shut down operations.[36] On June 15, 2018, Holmes and Balwani were indicted in federal court in the Northern District of California for wire fraud and conspiracy.[37] Holmes and Balwani are awaiting trial on these wire fraud and conspiracy charges.

In the end, Theranos turned out to be a mule rather than a mythical unicorn. In the wake of the company's downfall and that of its founder, there are many questions that remain, not the least of which is the question of how Holmes was able to achieve the level of financial success that Theranos rested upon, without the requisite due diligence and oversight from investors and regulators. Putting aside the question of Elizabeth Holmes' intent to defraud investors and her Board, the story of Elizabeth Holmes' rise and her route to success illustrates the inequities inherent in the culture of the startup world. The story of Theranos, "[a]t its root, [is] a parable that cuts to the central dysfunctions in the American economic and political order, one that should dismantle our notions of meritocracy and put a strict limit on our forbearance for elites."[38]

The central premise of this Article is that the culture of creating a model unicorn company in Silicon Valley seems to adhere and perpetuate the principle that white, connected, and pedigreed founders are given primacy over others. Elizabeth Holmes' story is firmly rooted in, and is illustrative of, this culture. She was able to raise astounding amounts of money from private investors, not just because she had a great idea, but arguably because she was white, connected, and had the right pedigree, consistent with the culture surrounding a unicorn company.[39] Her story is not just a story of personal charisma or bias—it's a story of the structures of entrepreneurship in America.

This Article reveals the ways in which aspects of Theranos reflects the larger structural problems within Silicon Valley, analyzing the structural underpinnings that perpetuate the closed market, patronage system that largely benefits white male entrepreneurs in particular. The two largest facets of this system are a startup culture that rewards only a certain narrow category of founders deemed "worthy" by the culture's standards and restricted private

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36. John Carreyrou, *Blood-Testing Firm Theranos to Dissolve*, WALL ST. J. (Sept. 5, 2018, 12:10 AM), https://www.wsj.com/articles/blood-testing-firm-theranos-to-dissolve-1536115130 (reporting that, on September 4, 2018, Theranos announced in an email to investors that it would cease operations and release its assets and remaining cash to creditors after all efforts to find a buyer came to nothing). At the time of the writing of this Article, Holmes is awaiting trial on the wire fraud and conspiracy charges; however, the trial has been delayed due to Holmes' recent pregnancy announcement. Yasmin Khorram, *Elizabeth Holmes Trial Pushed to August Following Surprise Pregancy Announcement*, CNBC (Mar. 17, 2021, 2:25 PM), https://www.cnbc.com/2021/03/17/elizabeth-holmes-trial-pushed-to-august-after-surprise-pregnancy-announcement.html.

37. Sara Ashley O'Brien, *Elizabeth Holmes Indicted on Wire Fraud Charges, Steps Down from Theranos*, CNN: BUS. (June 16, 2018, 10:20 AM), https://money.cnn.com/2018/06/15/technology/elizabeth-holmes-indicted-theranos/index.html.

38. Avi Asher-Schapiro, *What the Theranos Documentary Misses*, NEW REPUBLIC (Mar. 29, 2019), https://newrepublic.com/article/153419/theranos-documentary-misses.

39. *See* Sarah McBride, *Insight: In Silicon Valley Start-Up World, Pedigree Counts*, REUTERS (Sept. 12, 2013, 2:04 PM), https://www.reuters.com/article/us-usa-%20%20%20startup-connections-insight-idUSBRE98B15U20130912.

markets used by the elites to entrench their cultural norms. It is a culture that does not necessarily reward based on merit. There is a philosophy of worth, reflected in the cultural norms, and the private markets create a mechanism for enforcing the cultural mindset.

The Article proceeds in three Parts. Part I looks at the culture in the startup ecosystem that dictates the process of becoming a unicorn company. It describes the general problems that exist within startup culture and the way the problems manifested in the context of Theranos. Part I also unearths the ways in which race and other cultural norms play a role in entrepreneurial success. Part I notes dramatic racial, gender, and class differences across venture capital funding, innovation levels, profitability, and the economy as a whole. Part II describes the traditional private fundraising mechanisms for entrepreneurs and investors, building on Part I to discuss perverse market incentives that perpetuate racism and classism within the context of the private markets. Additionally, Part II demonstrates the ways the private markets effectively enforce and perpetuate the closed homogenous culture in Silicon Valley in which entrepreneurs are required to raise money. While a detailed discussion of any policy proposals for changing the private financial markets is outside the scope of this Article, Part III offers some considerations toward challenging and changing institutional bias in Silicon Valley. While this Article focuses on Silicon Valley, the approaches and practices in the region among the entrepreneurial community have implications for entrepreneurial ecosystems nationally, and increasingly, internationally.

I. CHASING UNICORNS: STARTUP CULTURE AND THE HEURISTICS THAT ENABLE IT

Within limits, Silicon Valley places a primacy on disruption and innovation.[40] Generally, new ventures seeking to be a disruptive company or a company that innovates and changes existing ways of doing business are lauded.[41] While those in the space admire some level of disruption, in many

40. *See* DAVID EISWERT, EMILY SCUDDER & JOEL GRANT, T. ROWE PRICE INSIGHTS, TECHNOLOGICAL INNOVATION AND DISRUPTION 1 (2019), https://www.troweprice.com/content/dam/fai/Collections/MarketScene/tech_innovation_disruption/Tech_Innovation_Disruption_Insight.pdf; *see* Maximilian Schroeck & Gopal Srinivasan, *How to Innovate the Silicon Valley Way*, DELOITTE: INSIGHTS (July 22, 2016), https://www2.deloitte.com/us/en/insights/topics/innovation/tapping-into-silicon-valley-culture-of-innovation.html ("Silicon Valley has been driving innovation and disruption for several decades, and through the beginning of the 21st century, it continues to be one of the world's most important centers of innovation and technology disruption. The region is notable for its combination of widely available capital and rapid scale-up of commercially viable intellectual property (IP). More than one-third of the 141 companies in the Americas, Europe, and Asia Pacific that grew to a valuation of greater than $1 billion between 2010 and 2015 were located in the Bay Area, a striking testament to the area's ability to accelerate commercial success. Perhaps for this reason, 61 percent of companies with innovation centers have a presence in Silicon Valley." (citation omitted) (footnote omitted)).

41. *See* Barry Ritzholz, *The World Is About to Undergo Even Faster Change*, INDUSTRYWEEK (July 6, 2017), https://www.industryweek.com/technology/world-about-undergo-even-faster-change; Clayton M. Christensen, Michael E. Raynor & Rory McDonald, *What Is Disruptive Innovation?*, HARV. BUS. REV. (Dec. 2015), https://hbr.org/2015/12/what-is-disruptive-innovation ("Many leaders of small, entrepreneurial

ways though, participants in the space are consistent in entrenching power and influence so that even innovative unicorn companies disrupting industries effectively reinforce the existing power structure and traditional influences of institutions and those of a certain pedigree.

High-growth companies looking to achieve unicorn status often seek to develop the latest innovation or game-changing product in order to disrupt the industry status quo. Some of the most famous unicorns, for example, Uber, GrubHub, and AirBnB, capitalized on smartphones and cloud-based software to disrupt taxi, food, and hotel industries by making them mobile.[42]

The ride-sharing company Uber Technologies, Inc. is a poster child for Silicon's Valley endless quest for innovation.[43] Uber has been so prominent in the startup economy that the drastic changes in industries as a result of it have been referred to as "uberisation."[44] Uber is a company that revolutionized the taxi industry, promoting environmentally friendly ride-sharing and ostensibly creating new jobs along the way.[45] Since its official launch in 2011 and until its initial public offering in 2019, critics of the company have argued that constantly pushing for growth, innovation, and profit led the company to mistakes and deviations from its original mission.[46] Uber has been criticized for its unfair treatment of drivers, for disrupting the taxicab business, for increasing traffic congestion, and for fostering a toxic workplace culture where retaliation and sexual harassment festered.[47] The company has also been criticized for its aggressive strategy in dealing with taxi regulators and for other potentially unlawful practices.[48] The company most recently came under fire for neglecting and exploiting its drivers, since Uber maintains and lobbies for the position that its drivers are independent contractors and therefore not eligible for the protections that an employer-employee relationship provides.[49] Further, Uber

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companies praise [disruptive innovation] as their guiding star; so do many executives at large, well-established organizations, including Intel, Southern New Hampshire University, and Salesforce.com.").

42. KC Karnes, *5 Disruptive Apps and How They Changed Their Industries*, CLEVERTAP (Nov. 5, 2019), https://clevertap.com/blog/disruptive-apps/; *see also* David Touve & Gosia Glinska, *Fact or Fiction? Debunking the Founder Myth*, UVA DARDEN: IDEAS TO ACTION (Sept. 12, 2019), https://ideas.darden.virginia.edu/fact-or-fiction.

43. Fan, *supra* note 9, at 633 ("Uber is the poster child for unicorns.").

44. Simon Jack, *Now What Next for Uberisation?*, BBC NEWS (Sept. 22, 2017), https://www.bbc.com/news/business-41359327 ("Uberisation has come to mean the turning of traditional service industries on their head, by providing a technological platform to match users and providers on a massive scale.").

45. Martin Luenendonk, *7 Strategies Uber Is Using to Disrupt the Taxi Industry*, CLEVERISM (Feb. 16, 2018), https://www.cleverism.com/strategies-uber-is-using-to-disrupt-the-taxi-industry/; *see About Us*, UBER, https://www.uber.com/us/en/about/ (last visited May 21, 2021).

46. *See* Farhad Manjoo, Opinion, *The Uber I.P.O. Is a Moral Stain on Silicon Valley*, N.Y. TIMES (May 1, 2019), https://www.nytimes.com/2019/05/01/opinion/uber-ipo.html.

47. *See id.*

48. Mike Isaac, *Uber's C.E.O. Plays with Fire*, N.Y. TIMES (Apr. 23, 2017), https://www.nytimes.com/2017/04/23/technology/travis-kalanick-pushes-uber-and-himself-to-the-precipice.html?module=inline.

49. *See* Michael Hiltzik, *Column: With Prop. 22, Uber and Lyft Used Their Wealth to Reshape Labor Law in Their Sole Interest*, L.A. TIMES (Nov. 4, 2020, 12:26 PM), https://www.latimes.com/business/story/2020-11-04/uber-lyft-proposition-22.

drivers are not paid a living wage.[50] Arguably, its environmental arguments have not yet been made clear; while certainly ride-sharing has increased and may have encouraged some to forego a vehicle, vehicle ownership has increased in cities where Uber and Uber's competitor, Lyft, are popular.[51] Research shows that ride-hailing growth has led to more traffic and less transit use in major American cities—not the reverse that was hoped for.[52]

Uber and Lyft combined forces on lobbying efforts for an exemption from California's A.B. 5 law. An exemption would allow the rise share companies to continue to treat their drivers as employees rather than independent contractors. Their lobbying efforts led to the most expensive campaign in California history.[53] In November 2020, California voters passed Proposition 22, exempting drivers and other gig economy workers from A.B. 5 and classifying them as independent contractors.[54] On the one hand, Uber and Lyft are lauded as innovating companies who have disrupted an entire industry, but on the other hand, they spent record amounts of money to lobby to maintain social and racial inequities, lobbying against a law that would have offered drivers minimum wage, overtime pay, workers' compensation, unemployment insurance, and paid sick leave.[55] Yet, because of Uber's success, founders of other startups seeking to replicate its success and investors backing those founders look to Uber as the "blueprint."

A. HOMOGENEITY AND THE EFFECT OF LACK OF DIVERSITY

The startup world—its investors and entrepreneurs—is a mostly homogenous, white and male community.[56] Intentions aside, the startup space

50. *See* Shannon Bond, *Uber and Lyft to Continue Treating Drivers as Independent Contractors*, NPR (Nov. 4, 2020, 4:02 PM), https://www.npr.org/2020/11/04/931435959/uber-and-lyft-to-continue-treating-drivers-as-independent-contractors.

51. *See* BRUCE SCHALLER, SCHALLER CONSULTING, THE NEW AUTOMOBILITY: LYFT, UBER AND THE FUTURE OF AMERICAN CITIES 2 (2018), http://www.schallerconsult.com/rideservices/automobility.pdf ("TNCs [transportation network companies] added billions of miles of driving in the nation's largest metro areas at the same time that car ownership grew more rapidly than the population.").

52. *Id.* ("Shared ride services . . . while touted as reducing traffic, in fact add mileage to city streets. They do not offset the traffic-clogging impacts of private ride TNC services like UberX and Lyft.").

53. Sara Ashley O'Brien, *Prop 22 Passes in California, Exempting Uber and Lyft from Classifying Drivers as Employees*, CNN (Nov. 4, 2020, 4:02 PM), https://www.cnn.com/2020/11/04/tech/california-proposition-22/index.html.

54. *Id.*

55. Uber exemplifies the innovation paradox in Silicon Valley. It is a company that literally transformed an entire industry, reshaping transportation across the globe, and also sparked the transformation of many other industries as startups inspired by Uber created on-demand services in other spaces. Yet despite all of its innovation, the technology company has been plagued by sexist and toxic culture in the workplace and took an approach to paying its labor force that many would argue entrenches the status quo. *See supra* notes 47, 49–50 and accompanying text.

56. *See* Kim-Mai Cutler, *Here's a Detailed Breakdown of Racial and Gender Diversity Data Across U.S. Venture Capital Firms*, TECHCRUNCH (Oct. 6, 2015, 7:00 AM), https://techcrunch.com/2015/10/06/s23p-racial-gender-diversity-venture/?guccounter=1.

has been dominated by middle and upper-class white males.[57] This issue is distinct from the pattern matching and implicit bias described below. The distinct point made by this Subpart is that those involved in the startup ecosystem are likely white and male. According to one analysis, 77.1% of venture-backed founders are white and 90.8% of them are men.[58] More white men than white women and more white men than men of color are involved in entrepreneurship.[59] As with entrepreneurs of color, women founders face an uphill battle when convincing investors of the value of their products and their ideas.[60] Race and gender play a role in entrepreneurship, but increasingly class is proving a factor as well.[61] Just under half of venture capitalists attended either Harvard or Stanford.[62] "The homogeneity is geographic, too: more than 90% of venture capitalists surveyed lived on the East or West coasts" according to the National Venture Capital Association.[63] Little data is known about the representation of angel investors or friends and family investors. In their report, *Access to Capital for Entrepreneurs: Removing Barriers*, the Kauffman Foundation looks at geographic barriers to accessing capital:

57. Mary Ann Azevedo, *Untapped Opportunity: Minority Founders Still Being Overlooked*, CRUNCHBASE (Feb. 27, 2019), https://news.crunchbase.com/news/untapped-opportunity-minority-founders-still-being-overlooked/.

58. RATEMYINVESTOR, DIVERSITY IN U.S. STARTUPS 7–8 (2018), https://ratemyinvestor.com/DiversityVCReport_Final.pdf.

59. *See id.* at 1, 8–10.

60. Lynn Perkins, *How to Secure VC Funding When You're the Only Woman in the Room*, ENTREPRENEUR: WOMEN (July 31, 2018), https://www.entrepreneur.com/article/316019; *see also* Press Release, Morgan Stanley, Access to Capital Survey: Investors Perceive Funding Landscape as Balanced, Despite a Substantial Gap in Their Actual Investments in Female and Multicultural Entrepreneurs (Dec. 11, 2018), https://www.morganstanley.com/press-releases/access-to-capital-survey--investors-perceive-funding-landscape-a ("Nearly 40% of men say that investing in women-owned businesses is not a priority at all, compared to only 7% of female investors. Similarly, 31% of white investors say they do not prioritize investing in minority-owned businesses. Investors report being less likely to connect to the sectors that female and multicultural entrepreneurs serve. Nearly half of investors (47%) cite an entrepreneur's sector as a compelling reason why they invest in businesses in general, but that number drops to 36% for women-owned businesses and 33% for minority-owned businesses."). Further, the survey finds that investors' perception is that multicultural and women business owners get the right amount, or more, of capital they deserve to run and grow their businesses. *The Trillion-Dollar Blind Spot*, MORGAN STANLEY (Dec. 11, 2018), https://www.morganstanley.com/ideas/trillion-dollar-blind-spot-infographic/. The reality is that investors report capitalizing multicultural and women-owned businesses at 80% less than businesses overall. *Id.*

61. "Data from 1996 to 2017 show that men are consistently more likely to start businesses each month than women, and 2017 was the first year in which the rate of black and white new entrepreneurs was the same." VICTOR HWANG, SAMEEKSHA DESAI & ROSS BAIRD, KAUFFMAN FOUND., ACCESS TO CAPITAL FOR ENTREPRENEURS: REMOVING BARRIERS 1 (2019), https://www.kauffman.org/wp-content/uploads/2019/12/CapitalReport_042519.pdf.

62. Simone Stolzoff, *Venture Capital's Diversity Problem in Two Words: Alma Mater*, QUARTZ (July 31, 2018), https://qz.com/1343912/venture-capitals-diversity-problem-in-two-words-alma-mater/.

63. Elizabeth Scharpf, *This Is Not a Typo: Only 3% of Americans Are Legally Allowed to Invest in Start-Ups*, Quartz (June 22, 2015), https://qz.com/431198/this-is-not-a-typo-only-3-of-americans-are-legally-allowed-to-invest-in-start-ups/.

> Five metro areas—New York City, Miami, Los Angeles, Houston, and Dallas—were estimated to have contributed to 50 percent of net new firm creation between 2010 and 2014.
>
> In addition, VC industry data reveals considerable geographic and industry concentration. Close to 80 percent of about $21.1 billion in VC funding in the first quarter of 2018 was disbursed in five regional clusters—San Francisco (North Bay Area), Silicon Valley (South Bay Area), New England, New York City metro, and LA/Orange County—with slightly more than 44 percent in the North and South Bay Areas.[64]

While public companies face public scrutiny and advocacy around the composition of their board of directors, private companies face less scrutiny. Indeed, although there is less publicly available information on private board diversity data, there is a lack of gender and racial diversity on private company boards.[65]

A study of private board diversity data was produced by a collaboration between Crunchbase and Him for Her.[66] In 2020, the researchers looked at the boards of the most heavily funded U.S.-based private venture-backed companies and found that 49% of companies did not have a woman on the board.[67] "Women held 11 percent of board seats, up from 7 percent the previous year."[68] Executives and investors compose 75% of director seats, of which 8% are held by women.[69] Their initial analysis of racial and ethnic revealed that "only 3 percent of board seats were held by women of color, compared with an estimated 18 percent held by men of color; and 81 percent of companies don't have a woman of color on the board at all."[70] Nearly half of private company boards are all male.[71] "The ratio of men to women in private-company boardrooms is roughly 9-to-1."[72] According to the researchers, at current rates, "it will take a decade for private company boards to achieve gender parity."[73] Most women directors are the only women on the board. "Among the roughly half of boards that include any women, 66 percent include just one woman."[74] Of the private company boards studied, only 18% included two or more women.[75] "While research suggests that boards need at least three women to capture the full

64. HWANG ET AL., *supra* note 61, at 7 (footnote omitted).

65. *See* Jennifer S. Fan, *Innovating Inclusion: The Impact of Women on Private Company Boards*, 46 FLA. ST. U. L. REV. 345, 345 (2019).

66. Ann Shepherd & Gené Teare, *2020 Study of Gender Diversity on Private Company Boards*, CRUNCHBASE (Mar. 1, 2021), https://news.crunchbase.com/news/2020-diversity-study-on-private-company-boards/.

67. *Id.*

68. *Id.*

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.*

75. *Id.*

economic benefits of diversity, only 6 percent of the companies studied met this criteria."[76]

Among the country's largest companies, a 2018 study of *Fortune* 500 boards found 4.6% of directors were "minority women."[77] Fewer than one in five of the companies studied had a single woman of color in the boardroom.[78] According to the Crunchbase and Him for Her Report:

> Directors on private-company boards can be classified in three groups: executive directors, investor directors and independent directors. CEOs, co-founders and any members of the management team who hold board seats are considered executive directors, which make up 22 percent of the board seats within the companies studied.
>
> As venture-backed companies raise outside funding, investors often take seats on the board. Within the study data, investor directors make up the largest pool of board members for venture-backed companies, with 53 percent of seats.[79]

The study found that "[b]oards can improve diversity by adding independent directors at an earlier stage and drawing from a diverse candidate pool sourced beyond the personal networks of sitting directors."[80]

Research on homogenous groups shows that the more a person looks like ourselves, the more we are willing to trust them.[81] We put too much trust in the judgment of people who look similar to us. Homogenous groups feel more comfortable and don't generate enough skepticism.[82] Diverse groups, in contrast, are more likely to ask tough questions and uncover important facts. Diversity increases innovation and leads to increased profits.[83]

Inequity is likely to occur when there is such pervasive homogeneity.[84] The prevalence of homogeneity in Silicon Valley exacerbates the problem of implicit

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76. *Id.*

77. DELOITTE, MISSING PIECES REPORT: THE 2018 BOARD DIVERSITY CENSUS OF WOMEN AND MINORITIES ON *FORTUNE* 500 BOARDS 17 fig.6 (2019), https://www2.deloitte.com/us/en/pages/center-for-board-effectiveness/articles/missing-pieces-fortune-500-board-diversity-study-2018.html (click "Download the PDF" to download).

78. Shepherd & Teare, *supra* note 66.

79. *Id.*

80. *Id.*

81. Steve Kelman, *Group Diversity and the Accuracy of Group Judgments*, FWC: THE LECTERN (Dec. 14, 2015, 12:29 PM), https://fcw.com/blogs/lectern/2015/12/kelman-group-diversity.aspx; Harry Farmer, Ryan McKay & Manos Tsakiris, *Trust in Me: Trustworthy Others Are Seen as More Physically Similar to the Self*, 25 PSYCH. SCI. 290, 290–92 (2014) ("Coupled with research suggesting that people have overly positive self-views, including viewing themselves as more trustworthy than the average person, these findings suggest that people favor those who are physically similar to themselves. Indeed, facial similarity leads to increased attributions of trustworthiness and increased cooperation in both trust games and common-good games." (citations omitted)).

82. *See* MALCOLM GLADWELL, TALKING TO STRANGERS (2019) (writing that our cognitive biases tend toward believing what others say is the truth with little natural skepticism).

83. *See* Katherine W. Phillips, *How Diversity Makes Us Smarter*, SCI. AM. (Oct. 1, 2014), https://www.scientificamerican.com/article/how-diversity-makes-us-smarter/; Fan, *supra* note 65.

84. *See generally* BUCK GEE & DENISE PECK, ASCEND FOUND., THE ILLUSION OF ASIAN SUCCESS: SCANT PROGRESS FOR MINORITIES IN CRACKING THE GLASS CEILING FROM 2007–2015 (2017), https://cdn.ymaws.com/

bias and pattern matching that is described below. The next Subpart discusses how the culture of fundraising, pattern matching and implicit bias play a role in the chase for the next unicorn.

B. Fundraising and Pattern Matching

The pursuit of unicorn status is comparable to the California gold rush and exemplifies a culture of pursuing growth at all costs.[85] The mentality of trying to get a piece of that gold, metaphorically speaking, is what drives the culture.[86] In order to grow fast, entrepreneurs rely on private capital to finance their goals. Capital raising, and the private market that supports it, is big business and probably the number one driver of startup culture.[87] For a high-growth startup venture, most founders are in a constant cycle of fundraising and prototyping for the product or service offered by their company. Founders typically start their company using their own funds, in a practice that is known as "bootstrapping."[88] Once they have used the available funds and resources available to them, they may turn to their friends and family to raise additional capital.[89] Where available to them, founders may often ask their parents to take out a second mortgage on their home or the founder may mortgage her own home.[90] It will be discussed in more detail below, but it is worth noting here how history, racism, and the racial wealth gap affect who typically can bootstrap and can access these initial financial resources.[91] Many entrepreneurs of color cannot tap into any

www.ascendleadership.org/resource/resmgr/research/theillusionofasiansuccess.pdf (pointing to distinctive diversity challenges for each racial and gender cohort in Bay Area technology companies and showing that the racial gap is worsening).

85. The California gold rush occurred during the middle of the nineteenth century and led directly to the settlement of California. Mike McPhate, *How the California Gold Rush Echoes in Silicon Valley*, Medium: Calif. Sun (Jan. 23, 2018), https://medium.californiasun.co/gold-rush-34072fd9d467.

86. *See id.* (highlighting the Californian tolerance for failure in capitalist enterprise, which the author asserts stems from California's encounter with gold-mining).

87. *See generally* Nat'l Venture Cap. Ass'n, Venture Impact: The Economic Importance of Venture Capital-Backed Companies to the U.S. Economy 9 (5th ed. 2009), http://faculty.msmc.edu/hossain/grad_bank_and_money_policy/economic%20importance%20of%20venture%20capital%20backed%20companies.pdf.

88. R.L. Adams, *8 Bulletproof Ways to Bootstrap Your Business*, Entrepreneur (Dec. 15, 2017), https://www.entrepreneur.com/article/305600 (defining bootstrapping in business as "self-funding through pre-existing cash flow and being critical of outgoing expenses").

89. *See* Alejandro Cremades, *How Funding Rounds Work for Startups*, Forbes (Dec. 26, 2018, 5:14 AM), https://www.forbes.com/sites/alejandrocremades/2018/12/26/how-funding-rounds-work-for-startups/#13bcd33b7386; *The Ins and Outs of Raising Money from Friends and Family*, Entrepreneur, https://www.entrepreneur.com/article/228103 (last visited May 21, 2021).

90. *See* Gene Marks, *Entrepreneurs Are Great, But It's Mom and Dad Who Gave Them Their Start*, Guardian (Jan 31, 2021, 7:00 AM), https://www.theguardian.com/business/2021/jan/31/small-business-entrepreneurs-success-parents; *Should Parents Fund a Child's Startup Company?*, Tarantino L. Firm, LLP (Dec. 5, 2019), https://www.tarantinolaw.com/blog/2019/12/should-parents-fund-a-childs-startup-company/; Krista Tuomi, *Mortgage Financing: Dangerous Headwinds for Startups*, VC List (May 1, 2020), https://vc-list.com/mortgage-financing-startups/.

91. Keenan Beasley, *For Black Entrepreneurs, the Racial Wealth Gap Makes Finding Funding Nearly Impossible*, Fast Co. (July 23, 2020), https://www.fastcompany.com/90531094/for-black-entrepreneurs-the-racial-wealth-gap-makes-finding-funding-nearly-impossible ("[A] historical product of the racial wealth gap—

meaningful resources to bootstrap their venture. After founders have exhausted the resources of their friends and family, founders might then turn to angel investors or venture capital investors for additional capital.[92] For high-growth companies, venture capital investment can prove instrumental for startup success since venture capital-backed companies are more likely to succeed than non-venture backed firms.[93]

For each round of funding, the valuation of the company becomes increasingly important as the valuation reflects the value of the investor's investment.[94] Valuation is a driver towards investment because a higher valuation increases the value of the investor's investment. It should be noted that high valuation does not necessarily correlate to a strong business model nor does it speak to the venture's profitability. Although a company may have hit a billion-dollar valuation on the private market, some unicorn companies may not have a working business model; the company may or may not even be profitable, yet investors believing in a company's mission, its potential, or its founder may clamor to invest and, in turn, push up the valuation.[95] In fact, many unicorn companies are often not profitable.[96] Several unicorn companies that captured our collective imagination we now know did not have a clear plan for profitability, such as Uber, Palantir, and Zenefits,[97] for example. The influx of capital and funding propelled these companies to success, not because they were the most efficient or capable company, demonstrating that investors are not

the inherent disparity in median wealth between people of different races—most Black entrepreneurs do not have access to a network that can provide them with a type of investment known as a "Friends and Family" round.").

92. *See* Cremades, *supra* note 89 (explaining that the pre-seed round is often the "friends and family" round, and more angel investors come in during the seed round).

93. Darian M. Ibrahim, *The (Not So) Puzzling Behavior of Angel Investors*, 61 VAND. L. REV. 1405, 1411 (2008).

94. *See* Nathan Reiff, *Series A, B, C, Funding: How It Works*, INVESTOPEDIA, https://www.investopedia.com/articles/personal-finance/102015/series-b-c-funding-what-it-all-means-and-how-it-works.asp (Mar. 5, 2020).

95. According to Pitchbook, "[s]ixty-four percent of the 100+ companies valued at more than $1 billion to complete a VC-backed IPO since 2010 were unprofitable, and in 2018, money-losing startups actually fared better on the stock exchange than money-earning businesses." Kate Clark, *Unicorns Aren't Profitable, and Wall Street Doesn't Care*, TECHCRUNCH (Mar. 26, 2019, 1:25 PM), https://techcrunch.com/2019/03/26/unicorns-arent-profitable-wall-street-doesnt-care; CAMERON STANFILL & JORDAN BECK, PITCHBOOK, SEARCHING FOR VALIDATION: AN ANALYSIS OF VALUATION PERFORMANCE FOR $1 BILLION+ VC-BACKED EXITS 10–11 (2019), https://files.pitchbook.com/website/files/pdf/PitchBook_1Q_2019_Analyst_Note_Searching_for_Validation.pdf.

96. *See* Jeffery Lee Funk, *Only 6 of 73 Unicorn Startups Are Profitable, and None Did Recent IPOs*, MEDIUM (Nov. 23, 2020), https://jeffreyleefunk.medium.com/only-6-of-73-unicorn-startups-are-profitable-and-none-did-recent-ipos-287d5c7ac8d0 ("In summary, only 6 of 73 Unicorns had profits in 2019 (and 2020) and most of the profitable Unicorns did IPOs many years ago. This suggests that privately-held Unicorns, ones that have yet to do IPOs, are likely unprofitable."); Clark, *supra* note 95.

97. Zenefits is a company that created human resource software and paid millions of dollars in fines to California regulators and the SEC because its employees sold insurance without proper licenses. *See* Heather Somerville, *Zenefits and Co-founder Parker Conrad to Pay SEC Fine of Nearly $1 Million*, REUTERS (Oct. 26, 2017, 4:14 PM), https://www.reuters.com/article/us-zenefits-sec/zenefits-and-co-founder-parker-conrad-to-pay-sec-fine-of-nearly-1-million-idUSKBN1CV3NS.

necessarily looking for profitability, but the next opportunity for the most return on investment.[98]

Fundraising for a new entrepreneurial venture is challenging in that the founder has to balance the everyday demands of starting a venture and at the same time seek cash to maintain that venture. Silicon Valley is flush with ambitious, unicorn-seeking founders who meet that challenge by massaging the truth to lure investors and investors who may accept incomplete information in the name of innovation.[99] In the early days in the life of a startup, the founder can likely be found creating her company's product or services. In addition to moving the company from a big idea to a tangible product or service, the founder is also likely to be in the process of fundraising to finance the big idea. It is often common for founders to start fundraising even before the product or service has launched.[100] This dual track of fundraising on the basis of a big idea while creating a tangible manifestation of the big idea has profound implications for Black and other non-traditional entrepreneurs. One of those implications is that, in reality, founders of color are typically required to have a viable product before fundraising. Adding to that is that investors, who are largely white, are not likely to take notice of founders of color. This failure could be explained by several factors that include pattern matching and implicit bias, but also cultural factors, reflecting a difference in cultural problems, solutions, surroundings, and resources.[101] There is an inherent tension in capital raising as entrepreneurs seek to quickly enter the market and scale their enterprises, while innovating and defining a product or service at the same time.

Fundraising culture is built around obfuscation of facts or the use of what has been coined "vaporware."[102] This opaqueness is relatively common among

98. Clark, *supra* note 95; *see* J.B. Maverick, *Is Profitability or Growth More Important for a Business?*, INVESTOPEDIA, https://www.investopedia.com/ask/answers/020415/what-more-important-business-profitability-or-growth.asp (Jan. 30, 2020) ("Profitability and growth go hand-in-hand when it comes to success in business. Profit is key to basic financial survival as a corporate entity, while growth is key to profit and long-term success. Investors should weigh each factor as it relates to a particular company.").

99. *See generally* Mary Jo White, Chair, SEC, Keynote Address at the SEC-Rock Center on Corporate Governance Silicon Valley Initiative (Mar. 31, 2016), https://www.sec.gov/news/speech/chair-white-silicon-valley-initiative-3-31-16.html ("Nearly all venture valuations are highly subjective. . . . We continue to see instances of public companies and their senior executives manipulating their accounting to meet various expectations and projections.").

100. *See* Kate Endress, *How to Do Seed Fundraising Right*, VENTUREBEAT (Sept. 2, 2012, 8:30 AM), https://venturebeat.com/2012/09/02/how-to-do-fundraising-right-on-a-seed-round/.

101. Norman, *supra* note 23.

102. The term "vaporware" was coined in the 1980s when software companies would hype their product to obtain funding often obscuring the reality of the company's progress. *See* Robert A. Prentice & John H. Langmore, *Beware of Vaporware: Product Hype and the Securities Fraud Liability of High-Tech Companies*, 8 HARV. J.L. & TECH. 1, 1–3 (1994). When applied in the context of the startup world, it is a term used to describe marketing strategy to promote a brand, product, or founder in the pre-money or pre-seed stage, typically meaning that the promotion is "little more than hot air." Joel KO, *Opinion: Why Startups Need More Vaporware and the 'Elon Musk Effect' to Innovate*, TECHINASIA (May 26, 2017), https://www.techinasia.com/talk/time-more-vaporware.

founders and is often accepted by and even encouraged by investors.[103] The idea is that founders create aspirational forecasts and optimistic projections to present to investors and potential investors. Founders are hoping that their mild deception will be overlooked and forgiven once they have made their investors' money back at a high return.[104] In turn, investors are hoping to make money at often outsized rates of return. It is therefore not uncommon for investors to believe in a white founder and invest in a product or services with little evidence of success or promises of future success.[105] On the other hand, founders of color are expected to provide a minimal viable product before pitching to investors.[106]

This environment creates a scenario where the investor is not always in complete possession of the facts related to their investment. Because there is little or no track record and often no product, investors might make investment decisions based on instinct or their gut. The effect of relying on one's gut is that investors may revert to heuristics or rely upon mental short-cuts to make investment decisions, meaning that investors default to pattern matching in how they determine which founder or startup to invest in. Valuing innovation and disruption means that funding and support happens at an unduly early stage, resulting in the entire ecosystem relying on heuristics from the start.

In the absence of concrete, tangible, and objective projections, forecasts, or products, the investor must make investment decisions based on their belief in the founder or on gut instinct.[107] The import of this phenomenon is that often investment decisionmaking is tied to implicit bias[108] and pattern matching,[109]

103. Robert Prentice, *Vaporware: Imaginary High-Tech Products and Real Antitrust Liability in a Post-Chicago World*, 57 OHIO ST. L.J. 1163, 1174 (1996) (discussing the utility of vaporware announcements).

104. Most investors seek no less than 20% to 40% return on their investment. *See What Is Your Potential 'Return on Investment' for an Angel Investor?*, VENTURE GIANTS (May 22, 2020), https://www.venturegiants.com/what-is-your-potential-return-on-investment-for-an-angel-investor ("Most experienced Angel Investors will expect no less than 31–40% annual returns on their early stage and start up angel investments."); *see also* Bob Zider, *How Venture Capital Works*, HARV. BUS. REV. (Nov.–Dec. 1998), https://hbr.org/1998/11/how-venture-capital-works ("In return for financing one to two years of a company's start-up, venture capitalists expect a ten times return of capital over five years.").

105. *See generally* Interview by Sally Smith Hughes with Donald T. Valentine, Founder, Sequoia Cap., in Berkeley, Cal. (Oct. 20, 2009), https://digitalassets.lib.berkeley.edu/roho/ucb/text/valentine_donald.pdf.

106. Norman, *supra* note 23.

107. Paul Gompers, William Gornall, Steven N. Kaplan & Ilya A. Strebulaev, *How Do Venture Capitalists Make Decisions?* 3 (Nat'l Bureau of Econ. Rsch., Working Paper No. 22587, 2016), https://www.nber.org/papers/w22587.pdf (confirming through survey work that "VCs consider factors that include the attractiveness of the market, strategy, technology, product or service, customer adoption, competition, deal terms and the quality and experience of the management team. The nature of the entrepreneurial team is an important component of the sourcing and screening process").

108. *See* Melissa De Witte, *Venture Capital Funds Led by People of Color Face More Bias the Better They Perform, Stanford Researchers Find*, STAN. NEWS (Aug. 12, 2019), https://news.stanford.edu/2019/08/12/race-influences-professional-investors-judgments ("In their evaluations of high-performing venture capital funds, professional investors rate white-led teams more favorably than they do black-led teams with identical credentials . . . .").

109. Cat Zakrzewski, *VC Focus: Venture Industry's 'Pattern Matching' Drives Bias, Critics Say*, WALL ST. J. (Oct. 30, 2017, 9:26 AM), https://www.wsj.com/articles/vc-focus-venture-industrys-pattern-matching-drives-bias-critics-say-1509369994; Lisa Fisher, *Stemming Implicit Bias in High-Tech STEM: The Vision of Project Include*, 12 J. APPLIED SOC. SCI. 127 (2018).

which has implications for racial, gender, and class dynamics. Studies have proven that when a person looks similar to ourselves, we are inclined to automatically believe they are more trustworthy.[110] Therefore, a white male investor is more likely to invest in a white male founder than, for example, a female founder of color. This is true, even if the business has high growth potential and high sales; the reality is that investors tend to bring founders into their portfolio that look like themselves, have the same status, and have the same levels of education.[111] Additionally, physical appearance can guide donation or investment decisions not only in person-to-person networks, but even in an anonymous and seemingly democratic vehicle such as a crowdfunding campaign.[112] This phenomenon is similar to the concept of "trust economics," a longstanding theory about creating systems where trust becomes a placeholder for money.[113] Investors rely on trust as they develop their financial relationships as startup investment opportunities come from a network of trusted business associates.[114] What makes for a trusted relationship is informed by sources such as the investor's family and friends, many of whom fit a certain demographic. This "network of trust" serves an important screening function for who gets funding and who does not.[115] Essentially these investors are deciding who is like them and therefore worthy of both the investors' trust and money. Trust economics as an investment principle within the startup ecosystem favors white entrepreneurs, since investors are likely to also be white.[116] These important decisions based on trust are made regardless of metrics and in the face of contrary metrics since women-led businesses are more profitable[117] and diverse teams are more profitable.[118] Even though the empirical analysis supports the

110. Farmer et al., *supra* note 81, at 290–92; Damian A. Stanley, Peter Sokol-Hessner, Mahzarin R. Banaji & Elizabeth A. Phelps, *Implicit Race Attitudes Predict Trustworthiness Judgments and Economic Trust Decisions*, 108 PROC. NAT'L ACAD. SCI. 7710, 7711 (2011).

111. *See* KATHRYN FINNEY, THE REAL UNICORNS OF TECH: BLACK WOMEN FOUNDERS 7 (2016).

112. *See* Joe Pinsker, *How to Succeed in Crowdfunding: Be Thin, White, and Attractive*, ATLANTIC (Aug. 3, 2015), http://www.theatlantic.com/business/archive/2015/08/crowdfunding-success-kickstarter-kiva-succeed/400232/ ("Regardless of whether such bias is conscious or unconscious, the researchers had a guess as to why some users were being swayed by physical characteristics. 'We argue that implicit discrimination may characterize lending decisions on Kiva [a crowdfunding site], because of the dizzying array of choices available and the lack of any obvious decision criteria for making a funding choice,' they write. Without anything else to go on, users default to old stereotypes.").

113. *The Trust Economy*, ATLANTIC (2017), https://www.theatlantic.com/sponsored/charles-schwab-2017-nt/the-trust-economy/1290.

114. Ibrahim, *supra* note 93, at 1432.

115. *Id.*

116. *See* DELOITTE, VC HUMAN CAPITAL SURVEY 7 (3d ed. 2021), https://www2.deloitte.com/us/en/pages/audit/articles/diversity-venture-capital-human-capital-survey.html (click "Download the PDF" to download).

117. Katie Abouzahr, Matt Krentz, John Harthorne & Frances Brooks Taplett, *Why Women-Owned Startips Are a Better Bet,* BOS. CONSULTING GRP. (June 6, 2018), https://www.bcg.com/publications/2018/why-women-owned-startups-are-better-bet ("[B]usinesses founded by women ultimately deliver higher revenue—more than twice as much per dollar invested—than those founded by men, making women-owned companies better investments for financial backers.").

118. Sundiatu Dixon-Fyle, Kevin Dolan, Vivian Hunt & Sara Prince, *Diversity Wins: How Inclusion Matters*, MCKINSEY & CO. (May 19, 2020), https://www.mckinsey.com/featured-insights/diversity-and-

financing of more diverse entrepreneurs, the market still invests in a pattern that benefits white male entrepreneurs.

Further, when an investor evaluates a founder, it is common for the investor to evaluate both the founder and the company based on a frame of reference from past deals, other successful founders, or deals that they have heard about. Using this frame of reference as a basis for investment decisionmaking is known as "pattern matching." In the entrepreneurial ecosystem, pattern matching is a term used to explain the practice of investors, primarily angel or venture capital investors, to evaluate startups and entrepreneurs based on what has worked in the past.[119] For example, John Doerr, a famous investor and partner in the venture capital firm of Kleiner Perkins, illustrated this point in a public presentation when he said that the most successful tech entrepreneurs are "white, male, nerds."[120] He then went on to say, "That correlates more with any other success factor that I've seen in the world's greatest entrepreneurs. If you look at [Amazon founder Jeff] Bezos, or [Netscape founder Marc] Andreessen, [Yahoo co-founder] David Filo, the founders of Google, they all seem to be white, male, nerds who've dropped out of Harvard or Stanford and they absolutely have no social life. So, when I see that pattern coming in—which was true of Google—it was very easy to decide to invest."[121] It is unlikely given the statistics about entrepreneurs of color in the startup space that investors have a frame of reference for a Black founder or a founder of color. Rather investors look for founders that pattern match to previous unicorn founders. Because the investor has no frame of reference for a Black founder, the founder does not match the pattern, and it is unlikely that the investor will take a chance and invest in a nontraditional entrepreneur.[122]

The next Subpart describes how Silicon Valley thrives on the mythology surrounding a founder and how the culture of celebrating the next messianic "wunderkind" is not only dangerous, it reinforces the pattern matching described above and surfaces how the brilliant founder myth was one of the drivers of Holmes' success at fundraising.

C. The Cult of Personality and the Myth of the Brilliant Founder[123]

Silicon Valley has historically fed in to cultivating a mystique around its legendary founders—Steve Jobs, Bill Gates, Mark Zuckerberg, and Elon Musk,

inclusion/diversity-wins-how-inclusion-matters# ("The most diverse companies are now more likely than ever to outperform less diverse peers on profitability.").

119. *See* Zakrzewski, *supra* note 109.

120. Scott Austin, *Doerr and Mortiz Stir VCs in One-on-One Showdown*, WALL ST. J. (May 8, 2008, 11:59 PM), https://www.wsj.com/articles/SB121025688414577219.

121. *Id.*

122. *See* Norman, *supra* note 23.

123. *See* Touve & Glinska, *supra* note 42 ("[The myth of the brilliant founder] goes something like this: a brilliant, ambitious tech wiz—clearly born to be an entrepreneur and predictably male—has a light-bulb moment.

for example.[124] Within startup culture, there is a cult of personality that has the effect of creating a pattern of a narrow image of who can be a founder, who can sit on a board, and who can be an investor in the race to pursue a unicorn.[125] Silicon Valley culture perpetuates this cult of personality within the startup community. Arguably this myth of the brilliant founder emerged from the fabled idiosyncrasies of Steve Jobs and Mark Zuckerberg.[126] As investors start to invest in ventures, they place a primacy on finding "the next Zuckerberg" or the "next Steve Jobs."[127] In other words, they are looking to replicate the success of Facebook and of Apple and believe that it comes in the form of a founder that is white, male, and awkward like either Mark Zuckerberg or Steve Jobs.[128]

The cult of personality is a heuristic born of pattern matching. One particular pattern that is attractive to investors is the pattern match of the twenty-something-year-old Stanford or Harvard drop-out with a world-changing idea. As a result, a narrow image of who can be a game-changing founder or CEO has emerged and there is little opportunity for different perspective or different patterns. This pattern replicates elitism and structural racism by reinforcing the idea that those who would consider dropping out of Ivy League institutions are likely people who have enough money and privilege to see that choice as not

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He drops out of college and bets everything on a startup, which ends up changing the world while generating massive wealth.").

124. *See generally* Isobel Asher Hamilton, *This Doomsaying Art Exhibition Recasts Bezos, Musk, and Zuckerberg as Mythological Figures Heralding the End of Civilization*, BUS. INSIDER (Apr. 28, 2019, 12:00 AM), https://www.businessinsider.com/3-d-printed-exhibition-reimagines-bezos-musk-and-zuckerberg-as-mythological-figures-2019-4.

125. Sheila Herrling, *The Myth of the Entrepreneur*, CASE FOUND. (Nov. 17, 2015), https://casefoundation.org/blog/the-myth-of-the-entrepreneur (discussing the vast majority of celebrated startups continuing to be founded and funded by "white, well-educated, well-networked males"); Ian Hathaway, *The Myth of the Young Startup Founder*, CTR. FOR AM. ENTREPRENEURSHIP (Jan. 6, 2020), https://startupsusa.org/the-myth-of-the-young-startup-founder/ (addressing the myth of founder age and deeming founders to be much older than presumed (around mid-40s on average)).

> The vast majority of today's celebrated startups continue to be founded and funded by white, well-educated, well-networked males. Women are at the helm of 30 percent of all businesses in the US, and these businesses are leading the way in terms of hiring and growth. However, startups with women CEOs still receive only three percent of venture capital funding. Minority-owned businesses are growing at a faster clip than non-minority owned businesses, but are receiving an even smaller fraction of investments.

Herrling, *supra*; *see also* Touve & Glinska, *supra* note 42 ("Having examined the genesis stories around tech's biggest breakthroughs, Touve dispels the common misconception that entrepreneurs are born, not made. He also suggests that there are four archetypes of the iconic founder: the genius, the guru, the gambler and the gunslinger.").

126. *See* Isaac Cabe, *6 Famous Tech Gurus and Their Less-Known Crazy Habits*, CRACKED (Mar. 6, 2018), https://www.cracked.com/article_25137_6-famous-tech-gurus-and-their-less-known-crazy-habits.html; *see also* Brian Scudamore, *6 Weird Quirks of Highly Successful Entrepreneurs (and Why They Work)*, INC. (June 27, 2017), https://www.inc.com/brian-scudamore/why-oddballs-make-the-best-entrepreneurs.html.

127. *See* Doug Gross, *Who Is the Next Steve Jobs (And Is There One)?*, CNN (Oct. 3, 2012, 9:34 AM), https://www.cnn.com/2012/10/02/tech/innovation/next-steve-jobs/index.html.

128. This form of pattern matching is common in fundraising. The term "pattern-matching" originated from computer science, and it describes the matching and locating of specific sequences of data of some pattern among raw data or a sequence of tokens. *Definition: Pattern Matching*, EDUCATIVE, https://www.educative.io/edpresso/definition-pattern-matching (last visited May 21, 2021).

much of a lifelong risk. This is likely because they can always get back into an elite institution, always pay for it, their parents will support them in the interim, or they won't be perceived as irresponsible or ruining their life. Therefore, those who are considered "super smart" Ivy League dropouts with a big idea are likely going to be a white, privileged person.

Although the numbers are on the rise, successful founders of color are largely absent in entrepreneurship because of a demonstrated lack of access to capital.[129] It is not just lack of access to capital, it is also the lack of inclusion of Black founders in the space. Many entrepreneurs of color do not have access to the traditionally white, male investors and advisors that Holmes relied on for funding Theranos. Generally, white (mostly male) entrepreneurs have more access to capital than any other group.[130] Venture capital firms employ mostly white men and then invest almost exclusively in companies owned by white men.[131] One percent of American venture capital-backed founders are Black and the percentage of Black people in decisionmaking roles within venture capital is not much better.[132] These numbers are relevant given the nature and role of pattern matching and cult of personality (described below) at play in private fundraising.[133] This bias stems from barriers to early-stage capital and a lack of representation in the investing space and is perpetuated by systems of racism that destroy opportunity within communities of color.[134] Fundraising culture and practices created an inherent funding bias.[135]

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129. *See* GEE & PECK, *supra* note 84, at 3.

130. *See* Elizabeth MacBride, *Is Entrepreneurship Becoming the Purview of Upper-Class Men?*, FORBES (May 31, 2019, 2:51 PM), https://www.forbes.com/sites/elizabethmacbride/2019/05/31/is-entrepreneurship-becoming-the-purview-of-upper-class-men/#59739d0cd594 (exploring areas of access available to white males through a Kauffman Foundation report); HWANG ET AL., *supra* note 61, at 10–14.

131. Jeanette Settembre, *Venture Capitalists Still Give Most of Their Money to White Men, Study Finds*, MARKETWATCH (Feb. 13, 2019, 1:43 PM), https://www.marketwatch.com/story/venture-capitalists-still-give-most-of-their-money-to-white-men-study-finds-2019-02-13.

132. Azevedo, *supra* note 57.

133. *See* Sarah Lyons-Padilla, Hazel Rose Markus, Ashby Monk, Sid Radhakrishna, Radhika Shah, Norris A. "Daryn" Dodson IV & Jennifer L. Eberhardt, *Race Influences Professional Investors' Financial Judgments*, 116 PROC. NAT'L ACAD. SCI. 17225, 17226 (2019) ("[I]n the world of investing, high-performing teams led by people of color are a rarity, and they fail to fit the template of what a successful fund manager looks like."). Even after first getting in the door, groups stereotyped as incompetent (for example, Black people) have a harder time advancing professionally than groups stereotyped as competent (for example, white people). Because having a strong track records is inconsistent with stereotypes about funds owned by people of color, asset allocators might be unable to recognize and appropriately evaluate these teams. Instead, they may fall back on pattern matching strategies and mitigate risk by sticking with familiar options—that is to say, by continuing to invest in white and male teams.

134. *See id.* at 17225–26.

135. *See id.* While this study does not address a connection between racial bias and funding startups, it speaks to a general racial bias in fundraising practices and culture, finding that:

> At stronger performance levels, asset allocators rate White-led funds more favorably than they do Black-led funds. At weaker performance levels, asset allocators actually prefer Black-led teams to White-led teams. However, asset allocators are unlikely to invest in weaker funds, diverse or otherwise. These results suggest that beyond racial disparities in the pipeline, there are additional systemic racial disparities in how investors evaluate funds and allocate money.

Implicit bias is a form of the more general phenomenon of pattern matching. Because the line between aspiration and reality is blurred and, as described above, is likely obscured by founders to potential investors, investors rely on their gut and pattern matching, which can lead to implicit bias.[136] For example, the investor believes that the founder may be a worthy investment because the founder dresses like Mark Zuckerberg or shares idiosyncratic traits as those of Steve Jobs, and therefore the investor is willing to bet on that founder based on those characteristics.[137] The "worthy" founder likely went to the right higher education institutions, as a result has sponsors or mentors from the right echelons to endorse them, and access to financial and cultural capital. Silicon Valley's cultural practices build on the socio-economic and racial forces that have built wealth for certain populations while literally devaluing others. The import of this is that despite the emphasis that Silicon Valley places on innovation and disruption of the status quo, the culture of Silicon Valley builds on the existing dominant racial and class practices to the detriment of entrepreneurs of color. In other words, the same ways that racial, social, and class hierarchies show up in larger society, they are equally reflected in Silicon Valley. Thus, those who do not have similar characteristics as the hegemonic participants in Silicon Valley culture—that is, women and founders of color—face challenges in accessing capital.[138]

Bias in the private investment system defies the logic of capitalism.[139] There is an unrecognized downside to pattern matching and implicit bias in this space. Pattern recognition has enabled venture capitalists to mitigate risk but has also limited their profit potential. In 2016, the Center for Global Policy Solutions reported that due to discriminatory financing practices and a bias towards

Id. at 17225.

136. *See generally* Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, 185 SCI. 1124 (1974).

137. *See* Channing Hargrove, *What Was Elizabeth Holmes Trying to Prove with Those Black Turtlenecks?*, REFINERY29 (Mar. 6, 2019, 12:50 PM), https://www.refinery29.com/en-us/2019/03/226213/elizabeth-holmes-black-turtleneck-suit-steve-jobs-style ("Reportedly, Holmes was so obsessed with owning the exact Issey Miyake black turtleneck Jobs wore in his iconic key note presentations (and every other day of his working life) that she reportedly tracked down and stocked up on the pieces, which were reissued in 2017 for $270."). The general trend is to dress like Zuckerberg or Jobs to establish a brand identity.

138. *See* Ben Hecht, *Why Entrepreneurs of Color Are Struggling*, BLOOMBERG (Apr. 23, 2018, 8:26 AM), https://www.citylab.com/equity/2018/04/closing-the-racial-startup-gap/557012 ("The systems in place for identifying, fostering and supporting entrepreneurs favor white males from the start. A recent study from Stanford economist Raj Chetty and his colleagues at the Equality of Opportunity Project found that people of color, women, and children from low-income families become inventors at a fraction of the rate of white men, often despite demonstrating higher performance at a young age."); *see also* KAUFFMAN FOUND., INCLUDING PEOPLE OF COLOR IN THE PROMISE OF ENTREPRENEURSHIP (2016), https://www.kauffman.org/-/media/kauffman_org/resources/2016/including-people-of-color-in-the-promise-of-entrepreneurship-pdf.pdf.

139. Christopher Steiner, *Biases: The Biggest Force Holding Back Startup Investors*, FUNDERSCLUB: BLOG (Oct. 26, 2016), https://fundersclub.com/blog/2016/10/26/biases-biggest-force-holding-back-startup-investors (providing a statement from K2 Global Managing Partner Minal Hasan) ("Pattern recognition stems from a fear of investing in people or spaces that are new or unknown. . . . [Y]ou can lose out on some of the most innovative and game-changing technologies because they're either unfamiliar to you, or because they don't fit a neat mold.").

companies primarily operated by white males, America is losing out on over 1.1 million minority-owned businesses, and as a result, foregoing over 9 million potential jobs and $300 billion in collective national income.[140]

D. Applying Fundraiser and Founder Incentives to Theranos and Other Unicorn Companies

Research shows that board diversity can be an effective safeguard against bad apples.[141] Diversity helps boards prevent problems and prevents comfortability with business practices as well as opens them up to new ideas.

> Companies with more gender diversity on their boards, for example, are less likely to reissue financial statements because of error or fraud. Diverse groups also tend to consider more factors when making a decision. Racially mixed juries deliberate longer, share more information, discuss a wider range of relevant factors and even make fewer mistakes when recalling facts about a

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140. Algernon Austin, Ctr. for Glob. Pol'y Sols., The Color of Entrepreneurship: Why the Racial Gap Among Firms Cost the U.S. Billions 3 (2016), http://globalpolicysolutions.org/wp-content/uploads/2016/04/Color-of-Entrepreneurship-report-final.pdf.

141. *See* Aida Sijamic Wahid, *The Effects and the Mechanisms of Board Gender Diversity: Evidence from Financial Manipulation*, 159 J. Bus. Ethics 705, 721–22 (2019) (finding that gender diversity on boards better ensure less financial misconduct); Deb DeHaas, Linda Akutagawa & Skip Spriggs, *Missing Pieces Report: The 2018 Board Diversity Census of Women and Minorities on Fortune 500 Boards*, Harv. L. Sch. F. on Corp. Governance (Feb. 5, 2019), https://corpgov.law.harvard.edu/2019/02/05/missing-pieces-report-the-2018-board-diversity-census-of-women-and-minorities-on-fortune-500-boards; *see also Why Diversity and Inclusion Matter: Quick Take*, Catalyst (June 24, 2020), https://www.catalyst.org/research/why-diversity-and-inclusion-matter. The Missing Pieces Report seems to be the most popular source of research for this claim, but the following article also appears supportive. George Tepe, *Boards Should Use Diversity as a Defense Against Activists*, Colum. L. Sch.: Blue Sky Blog (Sept. 21, 2017), https://clsbluesky.law.columbia.edu/2017/09/21/boards-should-use-diversity-as-a-defense-against-activists/ (explaining how diverse boards protect against investor activist campaigns that tend to diminish diversity) ("Board diversity helps promote social justice by ensuring that corporate leaders reflect the diversity of all corporate constituencies and the wider society. In addition, more diverse boards perform better financially and are less likely to be involved with bad governance or even bribery or fraud. Using board diversity as a hostile defense tactic adds another reason to diversify boards. By preemptively increasing the diversity of its board, a corporation increases the likelihood that an activist investor will attempt to replace board members with less diverse candidates. Moreover, the value of board diversity as a defense gives incumbent boards an incentive to increase diversity beyond a few seats. The more diverse a board, the more effective the defense." (footnotes omitted)). Researchers have found that the following benefits are associated with gender-diverse corporate boards:

> - **Effective risk-management practices.** Adding women to a board can improve investment efficiency and prevent risky overinvestment decisions as well as reduce the overconfidence of male CEOs.
> - **Increased engagement among board members**, including behavior like requesting additional information or updates on subjects being discussed and acting on specific tasks after board meetings.
> - **Fewer financial reporting mistakes and controversial business practices** such as fraud and earnings manipulation.
> - **Investment in higher-quality audits.**
>
> Companies with gender-diverse management teams experience fewer operations-related lawsuits.

Why Diversity and Inclusion Matter: Quick Take, *supra*; *see also* Wahid, *supra*, at 706 ("Using a sample of 6132 unique firms over the period from 2000 to 2010, I find, consistent with the hypothesis, gender diversity to be associated with a lower likelihood of financial manipulation, even after controlling for firm-specific factors (firm-fixed effects) and factoring in endogeneity issues through an instrumental variable approach.").

> case. Ironically, lab experiments show that while homogenous groups do less well on complex tasks, the report feeling more confident about their decisions.[142]

However, board diversity is an afterthought.[143] Larry Fink, the Chief Executive Officer of BlackRock, a global investment firm which manages $6.3 trillion in assets, opined in an open letter to chief executive officers that diverse boards result in "a more aware and diverse mindset. They are less likely to succumb to groupthink or miss new threats to a company's business model. And they are better able to identify opportunities that promote long-term growth.[144]

The lack of Board and investor diversity may have contributed to Theranos' fraud. From its incorporation in 2003 until 2018, Holmes was the company's Chief Executive Officer.[145] She recruited her former chemical engineering professor at Stanford to serve as its first Board member.[146] Through the life of the company, Theranos had on its Board some of the country's great citizens. She recruited former U.S. Secretary of State George Shultz to join the Board, and he would become one of her biggest champions even when his own grandson, who was briefly employed by Theranos as a researcher, revealed himself to be a whistleblower regarding Theranos' research practices in its lab.[147] George Shultz also played a role in recruiting an all-star board of former military experts and diplomats, which included former U.S. Secretary of Defense William Perry, former U.S. Secretary of State Henry Kissinger, former U.S. Senator Sam Nunn, former U.S. Senator and heart-transplant surgeon Bill Frist, Admiral George Roughead, and former U.S. Secretary of Defense James Mattis.[148] The Board also included an all-star cast of executives, including former Wells Fargo Chairman Richard Kovacevich, former CEO of Bechtel Group Riley Bechtel, venture capitalist and former CEO of Oracle Don Lucas,[149] and the founder and chairman of Boies Schiller Flexner, David Boies.[150] From

142. Chris Clearfield & Andras Tilcsik, Opinion, *How Board Diversity Might Have Prevented the Theranos Fiasco*, GLOBE & MAIL (Mar. 19, 2018), https://www.theglobeandmail.com/report-on-business/rob-commentary/how-board-diversity-might-have-prevented-the-theranos-fiasco/article38304767/.

143. Sukhinder Singh Cassidy, *Board Diversity Still Stumbling Block to Good Governance*, INFO. (Nov. 28, 2017, 6:45 AM), https://www.theinformation.com/articles/board-diversity-still-stumbling-block-to-good-governance.

144. Larry Fink, *A Sense of Purpose*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 17, 2018), https://corpgov.law.harvard.edu/2018/01/17/a-sense-of-purpose/.

145. Pflanzer, *supra* note 11.

146. Simon Firth, *The Not-so-Retiring Retirement of Channing Robertson*, STAN. ENG'G (Feb. 28, 2012), https://engineering.stanford.edu/news/not-so-retiring-retirement-channing-robertson.

147. CARREYROU, *supra* note 16, at 184–200.

148. Lydia Ramsey Pflanzer, *How Elizabeth Holmes Convinced Powerful Men Like Henry Kissinger, James Mattis, and George Shultz to Sit on the Board of Now Disgraced Blood-Testing Startup Theranos*, BUS. INSIDER (Mar. 19, 2019, 6:44 AM), https://www.businessinsider.com/theranos-former-board-members-henry-kissinger-george-shultz-james-mattis-2019-3.

149. Don Lucas was a founding investor who would also become Chairman of the Board at one point. *See* CARREYROU, *supra* note 16, at 2.

150. James B. Stewart, *David Boies Pleads Guilty*, N.Y. TIMES (Sept. 21, 2018), https://www.nytimes.com/2018/09/21/business/david-boies-pleads-not-guilty.html.

this list of Board members, Holmes had recruited a group of august and powerful citizens, but no health tech experts, medical professionals, or other similar experts.

Before the scandal that would reveal the company's claims to be fraudulent broke, the Theranos Board was a high-powered and high-profile group who was enthralled by Holmes, referring to her as a visionary, revolutionary, ethereal, and akin to Beethoven.[151] A look at the Board composition reveals that, other than Elizabeth and Sunny Balwani, every single Board member—for the ten-year duration of the company—was a white man.[152] And every one of those directors was over the age of sixty-five.[153] The average age of Theranos' Board of Directors was eighty years old.[154] In addition, the majority shared some affiliation with Stanford University, through the Hoover Institute on Stanford's campus where several Board members were appointed Hoover Fellows.[155] The homogenous Board composition may have contributed to the multitude of factors that enabled Holmes and Balwani to mislead investors, which included problems related to implicit bias, pattern matching, and the cult of personality that saw investors, employees, and board members blindly following her and throwing millions of dollars at a company whose claims would later turn out to be fraudulent. The orientation of the Board contributed to the embrace of the standard narrative and pattern matching that says who a successful founder is and what one looks like.[156]

Given the collective resume of the Board of Directors and Holmes' advisers, the inability of the Board to properly supervise and oversee the operation of the company is troubling.[157] Although the Board was a high-profile group, there was a glaring lack of diversity in almost all areas—race, gender, and age—and subject matter expertise. The lack of diversity could have been a reason for why the deception went unnoticed for so long. The intimate nature of the relationships among the investors reduced the amount of due diligence that

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151. Pflanzer, *supra* note 148; Ken Auletta, *Blood, Simpler*, NEW YORKER (Dec. 8, 2014), http://www.newyorker.com/magazine/2014/12/15/blood-simpler.

152. *See* Pflanzer, *supra* note 148.

153. *See id.*

154. Pamela Wasley, *The Theranos Crisis: Where Was the Board?*, FORBES (Apr. 27, 2016, 3:57 PM), https://www.forbes.com/sites/groupthink/2016/04/27/the-theranos-crisis-where-was-the-board/#4be92db5c58e.

155. Richard Beales, *Theranos Under Fire*, N.Y. TIMES (Oct. 27, 2015), https://www.nytimes.com/2015/10/28/business/dealbook/theranos-under-fire.html.

156. *See* Lyons-Padilla et al., *supra* note 133, at 17226 ("Because having a strong track record is inconsistent with stereotypes about funds owned by people of color, asset allocators might be unable to recognize and appropriately evaluate these teams. Instead, they may fall back on pattern matching strategies and mitigate risk by sticking with familiar options—that is to say, by continuing to invest in White and male teams.").

157. *See* Kirsten Weir, *Why We Believe Alternative Facts*, 48 AM. PSYCH. ASS'N: MONITOR ON PSYCH., May 2017, at 24, 24 ("In reality, we rely on a biased set of cognitive processes to arrive at a given conclusion or belief. This natural tendency to cherry pick and twist the facts to fit with our existing beliefs is known as motivated reasoning . . . . Research shows we also interpret facts differently if they challenge our personal beliefs, group identity or moral values.").

was conducted before investments were made.[158] The attention to detail that might have been shown by a more outwardly diverse board was not shown by the Theranos Board of Directors. In other words, it is likely that the similarities shared among the Board created a false sense of security and allowed for Holmes' deception to go undetected. This group of older, white men, mostly affiliated with Stanford, in some way created an environment where they never questioned the veracity of Holmes' research or her promises.[159]

Theranos is not just a story about malfeasance of one founder, but one that profoundly illustrates the ways in which race, class, and implicit bias play out in startup's culture of chasing unicorn status. The fact that investors were willing to blindly invest money in Holmes' company, and that board members championed her without question, despite the fact that she was a nineteen-year-old dropout with no business, healthcare, or engineering experience at the helm, is a strong statement on the role that homogeneity played in why the company's investors and its Board were not as critical of Holmes and consistently gave her the benefit of the doubt.

As described above, there is ample evidence to suggest that entrepreneurial fundraising ability is often tied to race and class, and investors ascribe an inordinate amount of credit to the mythical "brilliant founder," which is likely the result of lack of diversity and implicit bias. It is possible that with certain high-growth startup companies, race and class bias are the cause of the fundraising success. Perhaps evaluated in the absence of implicit biases, these companies truly were the most meritorious when pitched to investors. However, there are dramatic racial, gender, and class differences across startup funding, innovation levels, profitability, and the economy as a whole. Seemingly, the structural inequities in larger society are replicated in the startup community.[160]

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158. *See* Ibrahim, *supra* note 93, at 1432.

159. *See* Pflanzer, *supra* note 148 (highlighting the relationships and experiences between board members and Holmes).

> On February 6, 2019, the SEC Staff issued a new interpretation relating to director qualifications and diversity which could impact proxy statement disclosures for the upcoming proxy season, and potentially D&O questionnaires as well. On the same day, companion bills were introduced into both the U.S. House of Representatives and Senate that would require every public company to disclose in proxy statements: (i) data regarding the racial, ethnic and gender composition of its board of directors, director nominees, and executive officers, as well as the status of any such person as a veteran, in each case, based on voluntary self-identification; and (ii) whether the board has a policy or strategy to promote racial, ethnic and gender diversity among directors, nominees or executive officers. The SEC's interpretation and the Congressional "Corporate Diversity Bill" are the latest evidence that efforts over the past two years for enhanced board diversity are gaining considerable momentum.

Howard Dicker, Ade Heyliger & Aabha Sharma, *D.C. Speaks Up: A Push for Board Diversity from the SEC and Congress*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 25, 2019), https://corpgov.law.harvard.edu/2019/02/25/d-c-speaks-up-a-push-for-board-diversity-from-the-sec-and-congress/.

160. Sarah Jeong & Rachel Becker, *Science Doesn't Explain Tech's Diversity Problem—History Does*, VERGE (Aug. 19, 2019, 2:06 PM), https://www.theverge.com/2017/8/16/16153740/tech-diversity-problem-science-history-explainer-inequality.

The cult of personality dictates who gets funded, but also who is the face of the company through senior management. Holmes clearly understood this and went to great lengths to create an image of herself and of a company that matched a pattern of a typical successful unicorn startup. For example, she took to dressing in all black, modeling herself after Steve Jobs.[161] She brought Avie Tevanian, senior software engineer of Apple, on board early on in the company's start, ostensibly luring him away from Apple to increase the credibility of Theranos.[162] She also rented office space for Theranos in Facebook's old offices.[163] She likely did all of these things because she recognized the outsized importance placed on pattern matching, as opposed to a viable product. Holmes tapped into some of those idiosyncrasies and attempted to create a similar mystique about herself.[164] She then benefited from and capitalized on this myth of the brilliant founder.

Holmes, the "brilliant founder" of a company whose product never worked, raised historic amounts of private capital—approximately $700 million—from wealthy, successful venture capitalists and other prominent U.S. power brokers.[165] She also secured lucrative contracts with Walgreens and Safeway, companies who agreed to create health and wellness centers within their stores that would deploy the Theranos devices.[166] Yet behind closed doors, Theranos was in total disarray.[167] The technology was failing, although arguably it never worked in the first place, and the company's work culture was cloaked in secrecy and hostility. Turnover among key staff in the research and development

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161. *See* Hargrove, *supra* note 137.

162. *See* Taylor Dunn, Victoria Thompson & Rebecca Jarvis, *Ex-Theranos Employees Describe Culture of Secrecy at Elizabeth Holmes' Startup: 'The Dropout' Podcast Ep. 1*, GOOD MORNING AM. (Mar. 12, 2019), https://www.goodmorningamerica.com/news/story/theranos-employees-describe-culture-secrecy-elizabeth-holmes-startup-60544673.

163. Eli Segall, *Theranos Growing Close to Home in Palo Alto*, Silicon Valley Bus. J. (June 29, 2012, 6:00 AM), https://www.bizjournals.com/sanjose/print-edition/2012/06/29/theranos-growing-close-to-home-in-palo.html.

164. For example, Holmes sought advice and investment from Avie Tevanian, former head of software engineering for Apple who was known as Steve Jobs' "right hand." Dunn et al., *supra* note 162. Larry Ellison, of Oracle fame, also advised Holmes. Julia Belluz, *How Silicon Valley Got Played by Theranos*, VOX (June 15, 2018, 4:46 PM), https://www.vox.com/science-and-health/2018/6/12/17448584/theranos-elizabeth-holmes-bad-blood; *see also* Nick Bilton, *Exclusive: How Elizabeth Holmes' House of Cards Came Tumbling Down*, VANITY FAIR (Sept. 6, 2016), https://www.vanityfair.com/news/2016/09/elizabeth-holmes-theranos-exclusive; Francine McKenna, *The Investors Duped by the Theranos Fraud Never Asked for One Important Thing*, MARKETWATCH (Mar. 20, 2018, 7:08 AM), https://www.marketwatch.com/story/the-investors-duped-by-the-theranos-fraud-never-asked-for-one-important-thing-2018-03-19.

165. McKenna, *supra* note 164.

166. Mariella Moon, *Walgreens to Offer Affordable and Needle-Free Blood Tests in More Stores (Updated)*, ENGADGET (Nov. 18, 2014), https://www.engadget.com/2014-11-18-walgreens-blood-tests.html; John Carreyrou, *Safeway, Theranos Split After $350 Million Deal Fizzles*, WALL ST. J. (Nov. 10, 2015, 8:36 PM), https://www.wsj.com/articles/safeway-theranos-split-after-350-million-deal-fizzles-1447205796.

167. Emily Wasserman, *Safeway Severs Ties with Theranos as $350M Deal Collapses*, FIERCEBIOTECH (Nov. 11, 2015, 10:31 AM), https://www.fiercebiotech.com/medical-devices/safeway-severs-ties-theranos-as-350m-deal-collapses (describing claims from executives that "the testing never started" and "Theranos missed deadlines for its blood testing rollout and the clinics are now used mostly for flus shots and travel-related vaccines, current and former Safeway execs told the newspaper").

departments as well as the finance office occurred with alarming frequency.[168] Employees were subject to draconian nondisclosure agreements that were ruthlessly enforced.[169] Despite repeated failures of the testing system, such information about the product's failures was hidden (to varying degrees) from investors, customers, employees, and even Board members.[170] Moreover, the company engaged in outright lies to avoid detection by federal and state regulators, including creating a secret laboratory and falsifying reports for the better part of a decade.[171]

WeWork, a "global network of workspaces where companies and people grow together,"[172] at the time of this writing, was a unicorn company recently fallen from grace, in eerily similar and parallel ways to Theranos.[173] Although Theranos' downfall was fraud, WeWork's downfall was overconfidence, eccentricities, and incompetence. WeWork's founder Adam Neuman promoted a cult of personality around his company and courted investors based on him presenting his view of the world and fostering a mystique about himself akin to the mythical brilliant founders of the past.[174] WeWork reportedly was losing millions of dollars each month, but by the end of 2014, WeWork had raised more than half a billion dollars from venture capitalists.[175] Many of Silicon Valley's most prominent investors invested in the company. Eventually Softbank would invest $4.4 billion in the company, based not on financial estimates and analysis, but "on [WeWork's] energy and spirituality."[176]

Theranos' and WeWork's seemingly unlikely trajectory establishes that both problematic fundraising practices and "brilliant founder" mythology are intertwined with race, gender, and class. The notion of questioning Black genius in ways that white founders are not questioned is problematic. It is unlikely that there could ever be a Black Elizabeth Holmes—an individual with no science background, raising billions of dollars on the claim that they could develop the Theranos technology.[177]

168. CARREYROU, *supra* note 16, at 20.

169. *Id.* at 27.

170. An investigation by the Food and Drug Administration revealed that Theranos's proprietary analyzer was used only in twelve out of 250 blood tests. The company was using competitors' machines for the other tests. CARREYROU, *supra* note 16, at 113–14, 169.

171. Christopher Weaver, *Theranos Secretly Bought Outside Lab Gear and Ran Fake Tests, Court Filings Allege*, WALL ST. J. (Apr. 21, 2017, 10:42 PM), https://www.wsj.com/articles/theranos-secretly-bought-outside-lab-gear-ran-fake-tests-court-filings-1492794470 (sharing that Theranos secretly brought in lab equipment to run fake demonstrations).

172. *WeWork & Meetup*, WEWORK, https://www.wework.com/meetup-offer (last visited May 21, 2021).

173. *See* Lizzie Widdicombe, *The Rise and Fall of WeWork*, NEW YORKER (Nov. 6, 2019), https://www.newyorker.com/culture/culture-desk/the-rise-and-fall-of-wework.

174. *Id.*

175. Charles Duhigg, *How Venture Capitalists Are Deforming Capitalism*, NEW YORKER (Nov. 23, 2020), https://www.newyorker.com/magazine/2020/11/30/how-venture-capitalists-are-deforming-capitalism.

176. *Id.*

177. *See* Williams, *supra* note 23 ("Yet it's incredibly difficult to imagine a black woman having a chance to reach anywhere near the heights from which Elizabeth Holmes was able to fall, because black women typically get nowhere close to the same funding opportunities. The fact that Holmes raised over $700 million for Theranos

Not only do these fundraising practices and culture replicate societal inequities, but the use of implicit bias and the lack of diversity may possibly contribute to fraud and bad investment decisions. The lack of diversity among Theranos' investors and the company's Board likely contributed to hiding and overlooking the fraud.

As is common practice in venture capital-backed startups, the members of the Theranos board were also investors in the company. They brought in their wealthy and powerful friends to invest in the startup as well.[178] This phenomenon is not unique in Silicon Valley, but the practice of bringing your friends on board to an opportunity does have implications for who gets funding when the wealthy gatekeepers lack diversity.[179] The way in which Holmes was unfairly supported by a system designed to promote a certain class and type of entrepreneur demonstrates the role of implicit bias in the system.

Elizabeth Holmes' gender played an outsized role in the narrative around her success and contributed to her being perceived as a brilliant founder.[180] As a female inventor at the helm of the company she founded, she was an anomaly in Silicon Valley and she represented a variation of the wunderkind theme. Holmes was lauded as a role model and a wunderkind because her presence in the startup world was disruptive of the male wunderkind archetype.[181]

Indeed, as a female founder, Holmes likely experienced gender discrimination, but she is also white and came from socio-economic privilege. As such, Holmes was able to move easily among the circles of elite power in Silicon Valley because the socioeconomic forces in Silicon Valley ran in her favor, as a white, well-educated, and connected woman. This multi-dimensional aspect of her identity is important here because, as a woman, her gender makes her a part of a subordinated group, but as an upper-class, white woman, her race, as well as her class background, elevates her to a dominant group.[182] In other words, Holmes may have experienced gender discrimination, but as a wealthy, white woman of a certain class she also experienced racial and class privilege,

is a feat for any founder but especially for a woman: As it is, scarcely 2% of VC funding goes to women CEOs. By comparison, black women raise a paltry $36,000 in an average round.").

178. *See* CARREYROU, *supra* note 16, at 176–183.

179. *See* Interview by Sally Smith Hughes with Donald L. Lucas, in Berkeley, Cal. (Mar. 15, 2009), https://digitalassets.lib.berkeley.edu/roho/ucb/text/lucas_don.pdf (exploring and explaining through the words of participants how venture capital in the state originated in the 1960s and 1970s); *see also* Bettina Makalintal, *Theranos Founder Elizabeth Holmes Comes from a Baker's Yeast Empire*, VICE (Mar. 25 2019, 3:41 PM), https://www.vice.com/en_us/article/wjm3eb/theranos-founder-elizabeth-holmes-comes-from-a-bakers-yeast-empire.

180. *See* Sara Ashley O'Brien, *HBO Theranos Documentary Goes Inside the Secretive, Failed Company*, CNN: BUS. (Mar. 12, 2019, 12:27 PM), https://www.cnn.com/2019/03/11/tech/the-inventor-theranos-documentary/index.html ("She was celebrated as a female founder success story and often graced the cover of magazines.").

181. *See id.*

182. *See* Darren Lenard Hutchinson, *Identity Crisis: "Intersectionality, "Multidimensionality," and the Development of an Adequate Theory of Subordination*, 6 MICH. J. RACE & L. 285, 288 (2001) (describing intersectionality as "recogniz[ing] the multidimensional and complex nature of subordination").

which she was able to leverage to push her company forward. The argument here is that her whiteness and wealthy connections played a larger role in her story than her gender and that her race and class helped her to overcome the challenges raised by her gender and, in fact, the multi-dimensional aspect of her story contributed to her popularity and praise.[183] The fact that she was a woman only helped her to raise money and to continue to receive funding for her company. She used feminist and gendered language when it benefited her,[184] and then fashioned herself in Steve Jobs' image and lowered the register of her voice at other times to appear more masculine.[185] Elizabeth Holmes' success can be explained by her multidimensionality and the power dynamics of three important identities: race, class, and gender.[186] Although she is a woman and women in entrepreneurship are rare, she is a white woman who counted herself among the upper class. The import of this is that any experience of entrepreneurship by her as an underrepresented minority is arguably trumped by the position afforded her in society by her race and class and raises the possibility that her race and class afforded her the privilege of avoiding discrimination based on gender.[187] She was able to expertly leverage her racial and class privileges to overcome any ill effects of gender discrimination. In effect, her role as a wealthy, white woman in Silicon Valley is marginal diversity, and a form of tokenism at best.[188]

Juxtaposing her experience against entrepreneurs of color in Silicon Valley, there is a stark difference between Holmes' experience of entrepreneurship and that of entrepreneurs of color. Entrepreneurs of color face systematic challenges to being a minority or an outsider to an insider's club. The difficulties of fundraising are multi-dimensional and may include lack of social capital, access to a network, or any means to backchannel feedback or insider information when fundraising.[189] In Holmes' case, her parents gave her $50,000

183. Hanna Hart, *What Can Theranos' Elizabeth Holmes Teach Us About Feminism?*, FORBES (Mar. 31, 2019, 6:48 PM), https://www.forbes.com/sites/hannahart/2019/03/31/womens-history-what-does-theranos-elizabeth-holmes-tell-us-or-not-about-feminism/#297c019933f4 ("Her whiteness and wealthy connections helped her overcome this hurdle [as a woman]. Then, once she acquired critical sponsorship and funding, the fact that she was a young woman undoubtedly helped create Elizabeth Holmes as a media darling.").

184. *See* Kristen Bellstrom, *Elizabeth Holmes Hints at Sexism in Media Coverage*, FORTUNE (Dec. 10, 2015, 9:42 AM), https://fortune.com/2015/12/10/elizabeth-holmes-sexism-theranos.

185. Hart, *supra* note 183 ("She relied on the language of gender when it suited her, but set out to emulate Steve Jobs and amass as much personal power as possible.").

186. Williams, *supra* note 23.

187. *Id.*

188. Tokenism is "the practice of doing something (such as hiring a person who belongs to a minority group) only to prevent criticism and give the appearance that people are being treated fairly." Kara Sherrer, *What is Tokenism, and Why Does it Matter in the Workplace?*, VANDERBILT UNIV.: BUS. (Feb. 26, 2018), https://business.vanderbilt.edu/news/2018/02/26/tokenism-in-the-workplace/ (quoting the Merriam Webster definition of tokenism).

189. Solange Lopes, *5 Challenges Faced by Women Entrepreneurs of Color*, ENTREPRENEUR (May 30, 2018), https://www.entrepreneur.com/article/312662.

from an education trust that they had put aside for her tuition at Stanford.[190] She was given the benefit of the doubt at every turn. She was unfairly propped up by a system designed to promote a certain class and type of entrepreneur. Holmes' success in raising capital remains a lesson in the ways that race, privilege, and wealth dictate startup success. Startup culture along with the private markets enabled the meteoric rise of Theranos. The closed market system of private capital in Silicon Valley is the backbone of entrenching homogeneity.[191]

The lore around her family's pedigree acted as a form of pattern matching. The pattern is that investors convinced themselves that they know what elite success looks like and that it looks like Elizabeth Holmes' family history. Her parents were Christian and Noel Holmes.[192] On her father's side, she is descended from Charles Louis Fleischmann, a Hungarian immigrant who founded the Fleischmann Yeast Company.[193] The yeast company's success turned Fleischmann's family into one of the wealthiest families in America.[194] Charles' daughter, Bettie Fleischmann, married Dr. Christian Holmes. Dr. Holmes was Elizabeth's great-great-grandfather.[195] He helped to found Cincinnati General Hospital and the University of Cincinnati Medical School.[196] In the context of Theranos and Elizabeth Holmes' story, much would be made of Elizabeth's family tree and her family's connections.[197] Among the media and her investors, through the connection to entrepreneurship and to medicine, it was implied that Elizabeth was destined to found Theranos, a medical startup, since she had inherited both medical and entrepreneurial genes from her grandfather and great-great-grandfather.[198] This logic is essentially dynastic—that children

190. Roper, *supra* note 19 ("[Holmes] . . . dropped out of Stanford and founded a company called Theranos with her tuition money.").

191. Ellen Gamerman, *The New High-Tech Patrons*, WALL ST. J. (Feb. 28, 2013, 6:49 PM), https://www.wsj.com/articles/SB10001424127887323384604578328121811415726.

192. CARREYROU, *supra* note 16, at 9.

193. *Id.*

194. *Id.* at 9–10.

195. *Id.* at 10.

196. *See* Nathan Hood, *Dr. Christian R. Holmes, the Cincinnati General Hospital, and the Surgical Amphitheater*, U. CIN. LIBR.: LIBLOG (July 31, 2015), https://libapps.libraries.uc.edu/liblog/2015/07/dr-christian-r-holmes-the-cincinnati-general-hospital-and-the-surgical-amphitheater.

197. For example, Holmes' next-door neighbor growing up was Richard Fuisz, a noted entrepreneur and medical inventor. He is a true Renaissance man; he is a licensed doctor, was possibly a CIA agent, and he makes a successful living from royalties from licensing patents. CARREYROU, *supra* note 16, at 56, 60.

198. *See* Interview by Sally Smith Hughes with Donald L. Lucas, *supra* note 179. Describing Elizabeth Holmes, Lucas said:

> She had no background in business, and so it's quite presumptuous for somebody to say, 'I'm going to be president of the company.' But there's an important distinction. That's what I felt when I [first] met her. After spending a lot more time with her, I learned her great-grandfather was an entrepreneur and started Fleischmann's—packaged yeast. It was very successful. So that was one side, that's the entrepreneur side, but she was in the medical side. Ah! It turns out later, the hospital very near where they lived is named after her great uncle who was involved with medicine. So she came by both of the two talents necessary here, one medicine and the other entrepreneurship, quite naturally. You could just see it the way she handles things, the way she thinks.

Id.; *see also* Makalintal, *supra* note 179.

of elites are presumptively worthy of access to capital and leadership positions.[199]

For Holmes in particular, her pedigree also created a bit of a mystique about her and fed into her cult of personality. In the HBO documentary film *The Inventor*, Theranos chairman Don Lucas said that he knew that when he met Holmes, then a twenty-two-year-old startup founder, she "came by it naturally" (because her ancestor was an entrepreneur and her great-great-grandfather a famous doctor).[200] This statement seems to convey that to Don Lucas, it was her bloodline, not her work, that mattered to him as he considered an investment.[201] In fact, her pedigree and not necessarily her product is why Don Lucas invested in the company.[202]

Further, Board member George Shultz referred to Holmes as "the next Steve Jobs or Bill Gates" in a *Wall Street Journal* interview.[203] This article spawned the next wave of funding and sparked the $6 billion valuation. In 2014, she made a claim that she was developing a $100 million partnership with the U.S. Defense Department.[204] There was no evidence to this claim, but it was reported on and repeated.[205] This focus on the cult of personality, the idea that she might be the "next Steve Jobs or Bill Gates" gave her cover for her fraudulent

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199. *See* Henry Farrell, *David Brooks Has a Point—Upper Class Kids Have Invisible Cultural Advantages*, WASH. POST: MONKEY CAGE (July 11, 2017, 8:15 AM), https://www.washingtonpost.com/news/monkey-cage/wp/2015/09/23/why-are-working-class-kids-less-likely-to-get-elite-jobs-they-study-too-hard-at-college (providing a statement from Lauren Rivera, Associate Professor at Northwestern University's Kellogg School of Management) ("Whether intentionally or not, elite parents expose their children to different experiences and styles of interacting that are useful for getting ahead in society. Many of these are taken for granted in upper and upper-middle class circles, such as how to prepare a college application (and having cultivated the right types of accomplishments to impress admissions officers), how to network in a business setting in a way that seems natural, and how to develop rapport with teachers, interviewers, and other gatekeepers to get things you want from those in power. Basically, if we think of economic inequality as a sporting competition, elite parents give their kids a leg up, not only by being able to afford the equipment necessary to play but also by teaching them the rules of the game and giving them insider tips on how to win."); *see also* David Brooks, *Bobos in Paradise: The New Upper Class Rules and How They Got There*, 33 STAN. CTR. ON POVERTY & INEQUALITY 304 (2000), https://inequality.stanford.edu/sites/default/files/media/_media/pdf/key_issues/elites_journalism.pdf (exploring the generational rise of elites through the descriptions of brides and grooms in the *New York Times* weddings page).

200. *The Inventor: Out for Blood in Silicon Valley*, *supra* note 24.

201. *Id.*

202. *See* Eliana Dockterman, *Elizabeth Holmes Got Where She Was Through Privilege. A New Documentary About Her Doesn't See That*, TIME (Mar. 14, 2019, 6:16 AM), https://time.com/5551319/the-inventor-documentary-review ("The men she hustled were probably seduced by her pedigree; in the film, Theranos chairman Don Lucas says that he knew Holmes, then a 22-year-old startup founder, 'came by it naturally' because her great-grandfather was an entrepreneur and her great-uncle a famous doctor—as if her bloodline, not her work, was what mattered."); *see also* Gompers et al., *supra* note 107.

203. Joseph Rago, *Elizabeth Holmes: The Breakthrough of Instant Diagnosis*, WALL ST. J. (Sept. 8, 2013), https://www.wsj.com/articles/elizabeth-holmes-the-breakthrough-of-instant-diagnosis-1378526813.

204. United States v. Holmes, No. 5:18-CR-00258-EJD, 2020 WL 666563, at *2, *13 (N.D. Cal. Feb. 11, 2020); *see also* Press Release, *supra* note 31.

205. Press Release, *supra* note 31 ("In truth, Theranos' technology was never deployed by the U.S. Department of Defense and generated a little more than $100,000 in revenue from operations in 2014.").

claims because she was essentially vouched for time and time again by a member of the elite startup world.

This type of fundraising culture is what propelled Theranos to such success in raising capital. The normalized practice of founders obscuring facts and inflating claims in pursuit of fundraising capital played deeply in Elizabeth Holmes' favor. Patrick O'Neill, the media and ad representative from Chiat\Day, the company Theranos hired for publicity, described his experience with Theranos in an interview stating that "all tech startups were chaotic and secretive."[206] Despite the chaos and secrecy or the fact that her product did not work, Holmes was able to successfully fundraise. Knowing what we now know about the failure of the Theranos product, the fact that she was able to raise money in record-breaking numbers is an indictment of the vaporware culture described above. Because of the lack of evidence of her experience and expertise, one can only draw the conclusion that the intrigue of her story, along with her race, background, and connections, propelled her forward absent concrete factual projections.[207] The company ultimately raised $700 million in the private market from investors who committed capital often without reviewing audited financial statements, taking the company to a peak valuation of $9 billion.[208] This method of fundraising based on vaporware has the effect of reinforcing structural racism. The presumptions against people of color function much differently than with white founders.[209] Through this lens, vaporware is another way to demonstrate the closed system that will vouch for white founders even when their product doesn't work.

The allure of Theranos was that it was a seemingly innovative company with a mission to disrupt the diagnostic lab industry by providing low-cost blood testing services. The hype around the startup was that the company was making a major breakthrough in the large blood-testing market, where the U.S. diagnostic-lab industry posts annual sales of over $70 billion.[210] Theranos claimed its technology was revolutionary because it had developed devices to automate and miniaturize blood tests using microscopic blood volumes.[211] The company's tests required only about 1/100 to 1/1,000 of the amount of blood that would ordinarily be needed and cost far less than existing tests.[212] Theranos

206. CARREYROU, *supra* note 16, at 160.

207. *See* Kitanya Harrison, *Elizabeth Holmes and the Dangers of White Feminism*, MEDIUM (Mar. 22, 2019), https://medium.com/@kitanyaharrison/elizabeth-holmes-and-the-dangers-of-white-feminism-699cfe6333a3 (opining that Holmes took advantage of her identity to grain traction for her startup).

208. Francine McKenna, *The Last Days of Theranos—The Financials Were as Overhyped as the Blood Tests*, MARKETWATCH (Oct. 20, 2018, 2:21 PM), https://www.marketwatch.com/story/the-last-days-of-theranos-the-financials-were-as-overhyped-as-the-blood-tests-2018-10-16.

209. *See, e.g.*, Courtney Rubin, *What It's Like to Be a Black Entrepreneur Right Now*, MARKER (June 16, 2020), https://marker.medium.com/what-its-like-to-be-a-black-entrepreneur-right-now-509373dee85a.

210. Nickie Louise, *Theranos Is Finally Shutting Down After Investors Lost Nearly $1 Billion*, TECHSTARTUPS (Sept. 5, 2018), https://techstartups.com/2018/09/05/theranos-finally-shutting-investors-lost-nearly-1-billion.

211. Rago, *supra* note 203.

212. *See* Parloff, *supra* note 9.

dubbed its blood collection vessel the "nanotainer" and its analysis machine the "Edison."[213] The company's mission was compelling to investors because blood draws are painful, costly, and time consuming, and many patients want results quickly.

Elizabeth Holmes traded on the theme of disruption and innovation. Theranos' marketing and Holmes' pitch capitalized on the idea that Theranos' technology would revolutionize the staid blood-testing market. In fact, its vaunted technology turned out to be a sham and, in reality, Theranos performed tests using competitors' machines. In interviews, Holmes underscored that "Theranos' proprietary technology could take a pinprick's worth of blood, extracted from the tip of a finger, instead of intravenously, and test for hundreds of diseases—a remarkable innovation that was going to save millions of lives and, in a phrase that [Elizabeth Holmes] often repeated, 'change the world.'"[214] The theme of changing the world was what investors, partners, and employees interviewed after the fact would say had lured them in to the company.[215]

Before the sham was revealed, the claims of innovation and revolutionizing blood testing, with little or no documented evidence to support the claims, were enough to persuade former Safeway CEO Steven Burd to partner with Theranos.[216] In 2012, Safeway invested $350 million into retrofitting 800 Safeway locations with clinics that would offer in-store blood tests. However, after many missed deadlines and questionable results from a trial clinic at Safeway's corporate offices, the deal was called off in 2015.[217]

In September 2013, Theranos also partnered with Walgreens to offer in-store blood tests at more than forty Walgreens locations with plans to expand its "wellness centers" across the United States.[218] Like Safeway, Walgreens wanted in on innovation and Walgreens' senior executives pushed through the deal with

213. Norman A. Paradis, *The Rise and Fall of Theranos*, SCI. AM. (Apr. 22, 2016), https://www.scientificamerican.com/article/the-rise-and-fall-of-theranos/.

214. Bilton, *supra* note 164.

215. *See* Monica Torres, *4 Ways Elizabeth Holmes Manipulated Her Theranos Employees*, HUFFPOST (Mar. 22, 2019, 12:57 PM), https://www.huffpost.com/entry/elizabeth-holmes-office-employees_l_5c92abe3e4b01b140d351b6f.

216. *See* John Carreyrou, *From Startup to Meltdown: The Unraveling of Theranos*, WHARTON (July 17, 2018), https://knowledge.wharton.upenn.edu/article/the-secrets-and-lies-that-sunk-theranos (explaining that Holmes courted Burd for the partnership before he retired in 2013, but the executives that succeeded him were more skeptical about Theranos).

217. Carreyrou, *supra* note 166. A sad coda to this story is that of the Safeway Vice President, whose husband had cancer. She greenlit the Theranos partnership in part because she was hopeful that the company would help millions of people suffering with illness. David Shaywitz, *Learning the Right Lesson from Theranos: Fraud Is Bad, Wanting to Disrupt Healthcare Isn't*, FORBES (June 4, 2018, 5:31 PM), https://www.forbes.com/sites/davidshaywitz/2018/06/04/learning-the-right-lesson-from-theranos-fraud-is-bad-wanting-to-disrupt-healthcare-isnt/?sh=2337c76b60c7.

218. *See* John Soat, *Walgreens CIO: We Intend to Be a Leader in Healthcare Technology*, FORBES (Nov. 17, 2014, 10:00 AM), https://www.forbes.com/sites/oracle/2014/11/17/walgreens-cio-we-intend-to-be-a-leader-in-healthcare-technology/#44223bca543e.

Theranos under pressure to best CVS' minute clinic.[219] Walgreens executives ignored the private consultant's warnings and concerns based on the assurances of Holmes' Board. The same phenomenon occurred with the Safeway decisionmakers.[220] Holmes had an uncanny ability to bring people in and get them to believe that Theranos' technology could completely revolutionize how effective health care is delivered. She was able to draw people in—investors, board members, employees, and partners—based off the strength of her claims of changing the world.[221] The real story, however, was a little more complicated. In addition to her success stemming from investors compelled by her narrative of revolutionizing the medical industry, Holmes' connections, her cultural capital, and the overall startup culture of deception were also reasons for Theranos' success.

The next Part describes the private markets' role in protecting founders and propelling star companies forward and how the private fundraising market perpetuates the racial wealth gap and mirrors the structural barriers and inequities in larger society. Taken together, the fundraising culture and the private market's role combine to entrench mostly white men over any other group when it comes to dominating the startup market.

II. THE MODEL UNICORN TURNS BAD: THE PRIVATE MARKET'S ROLE

The private investment market is the wealthy and influential sector responsible for crowning unicorns.[222] In the private markets, investors are often given equity in startup companies in exchange for funding.[223] These investors include venture capital investors, angel investors, and individual investors that

219. *See* Amelia Lucas, *Ex-Theranos CEO Elizabeth Holmes 'Really Did Believe' She Was Helping the World, Bad Blood Author Says*, CNBC (Aug. 22, 2018, 7:25 PM), https://www.cnbc.com/2018/08/22/ex-theranos-ceo-holmes-believed-she-was-helping-the-world-author-says.html (providing a statement from Carreyrou that "[Walgreens was] so afraid that Theranos would turn around and strike a deal with their rival, their arch-rival, CVS that they just ignored their own in-house consultant," who alerted Walgreens of his suspicions in late 2010).

220. James Markarian, *How to Avoid Making Catastrophic Innovation Bets*, VENTUREBEAT (June 8, 2019, 12:12 PM), https://venturebeat.com/2019/06/08/how-to-avoid-making-catastrophic-innovation-bets ("By the time Theranos had been exposed as a sham, Safeway had dumped $350 million into the partnership—nearly half of its net income in 2012—and built clinics in over 800 stores.").

221. *See How a Silicon Valley Breakthrough Failed the Basic Test of Innovation*, CHICAGO TRIB. (June 13, 2016, 4:40 PM), https://www.chicagotribune.com/opinion/editorials/ct-theranos-walgreen-holmes-edit-0614-md-20160613-story.html (mentioning Holmes' persuasive salesmanship).

222. Davide Scigliuzzo, Kelsey Butler & Sally Bakewell, *Everything Is Private Equity Now*, BLOOMBERG: BUSINESSWEEK (Oct. 8, 2019, 1:10 PM), https://www.bloomberg.com/news/features/2019-10-03/how-private-equity-works-and-took-over-everything ("The business [of private equity] has made billionaires out of many of its founders. Funds have snapped up businesses from pet stores to doctors' practices to newspapers. PE firms may also be deep into real estate, loans to businesses, and startup investments—but the heart of their craft is using debt to acquire companies and sell them later.").

223. James Chen, *Private Equity*, INVESTOPEDIA, https://www.investopedia.com/terms/p/privateequity.asp (Apr. 30, 2020) ("Private equity is composed of funds and investors that directly invest in private companies, or that engage in buyouts of public companies, resulting in the delisting of public equity. Institutional and retail investors provide the capital for private equity, and the capital can be utilized to fund new technology, make acquisitions, expand working capital, and to bolster and solidify a balance sheet.").

may have a connection to the founders.[224] Generally, the general public is not eligible to invest in the private market because private companies are not publicly traded. As a result, access to the private investment market is, in most cases, restricted because of the federal securities laws. The import of this restriction is that wealthy, elite private actors carry the bulk of the influence with respect to entrepreneurship. In protecting the public from themselves, the resulting effect of the federal securities laws is that monied and connected individuals have an outsized advantage and control with respect to entrepreneurship.[225]

For the reasons described above in Part I related to lack of diversity, heuristics, and the brilliant founder myth, access to capital to launch a startup is often limited to those that are of a certain type. As a result, the private markets reinforce the existing structures of wealth inequality. While the federal securities laws focus on investor protection, accountability, and disclosure, the proxies used by the Securities and Exchange Commission (SEC) bar access by communities of color to private financial markets. The objective standard used by the SEC of using wealth as a proxy for sophistication has the effect of being both "under protective of wealthy investors and over protective of non-wealthy investors."[226] These race neutral regulations effectively bar most communities of color from participating in the private markets and therefore in "opportunities to create generational wealth through entrepreneurship and investing," also leaving founders of color underfunded.[227]

One of the problems with the private financial markets is that the exemptions from registration under the federal securities laws function to restrict participants to a small, insular class of mostly white investors.[228] Funding streams to entrepreneurs mirror where the wealth already exists, resulting in white male entrepreneurs receiving the majority of startup funding. This has resulted in disparity in capital raising between founders of color and white

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224. *See* Cremades, *supra* note 89 (differentiating between the types of investors that fund startups).

225. Musa Al-Gharbi, *The 1 Percent Wins Again: How Entrepreneurship—Supposedly the Cornerstone of American Society—Favors the Wealthy*, SALON (Mar. 20, 2016, 7:59 PM), https://www.salon.com/2016/03/20/the_1_percent_wins_again_how_the_wealthy_have_all_the_advantages_for_starting_new_businesses/; *see* Alice Marwick, *Silicon Valley Isn't a Meritocracy. And It's Dangerous to Hero-Worship Entrepreneurs*, WIRED (Nov. 25, 2013, 9:30 AM), https://www.wired.com/2013/11/silicon-valley-isnt-a-meritocracy-and-the-cult-of-the-entrepreneur-holds-people-back ("[A] level of material wealth is necessary to participate in San Francisco tech culture. . . . To forge the type of social connections necessary to move into the upper echelons of the tech scene requires being able to take part in group activities, travel to conferences, and work on personal projects. This requires middle- to upper-class wealth, which filters out most people.").

226. Kevin G. Bender, *Giving the Average Investor the Keys to the Kingdom: How the Federal Securities Laws Facilitate Wealth Inequality*, 15 J. BUS. & SEC. L. 1, 4 (2016).

227. Mariah Lichtenstern, *Investors Still Engage in Racist Redlining. Why Haven't We Done Something About It?*, FORTUNE (Jan. 6, 2021, 4:00 PM), https://fortune.com/2021/01/06/redlining-black-latinx-entrepreneurship-investment-sec/; *see also* Bender, *supra* note 226, at 3–4.

228. *See* Lyons-Padilla et al., *supra* note 133, at 17225 (explaining that white men control more than 98.7% of global financial assets and that "[o]f the $69.1 trillion global financial assets under management across mutual funds, hedge funds, real estate, and private equity, fewer than 1.3% are managed by women and people of color").

founders, which has developed over time.[229] This disparity in access to capital affects all methods of capital raising for entrepreneurs.[230]

A. Private Offering Exemptions, the Wealth Gap, and the Fallacy of Bootstrapping

Startup financing typically occurs through three investor types—friends and family investors, angel investors and venture capital investors—conducted through private offerings. Typically, "friends and family" rounds are investments from individuals willing to invest their own money ordinarily up to $150,000.[231] The reference to "friends and family" is because these investors usually have a personal relationship with the founders; the investor believes in the startup idea or the founder and would probably not make the investment but for her relationship with the founder.

After friends and family, there are angel investments, which are investments of up to $2 million typically by wealthy individuals who are either entrepreneurs themselves or otherwise have experience investing in early-stage companies.[232] Angel investors may or may not have a personal relationship with the founders, but investment by angel investors is heavily relationship driven.[233] Angel investors typically use their personal funds, which gives them flexibility to use nonfinancial as well as financial reasons to invest. They make their investment decision based on seeking a return on their investment and having the opportunity to mentor a startup founder. Angel investors usually bridge the gap between the friends and family round and venture capital rounds.[234] Angels play an important role in developing startups and as a mechanism for sorting new startups that later seek venture capital.[235] "Sorting" or screening is often

229. As a startup lawyer directing an entrepreneurship and community development clinic at Columbia Law School, I've worked with underrepresented entrepreneurs in several jurisdictions; I know first-hand how fundraising works and the challenges faced by entrepreneurs of color.

230. *See* Robert Fairlie, Alicia Robb & David T. Robinson, *Black and White: Access to Capital Among Minority-Owned Startups* (Stan. Inst. for Econ. Pol'y Rsch., Discussion Paper No. 17-03, 2016), https://siepr.stanford.edu/sites/default/files/publications/17-003.pdf ("Black-owned businesses are persistently smaller and face more difficulty in raising external capital. Large differences in credit worthiness are important for explaining the difference. Even controlling for credit worthiness, persistent differences in perceptions of treatment by banks are also important. Spatial variation in banking conditions and historical attitudes towards race are consistent with racial bias.").

231. *How to Raise a Friends and Family Round*, FOUNDER INST. (Mar. 22, 2019), https://fi.co/insight/how-to-raise-a-friends-and-family-round ("A Friends and Family round typically results in anywhere from $10,000 to $150,000 in funding that allows a startup to get through its first few months of operation.").

232. Anne Field, *What Is an Angel Investor? Who They Are, What They Do, and How They Help Startups Grow*, BUS. INSIDER (Nov. 12, 2020, 7:45 AM), https://www.businessinsider.com/what-is-an-angel-investor ("Angel investors generally are high-net-worth individuals who provide funding to startups in exchange for convertible debt (bonds) or equity (shares) in the company. The term is actually borrowed from show business . . . . Plus, many angel groups co-invest with other angel groups, individual angels, and even early-stage venture capitalists to make investments of $500,000 to $2 million per round.").

233. Ibrahim, *supra* note 93, at 1431 (explaining that angel investors are more likely to invest if they know the founder and the industry of the startup).

234. *Id.* at 1428.

235. *Id.* at 1428–29.

facilitated at the angel investor level.[236] Entrepreneurs signal the strength of their startup idea by how much angel investment they have in their company, since "[f]irms which are backed by angel investors are more likely to survive, create more jobs, and have a greater chance of successfully exiting the startup phase than otherwise comparable firms without this support."[237] According to the Center for Venture Research, total angel investments in 2019 were $23.9 billion, an increase of 3.2% over 2018, and a total of 63,730 entrepreneurial ventures received angel funding in 2019.[238]

Venture capital is a term used to describe risky, speculative investments, often in early-stage, high-growth technology companies.[239] It is a type of private financing for startups, where the investor, investment bank, or other financial institution believes that the investment has long-term growth potential.[240] The venture capital firm invests in the startup often by taking a sizable stake in the business until a certain point when the startup can be sold to another company or sold on the public-equity markets when the venture capital firm can exit and get a sizeable return on their investment.[241] U.S. venture capital funds set new records in deal making, exits, and fundraising in 2020, according to a new report from PitchBook and the National Venture Capital Association. "Deal value topped $150 billion for the first time, while exit value hit a record $290 billion after a surge of public listings in the second half of the year. Meanwhile, new venture capital funds raised $73.6 billion, surpassing the 2018 high of $68.1 billion, according to the report."[242]

All three of the above-described investment types implicate the federal securities laws.

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236. According to research by Josh Lerner et al., angels are beneficial to the growth, performance, and survival of startups, even if they are located in economies that are not friendly to entrepreneurs. Josh Lerner, Antoinette Schoar, Stanislav Sokolinski & Karen Wilson, *The Globalization of Angel Investments: Evidence Across Countries* (Nat'l Bureau of Econ. Rsch. Working Paper No. 21808, 2015), https://www.nber.org/system/files/working_papers/w21808/w21808.pdf. Startups that have angel backing are at least 14% more likely to survive for eighteen months or more after funding than firms that do not. *Id.* at 6. Angel-backed firms hire 40% more employees, and angel backing increases the likelihood of successful exit from the startup phase by 10 percent, to 17 percent. *Id.*

237. Laurent Belsie, *How Angel Investors Help Startup Firms*, NAT'L BUREAU OF ECON. RSCH. (Mar. 2016), https://www.nber.org/digest/mar16/how-angel-investors-help-startup-firms.

238. JEFFREY SOHL, CTR. FOR VENTURE RSCH., THE ANGEL MARKET IN 2019: COMMITMENTS BY ANGELS INCREASE WITH A SIGNIFICANT RISE IN DEAL VALUATIONS (2020), https://scholars.unh.edu/cgi/viewcontent.cgi?article=1032&context=cvr.

239. Fan, *supra* note 9, at 590.

240. Adam Hayes, *Venture Capital*, INVESTOPEDIA, https://www.investopedia.com/terms/v/venturecapital.asp (Mar. 16, 2021) ("Venture capital (VC) is a form of private equity and a type of financing that investors provide to startup companies and small businesses that are believed to have long-term growth potential.").

241. Zider, *supra* note 104.

242. Amy Whtye, *Venture Capital's Best Year Ever*, INSTITUTIONAL INVESTOR (Jan. 14, 2021), https://www.institutionalinvestor.com/article/b1q3tsrkkdv4m7/Venture-Capital-s-Best-Year-Ever.

1. *The Racial Effect of the Accredited Investor Rules*

All private offerings (even those made to friends and family) require registration with the SEC unless the offering is exempt from registration under the federal securities laws.[243] Registration with the SEC can be costly and burdensome.[244] As a result, the vast majority of companies choose to find an exemption from registration.[245] The easiest and most common exception to the registration requirement is the accredited investor rule promulgated under Regulation D, which creates an exemption for the offering if all investors are accredited investors.[246]

Any investment in a private offering is overwhelmingly restricted to company insiders, institutional investors, and wealthy individuals or "accredited investors."[247] The SEC created the concept of "accredited investors" to mitigate the tension in protecting individual investors in private securities offerings and

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243. *Investor Bulletin: Private Placements Under Regulation D*, SEC (Sept. 24, 2014), https://www.sec.gov/oiea/investor-alerts-bulletins/ib_privateplacements.html ("A securities offering exempt from registration with the SEC is sometimes referred to as a *private placement* or an *unregistered offering*. Under the federal securities laws, a company may not offer or sell securities unless the offering has been registered with the SEC or an exemption from registration is available.").

244. SEC, Registration Statement Under the Securities Act of 1933 (Form S-1), https://www.sec.gov/files/forms-1.pdf (listing all of the requirements for eligibility).

245. "For example, in 2014 only 3.5% of reported securities offerings were public offerings and only a fraction of those were with the required form S-1. The other 96.5% were offerings made pursuant to an exception to the registration requirement." Kyle Hulten, *Family and Friends Financing Round: Raising Capital from Non Accredited Investors*, VIGOR L. GRP.: THE CANAL ST. BLOG, https://www.invigorlaw.com/friends-and-family-financing-round/ (last visited May 21, 2021).

246. 17 CFR § 230.506 (2020).

247. Under existing Rule 501, a person qualifies as an accredited investor if he or she is either:

> Any natural person whose individual net worth, or joint net worth with that person's spouse, exceeds $1 million. . . .
>
> [or] who had an income in excess of $200,000 in each of the two most recent years or joint income with that person's spouse in excess of $300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year . . . .

Id. § 230.501.

In December 2020, at the time of writing this Article, the SEC adopted amendments to the accredited investor rule to add new categories of qualifying natural persons and entities and to make certain other modifications to the existing definition. According to the SEC:

> The amendments are intended to update and improve the definition to identify more effectively investors that have sufficient knowledge and expertise to participate in investment opportunities that do not have the rigorous disclosure and procedural requirements, and related investor protections, provided by registration under the Securities Act of 1993.

Order Designating Certain Professional Licenses as Qualifying Natural Persons for Accredited Investor Status, 85 Fed. Reg. 64,234, 64,234 (Oct. 9, 2020) (to be codified at 17 C.F.R. pt. 230).

> The amendments allow investors to qualify as accredited investors based on defined measures of professional knowledge, experience, or certifications in addition to the existing tests for income or net worth. The amendments also expand the list of entities that may qualify as accredited investors, including by allowing any entity that meets an investments test to qualify.

Press Release, SEC, SEC Modernizes the Accredited Investor Definition (2020), https://www.sec.gov/news/press-release/2020-191.

promoting investment in private offerings to encourage economic growth.[248] Notably, the SEC does not restrict investment in publicly traded companies.[249] An "accredited investor" is an individual or an entity that is presumed to not need the protection of federal or state securities laws based on their income or net worth.[250] In other words, an accredited investor's financial sophistication and ability to sustain the risk of loss of investment or ability to fend for themselves, as evidenced by their wealth, ostensibly renders the protections of the federal securities laws' registration process unnecessary.[251] Wealth is therefore a "proxy for sophistication."[252] Qualifying as an accredited investor is significant because accredited investors may, under SEC rules, participate in investment opportunities that are generally not available to non-accredited investors or "ordinary investors," such as investments in private companies and offerings by hedge funds, private equity funds, and venture capital funds.[253]

The SEC's "accredited investor standard" effectively means that only those with at least $1 million in assets or $200,000 in annual income can participate in private offerings.[254] Simply put, an accredited investor is someone who is quite wealthy. Accredited investor status is required for certain investments, such as angel investments, hedge funds, private equity, and others.[255] Because of the nature of private fundraising mechanisms and exemptions, the accredited investor standard has the effect of restricting most (87%) Americans from investment opportunities in Silicon Valley startups, or any startups for that matter.[256] The rules and regulations assume that only well-off individuals can

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248. Michael L. Monson, *The Evolution and Future of the Accredited Investor Standard for Individual*s, 23 UTAH BAR J.. Nov./Dec. 2010, at 36, 38.

249. *See* Paulina Likos, *How to Invest in the Private Market*, U.S. NEWS & WORLD REP. (Jan. 26, 2021, 3:56 PM), https://money.usnews.com/investing/investing-101/articles/how-to-invest-in-the-private-market.

250. *Id.* at 37.

251. Regulation D Revisions; Exemption for Certain Employee Benefit Plans, 52 Fed. Reg. 3,015, 3,015–22 (Jan. 30, 1987) (to be codified at 17 C.F.R. pts. 230, 239) (stating that the accredited investor standard is "intended to encompass those persons whose financial sophistication and ability to sustain the risk of loss of investment or ability to fend for themselves render the protections of the Securities Act's registration process unnecessary."); *see also* Fan, *supra* note 9, at 592 ("The theory behind Regulation D is that accredited investors are financially sophisticated and therefore do not need the protections of the securities laws.").

252. Syed Haq, Comment, *Revisiting the Accredited Investor Standard*, 5 MICH. BUS. & ENTREPRENEURIAL L. REV. 59, 69 (2015); *see also* Renee M. Jones, Essay, *The Unicorn Governance Trap*, 66 U. PA. L. REV. ONLINE 165, 186 (2017).

253. James Garrett Baldwin, *How to Become an Accredited Investor*, INVESTOPEDIA, https://www.investopedia.com/articles/investing/092815/how-become-accredited-investor.asp (Dec. 28, 2020) ("[T]he Securities and Exchange Commission (SEC) allows companies and private funds to skip the need to register certain investments as long as the firms sell these assets to accredited investors. Accredited investors are able to invest money directly into the lucrative world of private equity, private placements, hedge funds, venture capital, and equity crowdfunding." (footnote omitted)).

254. 17 C.F.R. §§ 230.501–.508 (2020).

255. Alexis Rhiannon, *Accredited Investors Have Access to Complex, Loosely Regulated Investments—Here's What It Takes to Qualify*, BUS. INSIDER (Apr. 27, 2021, 9:12 AM), https://www.businessinsider.com/accredited-investor ("[O]nce you become accredited, it 'unlocks' access to products not available to the general public, such as hedge funds, venture capital funds, private equity funds, and angel investing.").

256. Era Anagnosti, Colin J. Diamond, David Johansen & John R. Vetterli, *SEC: Time to Revamp Securities Offering Exemptions*, LEXOLOGY (July 23, 2019), https://www.lexology.com/library/detail.aspx?g=5945214c-

assess information to evaluate investment and they are sophisticated as evidenced by their wealth. As of 2015, 13% of households qualified as accredited investors under Rule 501(a)(6) of Regulation D.[257] Of those, only 1.3% are Black and 2.8% are Latinx.[258] "For [an entrepreneur] whose networks are largely rooted in Black and Latinx communities, that means less than 1% of the people 'like them' are allowed to invest freely."[259] In writing about her concerns regarding the accredited investor exemption generally, Professor Usha Rodrigues writes that, "the private and public markets have now grown radically disconnected and unequal."[260] The reason the SEC originally implemented such restrictive investor rules is because the SEC likely feared the majority of the population would be unsophisticated in their investments, sinking their savings into untested companies and losing money.[261] But the justification does not hold up when you realize that even certified public accountants, people with very high levels of proven competence and training, might not qualify today as an accredited investor without satisfying the minimum net worth requirement.[262] In the name of investor protection, the accredited investor rules bar the majority of communities of color from accessing opportunity for wealth formation.

Very little has been written on how these rules exacerbate racial and economic inequalities. While the SEC paternalistically attempts to distinguish between who can fend for themselves and who cannot, the real impact of the federal securities may be felt in the communities of color who, due to their economic status, are generally unable to access these markets.[263] What is at stake is equality of opportunity to grow and accumulate wealth. This phenomenon is a problem because the federal securities laws represent government regulation that perpetuates the ability for the wealthy to become wealthier and facilitates inequity in the opportunity to access the private financial markets.

2. General Solicitation

In addition to the accredited investor standard, before 2012 when the Jumpstart Our Business Startups Act of 2012 ("JOBS Act") was passed, the

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f980-4f26-a3ba-fdce62e42ae0; *see also* PK, *How Many Accredited Investors Are There in America? (2016)*, DQYDJ (Oct. 7, 2020), https://dqydj.com/2016-accredited-investors-in-america/ ("We estimate in 2016 there were 12,417,040 Accredited Investor Households in America, 9.86% of *all* American Households.").

257. Anagnosti et al., *supra* note 256.

258. Lichtenstern, *supra* note 227.

259. *Id.*

260. Usha Rodrigues, *Securities Law's Dirty Little Secret*, 81 FORDHAM L. REV. 3389, 3413 (2013).

261. *Id.*

262. Under the new rules, the SEC has determined that those with Series 7, 63, or 83 licenses qualify as accredited investors based on those licenses alone. *See* Press Release, *supra* note 247. Those with CFA and CFP designations have been considered as have licensed CPAs and attorneys, but ultimately those designations and licenses were not included in the new rule. Mat Sorensen, *SEC Expands Accredited Investor Rule*, ENTREPRENEUR (Sept. 1, 2020), https://www.entrepreneur.com/article/355590.

263. Leah Duncan, *Arbitrary Paternalism and the SEC Accredited-Investor Standard*, BLOG: MICH. J. RACE & L. (Dec. 4, 2018), https://mjrl.org/2018/12/04/arbitrary-paternalism-and-the-sec-accredited-investor-standard.

federal securities laws prohibited the general solicitation of the public in securities offerings.[264] Most of the exemptions from registration prohibit companies from engaging in general solicitation or general advertising—advertising in newspapers or on the Internet to the public in connection with securities offerings.[265] In other words, before 2012, private companies were only allowed to raise money from accredited investors and from those whom they had a substantial pre-existing relationship with or to whom they were introduced via a registered broker-dealer. The rationale for the ban on general solicitation was to protect unsophisticated investors from fraud due to lack of information, lack of education, or problematic disclosures.[266]

After 2012, the JOBS Act limited the removal of the ban on general solicitation. Primarily aimed at entrepreneurs seeking capital, the JOBS Act theoretically increases the ability of small businesses and startups to access capital and generate jobs through the use of crowdfunding.[267] Crowdfunding has the potential to mitigate some of the disparities between businesses that have access to capital and those that do not.[268] The reality, however, is that investment crowdfunding is not likely to democratize entrepreneurship. Given the extensive SEC regulatory requirements, it is unlikely that entrepreneurs will turn to investment crowdfunding to raise capital.[269] The JOBS Act was enacted to reduce regulatory burdens and increase initial public offerings (IPOs). According to Professor Renee Jones, the JOBS Act likely had the opposite effect and contributed to a new governance problem by "creating a class of unaccountable unicorns."[270]

It is difficult to determine the demographics of accredited investors, but investors in private and public offerings seem to be in the same category as in the private equity and venture capital space. In recent years, investment is very

264. *Fact Sheet: Proposing Amendments to Private Offering Rules*, SEC (July 10, 2013), https://www.sec.gov/news/press/2013/2013-124-item3.htm ("In April 2012, Congress passed the Jumpstart Our Business Startups Act (JOBS Act). Section 201(a)(1) of the JOBS Act directs the SEC to remove the prohibition on general solicitation or general advertising for securities offerings relying on Rule 506 provided that sales are limited to accredited investors and an issuer takes reasonable steps to verify that all purchasers of the securities are accredited investors.").

265. 17 C.F.R. § 230.502 (2020). For calculation purposes, the value of primary residence is excluded.

266. *See* Erin Griffith, *Does General Solicitation Matter for Tech Startups? Not Really*, PANDO (July 10, 2013), https://pando.com/2013/07/10/does-general-solicitation-matter-for-tech-startups-not-really.

267. *See* Christine Hurt, *Pricing Disintermediation: Crowdfunding and Online Auction IPOs*, 2015 U. ILL. L. REV. 217, 220 (2015).

268. *See* Andrew A. Schwartz, *The Digital Shareholder*, 100 MINN. L. REV. 609, 619–20 (2015) ("[C]rowdfunding can democratize the market for financing speculative companies by inviting ordinary people—'digital shareholders'—to make investments that are currently offered solely to accredited (wealthy) investors.").

269. *See* Lynnise E. Phillips Pantin, *What's Wrong with Jumpstart(ing) Our Business Startups (JOBS) Act?*, 16 N.Y.U. J.L. & BUS. 185, 191 (2019) ("[W]hile laudable steps have been taken to democratize the entrepreneurial ecosystem by implementing crowdfunding, isolated regulation such as the JOBS Act will do little to support entrepreneurs in their startup ventures, resulting in grave effects on this country's entrepreneurial ecosystem.").

270. Jones, *supra* note 252, at 170.

homogenous; venture capitalists, who are accredited investors and often lead the charge in early-stage investing, are 89% male.[271] According to the National Venture Capital Association/Deloitte Human Capital Survey, racial and ethnic groups are underrepresented in the Venture Capital workforce. Only 17% identified as Asian, with 4% identifying as African American, and 5% as Latino.[272] It's against that backdrop that venture capitalists choose their collaborators at other firms, investing their money side by side and joining the boards that guide the startups. Most investors specialize in a particular industry or sector, so potential partners are easy for researchers like us to identify: They are investing in the same types of deals at around the same time. And "venture capitalists are far more likely to partner with people if they share their gender or race."[273] There is a lack of data showing the demographics of investors strictly involved in private placement.

Based on Rule 506(c) of Regulation D, it seems unlikely that general solicitation meaningfully increases the percentage of investors of color. The rule "permits issuers to broadly solicit and generally advertise an offering, provided that (1) all purchasers in the offering are accredited investors." This confines eligible investors to the categories mentioned above. Due to the level of wealth disparity in our country in relation of race, it is unlikely that the requirements of general solicitation help increase the percentage of investors of color. This is the landscape on which startups incubate, operate, and scale on the path to creating a unicorn. Entrepreneurs are required to raise money in a very insular and homogenous private investment market. The effect of these rules is economic exclusion of people of color. Nonaccredited investors miss out on the privilege of investing in the private market, and entrepreneurs miss out on benefiting from their potential investment.

3. *The Wealth Gap and Its Implications for Bootstrapping*

This country has a profound and seemingly insurmountable wealth gap that falls along racial lines. "Differences in economic outcomes by race have persisted for centuries in the United States and continue up to the present day. For example, in 2016, the median household income of black Americans was \$39,500, compared with \$65,000 for non-Hispanic white Americans."[274] According to the Federal Reserve, in 2016, the median wealth of white families was ten times the wealth of Black families and eight times that of Latino families.[275] This wealth gap affects entrepreneurship in profound ways.

271. DELOITTE, *supra* note 116, at 6.

272. *Id.* at 8.

273. Paul Gompers & Silpa Kovvali, *The Other Diversity Dividend*, HARV. BUS. REV. (July–Aug. 2018), https://hbr.org/2018/07/the-other-diversity-dividend.

274. Raj Chetty, Nathaniel Hendren, Maggie R. Jones & Sonya R. Porter, *Race and Economic Opportunity in the United States: An Intergenerational Perspective*, 135 Q.J. ECON. 711, 712 (2020) (citations omitted).

275. Rakesh Kochhar & Anthony Cilluffo, *How Wealth Inequality Has Changed in the U.S. Since the Great Recession, by Race, Ethnicity and Income*, PEW RSCH. CTR. (Nov. 1, 2017), https://www.pewresearch.org/fact-

Although the numbers are on the rise, successful founders of color are largely absent in entrepreneurship, citing a lack of access to capital compared to their white counterparts.[276] The wealth disparity has implications for bootstrapping, the traditional path outside of seeking private investment that entrepreneurs take toward fundraising.[277] The expectation of bootstrapping and relying on friends and family stems from bias toward wealth. However, when entrepreneurs of color reach out to their friends and family for the seed capital to initially fund their venture, they are already behind their white counterparts because of the wealth and income gap.[278] Bootstrapping and fundraising through their social network is essentially a myth for entrepreneurs of color. With the limits on generational wealth, it is unlikely that the friends and family of entrepreneurs of color can invest on the level of their white counterparts.

It is hard for entrepreneurs of color to fundraise as evidenced by how few founders of color receive private investment. Beyond bootstrapping, minority women founders make up only 3% of all U.S. angel-backed deals, and minority men were 13% of all U.S. angel-backed deals in 2019.[279] Further, in 2018, just 3% of venture capitalists are Black, 1% are Latinx, and 18% of all venture capitalists are women.[280]

White (mostly male) entrepreneurs have more access to capital than any other group. As of 2017, only sixteen Black women-led companies had raised over a million dollars in venture capital funding.[281] Capital raised by Black

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tank/2017/11/01/how-wealth-inequality-has-changed-in-the-u-s-since-the-great-recession-by-race-ethnicity-and-income.

276. *See* Kathleen Janus, *Funders Must Give Minority Founders a Fair Deal*, TECHCRUNCH (Oct. 15, 2016, 1:00 PM), https://techcrunch.com/2016/10/15/funders-must-give-minority-founders-a-fair-deal (exploring the reasons why Black founders receive less than one percent of VC funding).

277. Alejandro Cremades, *The Pros and Cons of Bootstrapping Startups*, FORBES (Jan. 13, 2019, 7: 53 AM), https://www.forbes.com/sites/alejandrocremades/2019/01/13/the-pros-and-cons-of-bootstrapping-startups/#475be957273d ("Bootstrapping a startup means starting lean and without the help of outside capital. It means continuing to fuel growth internally from cash flow produced by the business. Many sizable businesses started out bootstrapping. Some have just made it happen on their own. Others have eventually taken offers of outside investment.").

278. *See* KIM PARKER, JULIANA HOROWITZ & BRIAN MAHL, PEW RSCH. CTR., ON VIEWS OF RACE AND INEQUALITY, BLACKS AND WHITES ARE WORLDS APART 24 (2016), https://www.pewsocialtrends.org/2016/06/27/1-demographic-trends-and-economic-well-being (click "Complete Report PDF" to download) (highlighting the wealth disparity between Black and white families, revealing a difficulty for black entrepreneurs to receive funding from family members) ("In 2013, the net worth of white households was $144,200, roughly 13 times that of black households, according to Pew Research Center analysis of data from the Federal Reserve's Survey of Consumer Finances.").

279. ANGEL RES. INST. & PITCHBOOK, HALO REPORT: ANNUAL REPORT ON ANGEL INVESTMENTS 15 (2020), https://angelresourceinstitute.org/reports/HALO-2019-%20October-2020-Update.pdf.

280. Richard Kerby, *Where Did You Go to School?*, NOTEWORTHY—THE J. BLOG (July 30, 2018), https://blog.usejournal.com/where-did-you-go-to-school-bde54d846188.

281. *See* DIGITALUNDIVIDED, THE STATE OF BLACK WOMEN FOUNDERS: PROJECTDIANE 2018, at 3 (2018) (on file with author). In 2018, this number grew to thirty-four Black female founders, and in 2020, ninety-three Black female founders secured $1 million in investor backing. Emma Hinchliffe, *The Number of Black Female Founders Who Have Raised More Than $1 Million Has Nearly Tripled Since 2018*, FORTUNE (Dec. 2, 2020, 10:39 AM), https://fortune.com/2020/12/02/black-women-female-founders-venture-capital-funding-vc-2020-project-diane.

women represented 0.06% of the $424.7 billion in total venture funding raised since 2009, and a majority of that funding was raised in 2017.[282] Juxtapose this with Elizabeth Holmes, who took her college tuition money from her parents and leveraged that trust fund to make her first million.[283] Holmes had access to all kinds of accredited investors in her network. One of her first investors, for example, Tim Draper, of famed venture capital firm Draper Fisher Jurvetson, was a family friend.[284] This Subpart described how the structures of financing restrict access to the rich, white and privileged. The next Subpart describes how cultural capital creates circles of power among the wealthy and elite.

B. Cultural Capital

Financial capital is a big part of startup success, but so is a form of hidden capital or cultural capital. Cultural capital is the background, occupation, gender, age, education, or other aspect about a person that gives them access to certain social groups or status.[285] Accessing cultural capital can lead to opportunities and advantages gained for possessing cultural capital.[286] Entrepreneurs often have success because they are able to tap into this cultural capital.[287] Beyond financial capital, cultural capital shapes the entrepreneurship game and influences who achieves success and who does not. The hidden nature of cultural capital means that some groups benefit unfairly from possessing it when others do not. In Silicon Valley, whiteness and maleness are undeniable assets. If an entrepreneur happens to be white, male, wealthy, and college-educated, cultural capital will probably get that entrepreneur in front of more venture capitalists and investors than an entrepreneur who is not all of those things. If that entrepreneur attended Harvard or Stanford, then that entrepreneur has even more access to cultural capital than most.[288] Richard Kerby found that in a study of about 1,500 venture investors, forty percent of venture investors attended Stanford or Harvard.[289] The implications of this are complicated. There is danger

282. DigitalUndivided, *supra* note 281, at 3.

283. Auletta, *supra* note 151.

284. *The Inventor: Out for Blood in Silicon Valley*, *supra* note 24.

285. Annette Lareau & Elliot B. Weininger, *Cultural Capital in Educational Research: A Critical Assessment*, 32 Theory & Soc'y 567, 570–73 (2003) (discussing dominant interpretations of cultural capital).

286. *See* Chris Rabb, Invisible Capital: How Unforeseen Forces Shape Entrepreneurial Opportunity 93 (2010).

287. Malgorzata A. Wdowiak, Erich J. Schwarz, Robert J. Breitenecker & Richard W. Wright, *Linking the Cultural Capital of the Entrepreneur and Early Performance of New Ventures: A Cross-Country Comparison*, 17 J. E. European Mgmt. Stud. 149, 149 (2012) (finding that entrepreneurial performance in new ventures is culture-driven).

288. *See* PitchBook, Universities Report 4 (2016–17 ed.), https://pitchbook.com/news/reports/2016-2017-pitchbook-universities; Lydia Belanger, *You're More Likely to Get Startup Funding If You Went to One of These Schools*, Yahoo!News (Sept. 9, 2016), https://nz.news.yahoo.com/amphtml/news/youre-more-likely-startup-funding-154500508.html ("Taking into account the number of entrepreneurs and companies a school has produced, as well as the amount of venture capital its undergraduate alumni have raised, PitchBook's primary ranking puts Stanford University at number one. The Silicon Valley university has produced 1,006 entrepreneurs who have raised more than $18.1 billion.").

289. Kerby, *supra* note 280.

in the idea that a handful of universities, alums, and affiliates control the startup economy. This phenomenon makes startup culture a closed community for a certain brand of endorsed elites.[290] The money and power are flowing among people who already have it.[291]

Cultural capital is born out of systemic racial and social inequality. The use of cultural capital "illuminates how the rich and well connected occupy different strata of life, enjoy a completely different set of opportunities from the rest of us, experience a different kind of justice, and are so often immune from consequences."[292] The problem with capitalizing on cultural capital is that there is little vetting that occurs when you take advantage of these relationships. The next Subpart describes how the market incentivizes racism among the actors in the financial system.

C. Market Incentives Drive Racist and Classist Outcomes

Defenders of Silicon Valley culture may raise several counterarguments about the central premise of this Article. These arguments may include that current norms are optimally designed to incent innovation; that some founders truly are visionaries that improve society even if they create toxic work environments; that the market is the most efficient way to allocate resources and should consider distributional equity; and finally, that the lack of diversity in Silicon Valley is merely a pipeline problem. Yet, there are many examples of the ways that a lack of representation of communities of color in the startup space is connected to structural racism. Brief and explicit engagement with these arguments may help convince the reader that a deeper problem lies within the culture of Silicon Valley itself. This Article specifically references Silicon Valley, but the themes discussed in this Article have implications beyond a critique of Silicon Valley. Fundamentally, this critique of a purported meritocracy can be applied to every place in society that says it operates as a meritocracy—for example, college admissions, tech company workplaces, and even legal academia. The larger lesson to be drawn from Theranos is that we need to care about these issues in Silicon Valley, not just for the health of our economy, but for the health of society.

Economic racism shuts out communities of color from startup investment opportunities. Ventures owned by people of color lack sufficient funding, typically due to lack of access to venture capital and/or small business loans.[293]

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290. Yu, *supra* note 6; *see* Hennessey, *supra* note 6 ("[Elitism] is found too often among entrepreneurs, particularly in tech startups. The myopia, the drive that fuels people to take risks, often creates great companies and great products, but it also cultivates a solipsism that assumes the work the entrepreneur is doing, and the way in which that work is being done, is the only important undertaking in the world.").

291. HWANG ET AL., *supra* note 61.

292. Asher-Schapiro, *supra* note 38.

293. In a Kauffman Foundation analysis of a 2014 Census Bureau survey, 28.4% of Black entrepreneurs reported that their profits were hurt by lack of access to capital, compared with 10.1% of white entrepreneurs. ALICIA ROBB & ARNOBIO MORELIX, KAUFFMAN FOUND., STARTUP FINANCING TRENDS BY RACE: HOW ACCESS

Underfunding limits a business' ability to launch, scale, and grow. Limitations on fundraising and access to capital is one part of the problem.[294] But the system in place for creating and supporting entrepreneurs favors white males at the outset.

There is deep bias within the Silicon Valley community that manifests as racism. The economic racism experienced by entrepreneurs of color is not likely to be addressed, since it occurs in the private market space.[295] There is no legal strategy to ensure that people of color have an equal opportunity to share in wealth creation. In fact, fighting economic discrimination is a difficult legal battle. The facts underlying the case in *Comcast Corp. v. National Association of African American-Owned Media* is analogous here. In that case, Byron Allen, who is Black and the founder of Entertainment Studios, sued cable television companies Comcast and Charter after the providers refused to carry Allen's channels.[296] Allen alleged claims of racial discrimination under § 1981 of the Civil Rights Act,[297] which, among other things, gives all races an equal right to make and enforce contracts.[298] The statute also requires proving that defendants were not just biased, but intentionally racist.[299] In its complaint, Allen's company, Entertainment Studios, presented specific factual allegations

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TO CAPITAL IMPACTS PROFITABILITY 6 (2016), https://www.kauffman.org/wp-content/uploads/2019/12/ase_brief_startup_financing_by_race.pdf.

294. *See* RATEMYINVESTOR, *supra* note 58, at 8 (showing that only one percent of VC money goes to companies founded by Black entrepreneurs).

295. According to a recent report by the *Washington Post*:

> More than a dozen black entrepreneurs, most of whom spoke on the condition of anonymity for fear of retribution, said in interviews that deeply ingrained racism plays a role in the low levels of funding for black entrepreneurs. Several entrepreneurs described being mistaken for delivery workers when they arrived for scheduled pitch meetings with venture capitalists. In one group of black tech employees who share stories online, an entrepreneur described being asked by a venture capitalist to "tone down the black."

Reed Albergetti, *Black Start-Up Founders Say Venture Capitalists Are Racist, but the Law Protects Them*, WASH. POST (July 22, 2020, 4:00 AM), https://www.washingtonpost.com/technology/2020/07/22/black-entrepreneurs-venture-capital/.

296. Comcast Corp. v. Nat'l Ass'n of African Am.-Owned Media, 140 S. Ct. 1009, 1013 (2020).

297. *Id.* This law, codified at 42 U.S.C. § 1981, prohibits discrimination against African Americans and other people of color in employment, housing, banking, consumer transactions, and in all other contractual relationships.

298. 42 U.S.C. § 1981. First, the Civil Rights Act of 1866 (which contained the original version of the law now codified at § 1981) proclaimed "[t]hat *all persons* born in the United States . . . are hereby declared to be citizens of the United States." Civil Rights Act of 1866, ch. 31, § 1, 14 Stat. 27, 27 (1866) (current version at 42 U.S.C. § 1981) (emphasis added). Second, the Act specifically defined the rights of American citizenship:

> [S]uch citizens, of every race and color, without regard to any previous condition of slavery or involuntary servitude . . . shall have the same right, in every State and Territory in the United States, to make and enforce contracts, to sue, be parties, and give evidence, to inherit, purchase, lease, sell, hold, and convey real and personal property, and to full and equal benefit of all laws and proceedings for the security of person and property, as is enjoyed by white citizens, and shall be subject to like punishment, pains, and penalties, and to none other, any law, statute, ordinance, regulation, or custom, to the contrary notwithstanding.

Id.

299. *See Comcast Corp.*, 140 S. Ct. at 1019.

supporting its claim that Comcast was motivated by racial discrimination in refusing to carry Entertainment Studios' channels.[300] The question before the Supreme Court was whether, in addition to pleading that racial discrimination was a "motivating factor" for Comcast's conduct, Entertainment Studios also had to plead that Comcast's racial discrimination was the but-for cause of its denial of a contract right to Entertainment Studios.[301] Comcast argued that Allen must prove Entertainment Studios would have earned the contract, were it not for race.[302] The Supreme Court unanimously agreed with Comcast and rejected the Court of Appeals for the Ninth Circuit's approach that it was sufficient to allege that race was a "motivating factor" for the denial of the contract, in favor of a "but-for" test for causation.[303] As Justice Sandra Day O'Connor recognized in her concurring opinion in *Price Waterhouse v. Hopkins*, the but-for test "demand[s] the impossible."[304]

The *Comcast* ruling has implications not only for entrepreneurs in Silicon Valley alleging discrimination, but for future civil rights litigation. There is now an even higher standard to prove racial discrimination in Silicon Valley. Instead of considering the statistical evidence that reveals the racial disparity for Black entrepreneurs, courts will more likely weigh their decisions based on a hypothetical situation in which the plaintiff's racial identity is erased and all other factors remain the same. This dangerously narrows the interpretation of the Civil Rights Act of 1866.[305] Silicon Valley investors and leaders will rely on the heightened standard when facing a claim of discrimination from entrepreneurs of color.

D. THERANOS HIGHLIGHTS STRUCTURAL BIAS AND INEQUALITY IN THE PRIVATE MARKET SYSTEM

The story of Theranos provides an opportunity to examine the ways that cultural capital influences entrepreneurship. Elizabeth Holmes held tremendous amounts of cultural capital that she was able to leverage in order to catapult her company into a unicorn. The idea that a nineteen-year-old college dropout with very limited chemical engineering training and no medical training could invent something as game-changing as what Theranos claimed it had done defies belief. But Elizabeth Holmes was believed. Not only was she believed, but she was

300. *Id.* at 1014.

301. *Id.*

302. *Id.* at 1013.

303. *Id.* at 1014–15.

304. Price Waterhouse v. Hopkins, 490 U.S. 228, 264 (1989) (O'Connor, J., concurring) (quoting Wex S. Malone, *Ruminations on Cause-in-Fact*, 9 STAN. L. REV. 60, 67 (1956)).

305. *See* Erwin Chemerinsky, *A Major Step Backwards for Civil Rights:* Comcast v. National Association of African American-Owned Media, AM. CONST. SOC'Y, https://www.acslaw.org/a-major-step-backwards-for-civil-rights-comcast-v-national-association-of-african-american-owned-media/ (last visited May 21, 2021) ("Obviously, the Court's decision in *Comcast* will make it more difficult for § 1981 plaintiffs to withstand a motion to dismiss and ultimately to prevail. Alleging and proving but-for causation is much harder than alleging and proving that race was a motivating factor in the denial of the contract.").

revered as a once-in-a-generation genius. One of the reasons why no one was skeptical of her is because she had tapped into her cultural capital and was vouched for by a trusted friend. It is also worth emphasizing here that Holmes made herself and indeed was the face and a key gatekeeper at Theranos. This was not an instance where someone with the connections, financial backing, and managerial skills worked to build bridges and bring the requisite expertise in the room. She, along with Balwani, cast themselves and indeed operated as the experts in the room.

There has been some commentary that Theranos' Board and investors were seduced by Elizabeth Holmes because she was a young, beautiful woman,[306] but I would argue that if they were seduced at all, they were likely seduced by her Stanford pedigree. Many of the company's Board members and investors were fellows at the Hoover Institute, former cabinet members, and military officers, including George Shultz, James Mattis, Henry Kissinger, William Perry, Sam Nunn, and Gary Roughead.[307] They all had some type of connection to Stanford University.[308]

Stanford University has produced more unicorn founders than any other university and to this day continues to play a large role in creating unicorns.[309] A connection to Stanford carries significant cultural capital and connections to the elite, monied, influential actors within Silicon Valley.[310] Elizabeth Holmes, who was not even a Stanford graduate, but a dropout, was able to tap into the incredible resources of the Stanford entrepreneurial ecosystem and gain access

306. *See, e.g.*, Leah Garchik, *Money, Medicine and a Good-Looking Woman: The Fall of Theranos*, S.F. CHRON. (Mar. 14, 2019), https://www.sfchronicle.com/leahgarchik/article/Money-medicine-and-a-good-looking-woman-the-13687000.php ("Holmes is a glamorous young woman, whose intense blue-eyed stare (she never blinked, said a Theranos employee) and trademark black turtlenecks were much admired in Silicon Valley. This, it was agreed upon in a panel discussion that followed the showing [of the Theranos HBO documentary], was part of the lure for investors and board members, most of whom—George Shultz, Henry Kissinger, Rupert Murdoch among them—were older men, seduced not only by her self-proclaimed genius but also by her youth and looks.").

307. Richard Beales, *How Theranos Hoovered up $9 Bln of Influence*, REUTERS (Oct. 27, 2015), https://www.reuters.com/article/idUS334041731220151027; Pflanzer, *supra* note 148.

308. *See* McKenna, *supra* note 208 ("Theranos investor list is a who's-who of Stanford University alumni . . . .").

309. In March 2019, Bloomberg reported that more than one out of ten unicorn founders went to Stanford. Sophie Alexander & Reade Pickert, *The Good and the Bad of Stanford's Massively Successful Startup Scene*, BLOOMBERG (Mar. 11, 2019), https://www.bloomberg.com/news/articles/2019-03-10/dreamers-and-dropouts-stories-from-stanford-cradle-of-unicorns; *see also* Larry Kim, *Billion-Dollar Unicorn Founders Came from These Universities, in Case You Were Curious*, MEDIUM (Mar. 20, 2018), https://medium.com/marketing-and-entrepreneurship/billion-dollar-unicorn-founders-came-from-these-universities-in-case-you-were-curious-398665cc82c4 ("The top school on the list, Stanford University, claims 51 unicorn founders as alumni while runner-up Harvard University has 37.").

310. *See* Ritika Trikha, *The Interdependency of Stanford and Silicon Valley*, TECHCRUNCH (Sept. 4, 2015, 5:00 PM), https://techcrunch.com/2015/09/04/what-will-stanford-be-without-silicon-valley ("In return, its entrepreneurial alumni offer among the most generous endowments to the university, breaking the record as the first university to add more than $1 billion in a single year. Stanford shares a relationship with Silicon Valley unlike any other university on the planet, chartering a self-perpetuating cycle of innovation.").

to those who would become her advisors, investors, board members, and employees.

Confirmation bias born out of cultural capital was a phenomenon that played out in the media as well. In 2014, she landed a cover story with *Fortune Magazine*. John Carreyrou wrote that since the author of the piece that publicly launched her and Theranos into stardom, Roger Parloff, the writer for *Fortune*, "didn't have the expertise to vet her scientific claims, Parloff interviewed and effectively relied on the dominant members of her Board of Directors as character witnesses."[311]

Since she was childhood friends with the daughter of billionaire venture capitalist Tim Draper, she was able to raise her first million dollars.[312] The investment by Tim Draper ostensibly gave her credibility for future investors. Once other investors saw Draper's endorsement, they were eager to invest; it did not seem to matter that health tech venture capital firms had passed on the venture.[313] Through tapping into the cultural capital afforded her by her connection to Stanford, Elizabeth Holmes had a level of access to investors and venture capital that is atypical for most startup founders in this country.[314] At the age of twenty-two, she was pitching to Novartis;[315] at twenty-five, she was pitching to the Safeway and Walgreens CEOs to develop hundred-million-dollar deals that would put Theranos in Safeway and Walgreens stores.[316] That access to those stores then led her to use those pitches to increase the valuation of her company to $165 million based on deals with pharmaceutical companies (note that these deals did not actually exist).[317] Theranos raised $700 million of private investment money from 2003 to 2015.[318] By 2014, the company was valued at $9 billion, and Holmes was lauded as the first woman billionaire tech founder.[319]

311. CARREYROU, *supra* note 16, at 207.

312. *Id.* at 15.

313. *See* Polina Marinova, *Why VC Tim Draper Keeps Defending Theranos CEO Elizabeth Holmes*, FORTUNE (May 11, 2018, 7:52 AM), https://fortune.com/2018/05/11/tim-draper-theranos-elizabeth-holmes/; Peter Cohan, *How Theranos' Big Investors Were Taken*, FORBES (Dec. 1, 2016, 8:23 AM), https://www.forbes.com/sites/petercohan/2016/12/01/how-theranoss-big-investors-were-taken/#4fd95c315f4f (highlighting parallels between Bernie Madoff and Holmes in their ability to manipulate investors).

314. Major investments were made by the Walton family ($150 million), Rupert Murdoch ($121 million), Betsy DeVos ($100 million), and the Cox family of Cox Media Group ($100 million). John Carreyrou, *Theranos Cost Business and Government Leaders More Than $600 Million*, WALL ST. J. (May 3, 2018, 8:01 PM), https://www.wsj.com/articles/theranos-cost-business-and-government-leaders-more-than-600-million-1525392082.

315. *See* Meagan Parrish, *Reliving Biotech's Most Shocking Scandal—The Story of Theranos*, PHARMA MFG. (Apr. 17, 2019), https://www.pharmamanufacturing.com/articles/2019/reliving-biotechs-most-shocking-scandal-the-story-of-theranos (mentioning that Holmes and Theranos executives flew to Switzerland in 2006 to demo their technology to Novartis).

316. *See id.*

317. CARREYROU, *supra* note 16, at 182; Mitch Rencher, *Bad Blood*, MEDIUM (Feb. 25, 2019), https://medium.com/@mitchrencher/bad-blood-af5b519e1045.

318. Press Release, *supra* note 31.

319. Kevin Loria, *This Woman's Revolutionary Idea Made Her a Billionaire—And Could Change Medicine*, BUS. INSIDER (Sept. 29, 2014, 4:23 PM), https://www.businessinsider.com/theranos-founder-elizabeth-holmes-is-a-billionaire-2014-9.

The list of investors in Theranos was made up of heavy hitters (for example, the DeVos Family, Rupert Murdoch, and the Walton Family), all of whom had heard about the investment by word of mouth.[320] Elizabeth Holmes raised hundreds of millions of dollars from investors enchanted by her pitch. More significantly, the investors had access to the investment because their wealthy friends and connections knew about it. If this was a good investment opportunity, it would have made these investors a lot more money, perpetuating circles of wealth and power, and the ordinary investors would not have had access to the investment opportunity.

Besides perpetuating and contributing to structural privilege, the problem with Elizabeth Holmes tapping into the cultural capital afforded to her because of her connection to Stanford is that her company and its claims were given the benefit of the doubt because of how class functions to reinforce perceptions of Holmes as a mythic entrepreneur.

Startup culture's tacit endorsement of Elizabeth Holmes was pivotal to her success. Arguably, Holmes cultivated Theranos and her persona to conform to startup culture and secure this endorsement. She created the company in the heart of Silicon Valley on Stanford's campus, and then moved offices to inhabit Facebook's former headquarters. She got the idea for her company while she was at Stanford University studying biomedical engineering. In a culture where hyping your product to get funding while also concealing its true developmental progress and hoping reality catches up to that hype is normative and there is private investment available in abundance to Stanford-affiliated founders of ventures disrupting industries, it is easy to see why Holmes was able to raise so much money so easily. Fraud and deception aside, the startup culture created by Silicon Valley and the common methods of fundraising, the homogeneity of the Board, groupthink, implicit bias, pattern matching, and certain opportunities that are concentrated within an elite circle generated an environment out of which Theranos was born.

Despite her disgrace, the capital-raising success of Elizabeth Holmes, who created a unicorn company in ten years' time, remains a lesson in the ways that race, privilege, and wealth dictate startup success and perpetuates itself within circles of power. Most entrepreneurs do not have access to the traditionally

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320. *See* Reed Abelson & Katie Thomas, *Caught in the Theranos Wreckage: Betsy DeVos, Rupert Murdoch and Walmart's Waltons*, N.Y. TIMES (May 4, 2018), https://www.nytimes.com/2018/05/04/health/theranos-investors-murdoch-devos-walmart.html; *see also* Peter Cohan, *How Theranos's Big Investors Were Taken*, FORBES (Dec. 1, 2016), https://www.forbes.com/sites/petercohan/2016/12/01/how-theranoss-big-investors-were-taken/#24612ac45f4f ("[A] veteran medical technology investor concludes that there may be two big reasons they agreed to invest in Theranos—it seemed to offer a compelling mission to the managers of their family offices and they assumed that with all the luminaries associated with Theranos, someone must have done their due diligence on its product"). Powerful and rich investors brought in their rich and powerful friends to join in the scheme to make more money together. For example, Larry Ellison brought in his friend Don Lucas. Sara Ashley O'Brien, *Elizabeth Holmes Surrounded Theranos with Powerful People*, CNN (Mar. 15, 2018, 6:43 PM), https://money.cnn.com/2018/03/15/technology/elizabeth-holmes-theranos/index.html.

white, male networks that Holmes relied on for funding, and most investors do not have access to the private market of pre-IPO startups.

III. ADVANCING RACIAL EQUITY AND ECONOMIC INCLUSION IN THE STARTUP SPACE

The themes raised in this Article are informed by the racial wealth divide, which has been created and maintained by public policies that span the history of this country. Economic racism and the implicit bias prevalent within Silicon Valley will not change without structural reforms to the private financial markets system. However, a detailed discussion of policy proposals is outside of the scope of this Article. Instead, offered below is a discussion of the necessity to find a path forward with some ideas of areas for consideration, which fall into the following categories: the potential of legal reform, the potential of government programming, and the potential of private actors.

A. THE POTENTIAL OF LEGAL REFORMS

The downfall of the Theranos fraud is significant beyond the collateral financial cost to its large investors. Theranos' downfall had a domino effect affecting its employees and the patients upon which the product was used. The company's fraud put ordinary consumers at risk, and it begs the question of what the role should be of the government in the regulation of unicorn companies. It is worth exploring the need for heightened regulatory oversight of certain investment bodies, including venture capital firms or of board membership of large, privately held companies. The private markets have demonstrated being incapable of making changes without an intervention. If the government starts to regulate unicorns and others who aspire to the unicorn designation, those companies may begin to implement such strategies when they are startups rather than waiting until they reach unicorn status. Perhaps such exploration might reveal the need to replicate nationally some of the various state laws described below that were implemented in an effort to diversify private company boards.

1. Federal Regulation

The SEC is already watching companies that stay private and are not subject to extensive securities law disclosures required of public companies.[321] Beyond watching the companies, it may prove useful for the government to begin to compile and analyze data relevant to unicorn companies, which would include data about the diversity of the companies, their boards, and their investors.

321. *See* Lizetta Chapman & Kartikay Mehrotra, *Investors Warn Unicorns: Share Info Evenly or Get Sued*, Bloomberg (June 13, 2016, 2:23 PM), https://www.bloomberg.com/news/articles/2016-06-13/investors-warn-unicorns-share-information-evenly-or-get-sued; *see also* Kevin M. LaCroix, *SEC Warning: It Is Watching Private Companies*, D&O DIARY (Apr. 6, 2016), https://www.dandodiary.com/2016/04/articles/securities-laws/11893/.

2. *State Regulation*

Selecting board members in tech startups is an informal process where "candidates advertise themselves [and] founders ask around . . . . And given the demographics of Silicon Valley's elite, it has favored white men."[322] Diversification in board composition has been a trending topic and has been a recent focus of the SEC as well as regulators in various states.[323] Changes made at the state level to diversify the make-up of the boards of private companies could have potential to bring about change to the status quo. For example, the state of California passed a new law[324] requiring that public corporations incorporated in California or whose principal executive offices are located in California have a mandated minimum number of female directors.[325] Five other states (Colorado, Illinois, Massachusetts, Pennsylvania and Ohio) have passed nonbinding resolutions urging companies in their states to add women to their boards.[326] According to the most recent report by the California Secretary of State, around fifty percent of public companies in California are compliant with the gender rule.[327]

B. THE POTENTIAL OF GOVERNMENT PROGRAMS

The ways that economic racism has effectively shut out communities of color from startup investment opportunities is deeply troubling and the evidence provided above paints a clear need for change. As illustrated above, entrepreneurs of color are not likely to have access to capital and networks that might yield investments. Possible solutions to consider might be the creation of fund structures that replicate "friends and family" investments for lower-income and lower-wealth entrepreneurs. Additionally, something worthy of considerations are programs that formalize mechanisms to mentor and support entrepreneurs of color.

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322. Vauhini Vara, *How the Boardlist Plans to Get More Women onto Startup Boards*, FAST CO. (Apr. 18, 2016), https://www.fastcompany.com/3058458/how-the-boardlist-plans-to-get-more-women-onto-startup-boards.

323. *See* Dicker et al., *supra* note 159.

324. S.B. 826, Gen. Assemb., Reg. Sess. (Cal. 2018) (amending California's General Corporation Law). The law requires that by the end of 2019, corporations must have one female director. In addition, by the end of the 2021 calendar year, any such corporation must have a minimum of two female directors, if its number of directors is five; or a minimum of three female directors if its number of directors is six or more. *Id.*

325. *Id.*

326. H.J.R. 17-1017, 71st Gen. Assemb., Reg. Sess. (Co. 2017); H.R. 0439, 99th Gen. Assemb., Reg. Sess. (Ill. 2015); S. Res. 1007, 189th Gen. Ct., Reg. Sess. (Mass. 2015); H.R. 114, Gen. Assemb., 2019–2020 Reg. Sess. (Pa. 2019), H.R. 344, 131st Gen. Assemb., 2015–2016 Reg. Sess. (Ohio 2016).

327. *See* SHIRLEY N. WEBER, CAL. SECRETARY OF STATE, WOMEN ON BOARDS (2021), https://bpd.cdn.sos.ca.gov/women-on-boards/wob-report-2021-02.pdf; *see also* Cydney Posner, *California Posts New Report on Board Gender Diversity—What Does It Tell Us?*, Cooley PubCo (Mar. 25, 2021), https://cooleypubco.com/2021/03/15/california-report-board-gender-diversity/.

C. Potential for Private Market Participants

The major focus of this Article has been on the private actors who funded Theranos and who are largely responsible for crowning unicorns. For those individuals or companies who wish to mitigate some of what has been described in this Article,[328] I offer a few considerations: invest in founders of color, put people of color on boards, and embrace antiracism as a guiding principle.[329] In this Article, I have situated the problem in the context of cognitive biases and market-based incentives in Silicon Valley that have led to economic racism. Firms and investors interested in changing the phenomenon described herein might wish to counteract bias by evaluating their portfolios, examining the percentages of women and founders of color-led businesses, and increasing those numbers. They may also wish to expand and develop concrete criteria for evaluating investment opportunities and founders in a way that moves away from pattern matching or valuing entrepreneurs based on their pedigree, changing their frame of reference and focusing on the opportunity. Additionally, limited partners who invest in a particular fund of a venture capital firm could insist on language in their respective limited partnership agreements to encourage the venture capital firm to invest in companies led by founders of color.

Conclusion

Silicon Valley, a fifty-square-mile region in the San Francisco Bay Area, "has created more wealth than any place in human history."[330] Given the wealth creation derived from Silicon Valley, it is hard to make a case for changing the culture, but in the end representation matters. It is necessary to tear down the post-racial myth of unicorns and show the places where homogeneity and lack of diversity create and perpetuate inequity.

As of the writing of this Article, the country is in the middle of a global pandemic, due to the spread of the coronavirus, and a racial reckoning, which includes a racial economic reckoning for our institutions. Racial equity is tied to economic inclusion and economic opportunity. Some of that reckoning is happening now, or has happened relatively recently, with respect to Silicon Valley's prized unicorns. The Theranos trials are approaching, WeWork unraveled most recently, and Uber has been under fire especially in the past three to four years. In addition to that economic reckoning, the global coronavirus

328. *See* Press Release, Apple, Inc., Apple Launches Major New Racial Equity and Justice Initiative Projects to Challenge Systemic Racism, Advance Racial Equity Nationwide (Jan. 13, 2021), https://www.apple.com/newsroom/2021/01/apple-launches-major-new-racial-equity-and-justice-initiative-projects-to-challenge-systemic-racism-advance-racial-equity-nationwide/.

329. During the 2008 Recession, companies with diverse boards and leadership performed better than less inclusion companies. *See* Ed Frauenheim & Nancy Cesena, *New Study Reveals That Diversity and Inclusion May Be the Key to Beating the Next Recession*, FORTUNE (Dec. 20, 2019), https://fortune.com/2019/12/20/diversity-inclusion-key-to-beating-next-recession/amp/.

330. Bilton, *supra* note 164.

pandemic will have an effect on the issues raised in this Article. The coronavirus crisis is compounding the deeply-entrenched inequities in our society—inequities rooted in structural racism. Businesses owned by people of color have been affected the most.[331] In thinking about the state of entrepreneurship post-pandemic, the concepts explored in this Article regarding institutional bias should very much be front and center, particularly as ventures owned by founders of color will be disproportionately impacted by the ongoing economic crisis rooted in the pandemic.[332] What will be needed are real, concrete solutions. Efforts cannot be band-aid solutions to a gaping economic wound.

The underrepresentation of people of color in the entrepreneurship ecosystem represents the loss of a multi-billion-dollar business opportunity.[333] The barriers to entry are structural and cultural for entrepreneurs of color, and the loss is incalculable in ways that are not quantifiable. Professor Jennifer Fan raises a prescient question: "for all the wonderful new technology and innovations that have been brought by [technology companies], how many more could we have had if entrepreneurs and investors came from different backgrounds?"[334] We can only imagine what innovations might have occurred if people of color enjoyed equal access to capital and opportunity such as those of their white counterparts.

Addressing the racial disparity in capital raising is particularly imperative as the United States becomes a majority-minority country by 2040.[335] How we make capital available to entrepreneurs can have significant material consequences in the market. With 82% of the industry being male, nearly 60% of the industry being white and male, and 40% of the industry coming from just

331. In 2016, the Center for Global Policy Solutions reported that due to discriminatory financing practices and a bias towards companies primarily operated by white males, America is losing out on over 1.1 million minority-owned businesses. As a result, the economy is foregoing over nine million potential jobs and $300 billion in collective national income. AUSTIN, *supra* note 140, at 14.

332. Businesses owned by people of color are being hit the hardest by the pandemic's health and socioeconomic conditions. *See* Robert W. Fairlie, *The Impact of COVID-19 on Small Business Owners: Evidence of Early-Stage Losses from the April 2020 Current Population Survey* 5, 14 tbl.2 (Nat'l Bureau of Econ. Rsch., Working Paper No. 27309, 2020), https://www.nber.org/papers/w27309.pdf.

333. Between the onset of the COVID-19 outbreak in February and April 2020, the number of Black and Latinx-owned businesses nationwide fell by 41% and 32% respectively, compared to just 17% of white-owned businesses. *Id.*

334. Fan, *supra* note 65, at 352.

335. According to the U.S. Census Bureau, the minority population is expected "to rise to 56 percent of the total population in 2060, compared with 38 percent in 2014." Press Release, U.S. Census Bureau, New Census Bureau Report Analyzes U.S. Population Projections (Mar. 3, 2015), https://www.census.gov/newsroom/press-releases/2015/cb15-tps16.html. That growth, coupled with the fact that minority-owned businesses have increased to comprise more than fifty percent of new businesses started in the United States over the last decade, means that the future economic growth of the United States will include this group. *See Minority Entrepreneurs*, U.S. SENATE COMM. ON SMALL BUS. & ENTREPRENEURSHIP, https://www.sbc.senate.gov/public/index.cfm/minorityentrepreneurs (last visited May 21, 2021). Business policies and investments will need to be much more diverse than they are not to support the United States as an economic leader and driver in a global economy.

two academic institutions,[336] the culture needs to be less insular and more diverse.

The story of Elizabeth Holmes could not be a more intriguing story. The massive fraud and the drama around the inner workings of the company make for great entertainment.[337] But fraud and deception have happened before in Silicon Valley and it is certainly likely to happen again.[338] While the SEC and the federal courts will deal with Elizabeth Holmes and Sunny Balwani as the source of the fraud, how the structures in place and the culture of pursuing unicorn status at all costs contribute to and enable fraud and deception should also be examined. The stories around startup culture and the private investment market and the structural bias inherent therein converge in the figure of Holmes and her failed startup, Theranos, as a cautionary tale. The massive fraud by Theranos appears to be an outlier, but its implications are vast. As startups and their investors seek to model themselves after and replicate the successes of past unicorn companies and their founders, it is worth examining, and indeed, changing the culture of the startup ecosystem. There remains a lot of work to do to make entrepreneurship more equitable.

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336. Kerby, *supra* note 280.

337. In May 2018, John Carreyrou released the book *Bad Blood: Secrets and Lies in a Silicon Valley Startup*. CARREYROU, *supra* note 16. As of June 2018, a film version was in the works starring Hollywood film Jennifer Lawrence as Elizabeth Holmes. Dana Rose Falcone, *Everything to Know About the Elizabeth Holmes Movie Starring Jennifer Lawrence*, PEOPLE (Mar. 22, 2019, 4:26 PM), https://people.com/movies/elizabeth-holmes-theranos-jennifer-lawrence-movie/. In January 2019, ABC News *Nightline* released a podcast and documentary about the Holmes story called *The Dropout*, and HBO released the documentary *The Inventor: Out for Blood in Silicon Valley* about Holmes and Theranos, which made its official debut at the Sundance Film Festival in Park City, Utah, on January 24, 2019. *See* ABC News, *The Dropout* (Jan. 15, 2019) (downloaded using iTunes); *The Inventor: Out for Blood in Silicon Valley*, *supra* note 24.

338. *See 16 of the Biggest Alleged Startup Frauds of All Time*, CB INSIGHTS (May 23, 2019), https://www.cbinsights.com/research/biggest-startup-frauds ("There's almost always an element of 'fake it 'till you make it' for a successful, disruptive startup. Some companies just push their luck a little too far. When that's happened, some companies survive. Others are forced to rebrand in an attempt to distance themselves from the notoriety of their founders. And others disappear forever.").

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