



# THE STATE OF LGBT ENTREPRENEURSHIP IN THE U.S.

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Most of all, we would like to thank the many great entrepreneurs and investors who took time out of their busy schedules to answer all our questions and contribute to this landmark study.

# TABLE OF CONTENTS

|   |    |
|---|----|
| Executive Summary .....   | 2  |
| Introduction .....  | 4  |
| Methodology .....   | 5  |
| Profile of Entrepreneurs Surveyed.....                                    | 5  |
| Profile of Investors Surveyed .....                                       | 8  |
| Three Themes Emerge from the Data .....                                   | 10 |
| Location and Migration .....  | 10 |
| Gender versus Sexual Orientation - The Bigger Tax for Entrepreneurs?..... | 13 |
| Relevance and Relationships .....   | 15 |
| Implications for Stakeholders .....                                       | 21 |
| Conclusion.....   | 22 |
| About StartOut .....  | 23 |

# EXECUTIVE SUMMARY

In the spring of 2016, StartOut announced the launch of its ongoing research program with a commitment to deliver an inaugural report investigating the state of LGBT entrepreneurship in the United States (U.S.). Focusing exclusively on emerging high-growth companies with a sample size of 140 LGBT entrepreneurs, this study is the most comprehensive of its kind, and is intended to paint a clearer picture of the LGBT entrepreneurial experience in the U.S. To supplement data gathered from the entrepreneurs, we also surveyed 87 early-stage angel and venture capital investors. We then conducted in-depth interviews with ten LGBT entrepreneurs and five early-stage investors. Finally we culled public data sources and StartOut's membership list to compare 6,703 LGBT growth entrepreneurs with 92,096 entrepreneurs whose orientation was straight or unknown.

As entrepreneurial activity plays an increasingly important role in the overall U.S. economy, the goal of this and subsequent research is to provide more clarity, visibility, and contour around the experiences and contributions of LGBT entrepreneurs.

## KEY FINDINGS FROM THE RESEARCH

### PROFILE OF LGBT GROWTH ENTREPRENEURS

- LGBT founders are primarily motivated to start their businesses by a passion for the idea or opportunity, with 67% of our sample citing that as the reason for launching their ventures. The second most frequent response of being one's own boss was cited by 14% of our sample.
- LGBT people choose to start and run their businesses in places that are more open, tolerant and friendly to the LGBT population. 84% of our sample companies operated in cities that earned a 100% positive ranking on the Human Rights Campaign's (HRC) Municipal Equality Index.
- 75% of LGBT growth entrepreneurs are concentrated in three sectors - software, internet/media and consumer goods/recreation.

### LGBT ENTREPRENEURS IN INVESTOR PORTFOLIOS

- 48% of investors surveyed could identify at least one openly LGBT founder in their portfolios.
- While 48% of our surveyed investors said they actively invest with diversity in mind, that focus did not lead to a higher incidence of having LGBT founders in their portfolios. Nor did being LGBT themselves correlate with the presence of LGBT founders in their portfolios. Of our twelve self-identified LGBT investors, half could identify LGBT founders among their investments and the other half could not.

## THREE THEMES EMERGED FROM THE DATA

- **Location and migration** - states with policies unfriendly to the LGBT community lost many, if not all, of their nascent growth entrepreneurs before they founded their companies. Later, when LGBT founders moved the headquarters of their companies to a new state, 78% moved to California, New York and Illinois. This translates to over 1 million jobs lost for states unfriendly to the LGBT community.
- **Gender trumps LGBT status in adding difficulty to the funding process** - in this sample, approximately 38% of both male and female entrepreneurs raised outside capital to help fund their business but 70% of female LBT entrepreneurs raised less than \$750K while 47% of male GBT entrepreneurs raised more than \$2M, mirroring the gender funding gap seen in entrepreneurship in general.
- **Many LGBT founders choose to remain closeted while raising capital** - when fundraising, 63% of LGBT founders came out to investors during the process - most in the early stages of discussions - but a meaningful 37% chose not to self-identify as members of the LGBT community, 12% citing concerns that it might hurt their chances to get capital, while 47% said that "being out" wasn't relevant.

## IMPLICATIONS FOR STAKEHOLDERS

- **LGBT growth entrepreneurs** - "Coming out" during the entrepreneurial process remains a difficult decision for many. Evidence suggests most investors normally would value such openness as part of building a healthy entrepreneur-investor relationship.
- **Investors** - For angels, VCs and syndicates interested in LGBT diversity within their portfolio companies, it may be necessary to actively signal this acceptance of LGBT founders to lower the risks LGBT people feel in coming out during the process.
- **Policy makers** - Communities seeking to capture a share of new job creation driven by high-expectation entrepreneurs should create LGBT friendly environments. Otherwise they are driving away an active segment of job creators and damaging their local economies.

# INTRODUCTION

In the spring of 2016 StartOut launched its research program with a plan to deliver an inaugural report covering the state of LGBT entrepreneurship in the United States (U.S.). Focusing exclusively on emerging growth companies with a survey sample size of 140 LGBT entrepreneurs and a big data set of 6,703 LGBT entrepreneurs and 92,096 growth entrepreneurs of straight or unknown sexual orientation, this study is the most comprehensive of its kind, and is intended to paint a clearer picture of the LGBT entrepreneurial experience in the U.S.

Research in this area is sparse, with one major academic study having been conducted in 2005<sup>1</sup>. That study, which sampled over 300 LGB business owners, was more focused on LGB small business ownership than what is today referred to as growth or high-expectation entrepreneurship. Firms in that study averaged 11 years in operation and 13 employees. StartOut's current research seeks to update that study with a concentration on early-stage growth firms.

As entrepreneurial activity plays an increasingly important role in the overall U.S. economy, the goal of this and subsequent research is to provide more visibility around the experiences and contributions of LGBT entrepreneurs.

By exploring topics such as: what the primary motivators were for LGBT entrepreneurs in starting their own businesses; where LGBT entrepreneurs grew up, launched and migrated their businesses; and what their experiences were in securing funding, StartOut researchers have uncovered insights derived from quantitative and qualitative analysis around the current state of LGBT entrepreneurial activity in the U.S.

In this inaugural report StartOut's goal is fourfold: 1) to deliver a report on LGBT entrepreneurship in the U.S. that serves as a launch pad for future research; 2) to demystify the LGBT entrepreneurial experience; 3) to document the economic contributions of LGBT entrepreneurs; and 4) to provide insights and recommendations for LGBT entrepreneurs, investors and policy makers as we realize economic empowerment in the 21st century.

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<sup>1</sup> "Homosexuality and Entrepreneurship: Implications of Gay Identity for the Venture-Creation Experience," Minet Schindehutte, Michael Morris and Heffrey Allen, *Entrepreneurship and Innovation*, February 2005.

# METHODOLOGY

Our survey sample consists of 140 U.S.-based, self-described founders or C-level executives of emerging growth companies no more than 10 years in business. The survey was delivered to three sources: StartOut's membership database, former participants in the Chicago Booth New Venture Challenge Business Plan Competition, and through 500 Startup's social media lists. Non-LGBT survey recipients were asked to forward the survey to entrepreneurs in their networks who qualified. Obvious self-selection bias will exist.

In addition, we surveyed 87 early stage - angel, seed and series A - investors, sourced from four databases: 1) StartOut's membership list, 2) Pitchbook's Angel and VC list, 3) past participants of ChicagoBooth's New Venture Challenge and 4) 500 Startup's social media lists.

As a follow-up to the survey research, we also conducted qualitative interviews with five early-stage investors and ten LGBT-affiliated entrepreneurs.

# PROFILE OF ENTREPRENEURS SURVEYED

## COMPANY AGE



**72%** of early stage companies were less than 5 years old

**28%** of early stage companies were 5-10 years old

Our sample removed any companies over ten years old. Nearly three quarters of companies were less than five years in business.



## Big Data Analysis

On a parallel path, we undertook some big data analysis to supplement our understanding of the state of LGBT entrepreneurship. Looking first at where entrepreneurs chose to launch their ventures, we conducted a migration analysis. To understand the migration patterns of all Americans we used the interstate migration numbers published by the U.S. Census Bureau. As their most recent estimates cover years up to 2014, we focused on the ten-year period 2005-2014. From the census data we created a 52x52 matrix (including DC and Puerto Rico) representing the interstate migration probabilities, i.e., the probability for the resident of any given state moving to any other state or staying home.

To assess entrepreneurial migration, we collected public data from three websites: Crunchbase, CB insights and AngelList. Crunchbase and CB Insights are commercial sites that collect and sell data on startups and entrepreneurs. AngelList is a platform connecting entrepreneurs and startups with potential angel investors online. Once we identified people as members of a "founding team," we used LinkedIn to see if we could identify where those entrepreneurs grew up. In many cases hometowns are explicitly listed in the entrepreneur's profile. Where it wasn't listed, we inferred it from data such as their listed high school. In total we found 100,799 founding team members to whom we could ascribe home states. Then, to supplement findings about gender, we also built a name-based classifier to infer the gender of the entrepreneurs. Though a name-based gender classifier is far from

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perfect, hand analysis of 300 profiles suggested that roughly 90% of profiles were correctly labeled. This allows us to look at the broad trends in VC funding, job creation and migration, and how it compares by gender and sexuality.

Our final dataset - LGBT-identified entrepreneurs - was particularly challenging to collect because LinkedIn and the other sites rarely contain explicit reference to sexuality or gender identity. To collect data on LGBT entrepreneurs we leveraged the membership data of StartOut, a nonprofit with a mission to support LGBT entrepreneurs. StartOut's membership includes over 15,000 LGBT individuals, and their profiles contain information on the companies they founded.

We restricted our analysis to the overlapping population between StartOut's membership and the entrepreneur dataset we described above. This left us with 6,703 LGBT entrepreneurs and founding team members and 92,096 straight or unknown. So, LGBT profiles represented approximately 7% of our growth-oriented entrepreneur dataset. Given that the Williams Institute at the UCLA School of Law estimates the LGBT community in the U.S. at about 3.5% of the population, this may be early evidence that LGBT people choose high-growth entrepreneurship at a higher rate than the general population, but this hypothesis requires further research to substantiate.

## COMPANY SIZE

Like most early stage companies, our sample skewed toward small companies.

### MOSTLY SMALL COMPANIES

| Employees |     | Revenue   |     |
|-----------|-----|-----------|-----|
| 1-4       | 61% | \$0-100K  | 61% |
| 5-10      | 19% | \$101K-1M | 24% |
| 11-25     | 11% | \$1-5M    | 5%  |
| 26-100    | 7%  | \$5-20M   | 7%  |
| >100      | 2%  | \$>20M    | 3%  |

## GENDER

Our sample was split three quarters male and one quarter female. This is slightly less female participation than the Kaufmann Index indicates for new entrepreneurs entering the U. S. market (36.8%)<sup>2</sup>. However, our female sample was greater than female ownership of small businesses in general: about 18% of employer companies, according to the Small Business Association.

## IMMIGRANTS

While most of our entrepreneurs grew up in the U.S., our sample was comprised of 14.2% immigrants. 45% were from Asia and India while 35% came from Europe and Eastern Europe.

## MOTIVATION

Our panel mirrored the general entrepreneur population in the U.S., with 67% of them saying that passion for the idea or opportunity drove their decision to become an entrepreneur. The second most popular response was the opportunity to be their own boss at 14% of the panel. Only 6% of our LGBT entrepreneurs

<sup>2</sup> The Kauffman Index: 2015 Startup Activity National Trends



reported that building an inclusive work environment was their primary reason for starting their own business.

Motivation was not significantly impacted by gender with 64% of gays and 68% of lesbians choosing 'passion for the opportunity' as the primary motivation and 'being one's own boss' coming up as the second most popular response for each.

| Business type  | % of Participants |
|----------------|-------------------|
| LLC or S-Corp  | 53.5%             |
| C-Corp         | 33%               |
| B-Corp         | 3.5%              |
| Unincorporated | 10%               |

## INCORPORATION

Our sample was far more likely to be incorporated than a random sample of early stage firms, perhaps because we qualified on the criteria of emerging growth company.

Incorporation as a C-Corp was heavily weighted toward Delaware companies at 76% as compared to the 50% of publically traded U.S. companies. While LLC or S-Corp structures were spread across 15 states, only 21% of these companies incorporated in Delaware.

## FINANCING

As with incorporation, the companies in our sample were more likely than a random sample to have raised outside capital. While about 15% of new startups receive angel funding in any given year, 39% of our sample had received outside funding with an additional 26% anticipating raising a round in the next 12 months.

Of the 54 companies that had received outside funding, 22% had raised less than \$250K indicating angel or friends and family financing, while 37% had raised more than \$2M.

## LOCATION

As might be anticipated, our sample clustered in California (31%), with 26 companies in San Francisco, and New York (29%). Three other states made up the bulk of the rest of our sample with 11% in Illinois, 8% in Texas (64% of the Texas companies being in the Austin area) and 7% in Massachusetts. That left only an additional 14% scattered across 12 additional states.

## INDUSTRY MIX

The entrepreneurs in our sample clustered in three industries, with 75% of our participants choosing internet/media, software or consumer oriented businesses. Those who had received funding were far more likely to start consumer goods and media businesses than what is typical

| Industry                  | Funded LGBT Entrepreneurs | VC Deals | Angel Deals |
|---------------------------|---------------------------|----------|-------------|
| Software                  | 30%                       | 31%      | 34%         |
| Internet/media            | 28%                       | 7%       | 4%          |
| Consumer goods/recreation | 24%                       | 7%       | 2%          |
| Healthcare                | 11%                       | 10%      | 14%         |
| Commercial services       | 5%                        | 11%      | 9%          |
| Pharma/biotech            | 0%                        | 16%      | 7%          |
| IT Hardware               | 0%                        | 7%       | 2%          |
| Energy                    | 0%                        | 10%      | 2%          |
| Other                     | 2%                        | 1%       | 26%         |

for angel and VC backed companies<sup>3</sup> and were completely absent in intensely science oriented fields like biotech, hardware and energy.

## PROFILE OF INVESTORS SURVEYED

### LOCATION

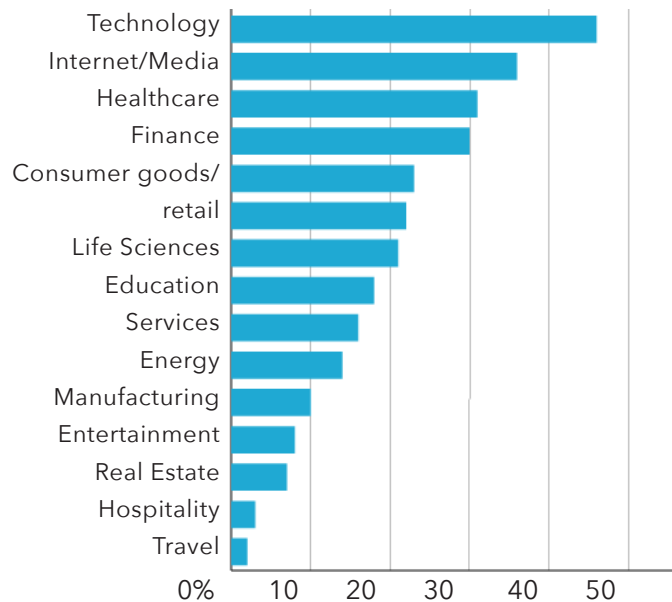
Turning now to an analysis of investors, some working with LGBT entrepreneurs (and some not), we see the bulk of our sample in West Coast (39%) and East Coast firms (31%), but there is also solid representation from the Midwest (14%) and the South (10%).

### INVESTMENT STAGE

The majority of the investors reported investing at the seed and series A & B levels (60%) while the remaining 40% focused solely on angel/seed investing.

### INDUSTRY FOCUS

The top areas of investment interest for our investors were technology, internet/media and healthcare.



Percent of firms investing in these industries

<sup>3</sup> Angel deals source, 2015 Halo Report, VC deals source, Entrepreneur Magazine, 10/9/13 "Venture Capital Trends by State, Industry (Infographic)"

## LGBT ENTREPRENEURS IN INVESTOR PORTFOLIOS

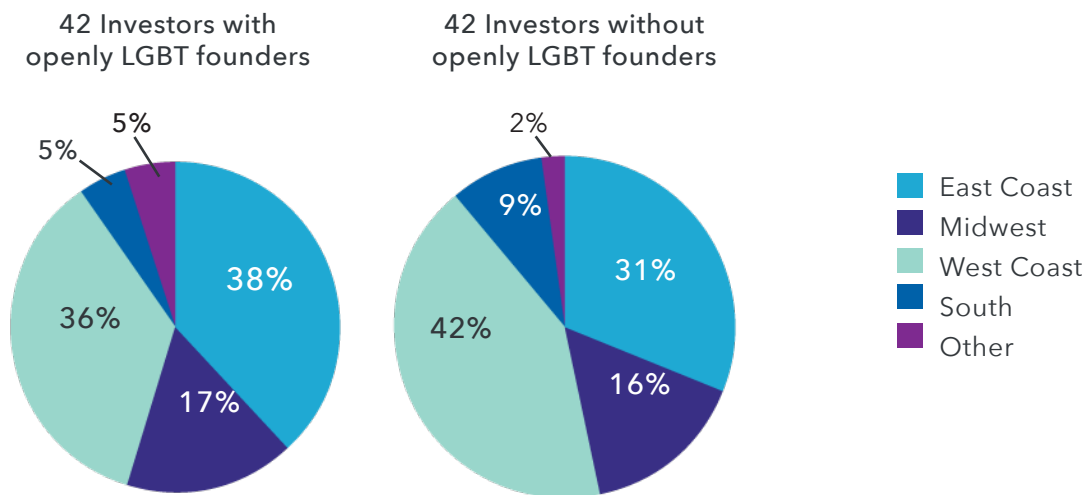
Almost half of our sample (48%) said they had an openly LGBT founder or C-level executive team member in at least one of their portfolio companies while 52% said they did not. But, while investors can typically identify female and minority entrepreneurs, the question of sexual orientation is not necessarily self-evident as two of our respondents pointed out in our comments section:

*"I answered 'Do you have any openly LGBT founders or executive team members in any of your portfolio companies?' with 'No' because we've never had discussions with our founders on such a subject and it's been non-obvious as to their status." - Investor survey participant*

*"In response to your question 'Do you have any openly LGBT founders or executive team members in any of your portfolio companies?' I answered 'Yes' because, given the number of portfolio companies we have and the size of the group of founders and management, it's almost certain that some will be LGBT. Are they 'openly LGBT'? I would assume so, but it's not a topic that ever comes up in our business discussions. We fund great management teams - whatever their personal relationship preferences are. Perhaps you could add 'Unsure' as a choice." - Investor survey participant*

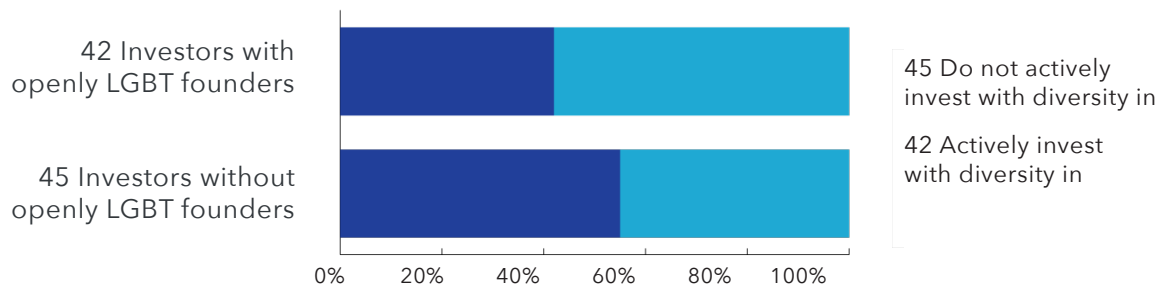
We looked for patterns that correlated with a higher likelihood of having an out LGBT founder in the portfolio and found nothing.

Location was not a predictor as those with and without LGBT founders were split fairly closely across regions.



We asked if the firm actively seeks to “fund with diversity in mind?” and the answer to this question didn’t seem to correlate with having openly LGBT founders in the portfolio. In fact, those who did not actively invest with diversity in mind had a slightly higher presence of openly LGBT founders in their portfolios.

Even when the investor self-identified as a member of the LGBT community, this did not predict the presence of openly LGBT founders. Albeit a small portion of our sample, the 12 LGBT-identified investors split 50/50 on the question, “do you have any openly LGBT founders or executive team members in any of your portfolio companies?”



## THREE THEMES FROM THE DATA:

### LOCATION AND MIGRATION

It is already established that young LGBT people in general tend to migrate towards states with higher levels of tolerance for difference. Our sample is the same. States like Arizona, Florida, Georgia, Missouri, New Mexico, Pennsylvania, South Carolina and Tennessee lost most or all of their LGBT would-be entrepreneurs just before these people established their companies. They predominantly moved to California and New York. Texas lost half of its future entrepreneurs and only one returned to operate his business in Austin, Texas's progressive haven. In fact, seven of the eleven companies in our sample located in Texas are in Austin.

This is definitely a diversity issue - not an entrepreneurship issue.

Fast Company's research ranked the top five states for innovation<sup>4</sup> - factoring in number of startups per capita, health of young firms, jobs created and startup community as:

1. Florida
2. Texas
3. Maryland
4. Arizona
5. Alaska

With California coming in 6th.

<sup>4</sup> Fast Company, 4/15/2013 "The United States of Innovation"



### Location & Migration in the Big Data

Unsurprisingly, entrepreneurs show dramatically different migration patterns from the average American. For example, they are nearly three times as likely to move to California and Massachusetts than average Americans. Entrepreneurs are 12 times more likely to move to DC. In total, the states with significantly greater inbound migration are DC, California, Massachusetts, New York, Colorado, Washington and Illinois. The least likely states for entrepreneurs to migrate to are Arkansas, South Dakota, West Virginia and Mississippi - in fact, the average American is ten times more likely to move to one of these states than an entrepreneur.

Generally, LGBT entrepreneurs show the same migration patterns as their straight counterparts, but the effect is substantially exaggerated. Gay and lesbian entrepreneurs are almost four times as likely to move to California as straight entrepreneurs. They are 260% more likely to go to Massachusetts, 230% to New York, 221% to Colorado, 203% to Washington and 197% to Illinois. Data on LGBT entrepreneurs was completely absent from twelve states including Arkansas, South Dakota, West Virginia and Mississippi.

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What is the impact in those states on job creation? The data sources provide job ranges for the companies our founding team members created. Using a mean of the range with a variance<sup>1</sup>, we found that 2.8 million ( $\pm 321,000$ ) people held jobs created by LGBT entrepreneurs between 2005 and 2014. We then ran simulations, shuffling the entrepreneurs all over the country as though they were straight. For each simulation, we then re-computed how many jobs would have been created in each state. At each iteration of the simulation we computed the difference between the real state-by-state job creation for LGBT founders vs the simulated numbers. These differences give us a distribution over the total jobs created in each state which are not predicted by the regular straight founder migration pattern. From this we estimate that nearly 1.1 million jobs (1.08 million  $\pm 201,000$ ) are not explainable by the standard migration patterns of straight entrepreneurs. In other words, between 2005-2014 more than 1,000,000 jobs left discriminatory states in favor of inclusive states.

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<sup>1</sup> *In more detail, combining the above migration data with the individual job creation data collected from our dataset required us to account for the uncertainty in the reported job number from the websites. Those numbers were always reported as a range. To handle this we represented each range as a Gaussian, centered at the mean of the range and with the variance fit such that the high and low numbers for the range were the 95% confidence interval for the Gaussian. To aggregate the jobs we then summed the Gaussians estimated for every company in the dataset, giving a final estimate that is the sum of the Gaussian means with a variance as the sum of the variances.*

From a sheer volume perspective, the top five states for new company launches in 2015 were<sup>5</sup>:

1. California with 115,374 new starts
2. Florida with 56,821
3. Texas with 50,050
4. New York with 43,931
5. Pennsylvania with 21,782

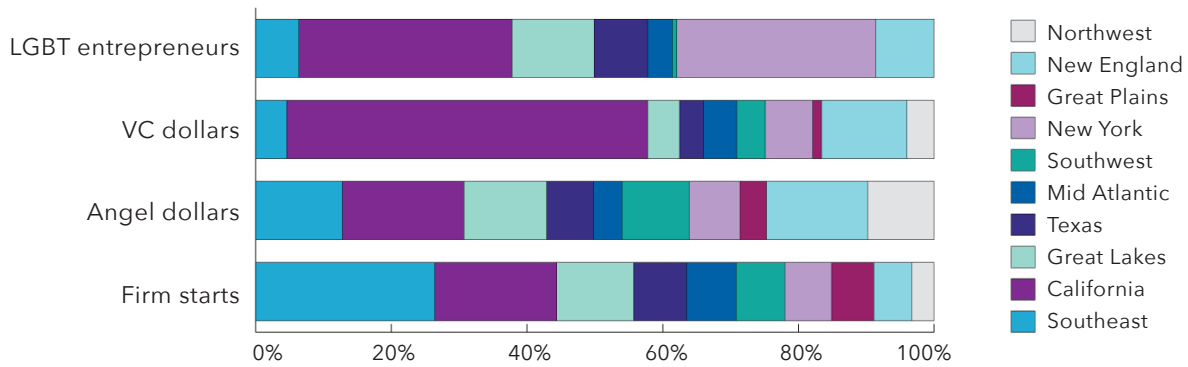
So from a pure activity perspective, these entrepreneurs are not leaving home because of a lack of entrepreneurial opportunities in their states. What about funding potential?

The Halo Report of 2015 released by the Angel Resource Institute and PitchBook looks at angel funding by region in the U.S. and venture dollars by state<sup>6</sup>. When we map our sample - where their businesses are headquartered today - to these regions, we see that the LGBT entrepreneurs are not chasing capital. A disproportionate number of them are in New York, which sees much lower VC and angel investment relatively speaking.

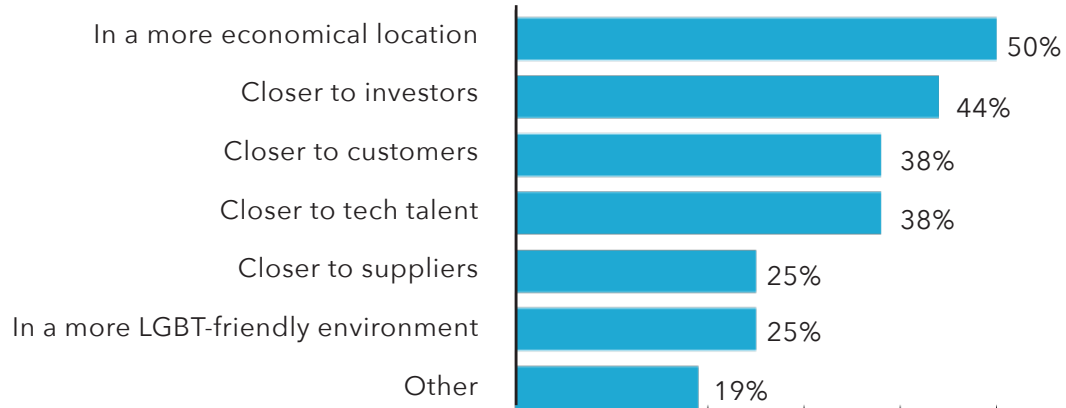
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<sup>5</sup> *Bureau of Labor Statistics, Business Employment Dynamics database*

<sup>6</sup> *VC data from the NVCA as reported in Entrepreneur Magazine, 10/9/13 "Venture Capital Trends by State, Industry" (Infographic)*



But, despite the indication that diversity and tolerance seem to motivate the entrepreneur's choice of location, that is not the stated conscious driver in most cases for the 10% of entrepreneurs in our sample who moved their headquarters to a new state. While 78% of these entrepreneurs chose to move to California, New York or Illinois, the most frequent cited reasons for making the move were to be:



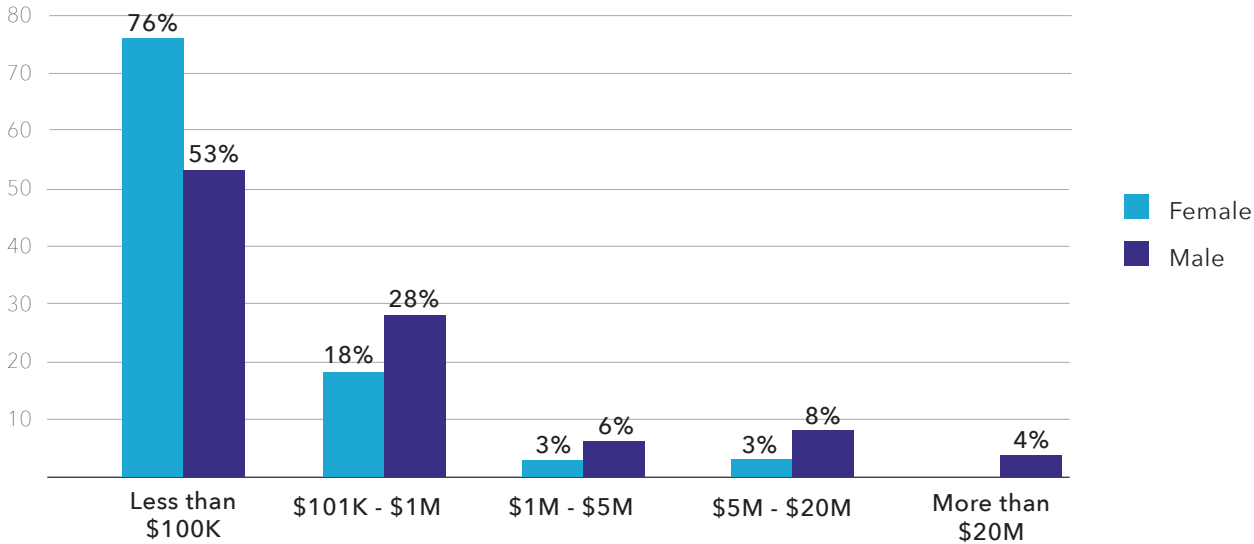
Even with the option to choose all answers that applied, only three of the 14 mentioned being in a location that is more LGBT friendly.

Nevertheless 83.6% of the companies represented by our survey were located in cities that received a perfect 100 score on the Human Rights Campaign's Municipal Equality Index which factors in non-discrimination laws, equality of employee benefits and community relationships with the LGBT community.

# GENDER VERSUS SEXUAL ORIENTATION - THE BIGGER TAX FOR ENTREPRENEURS?

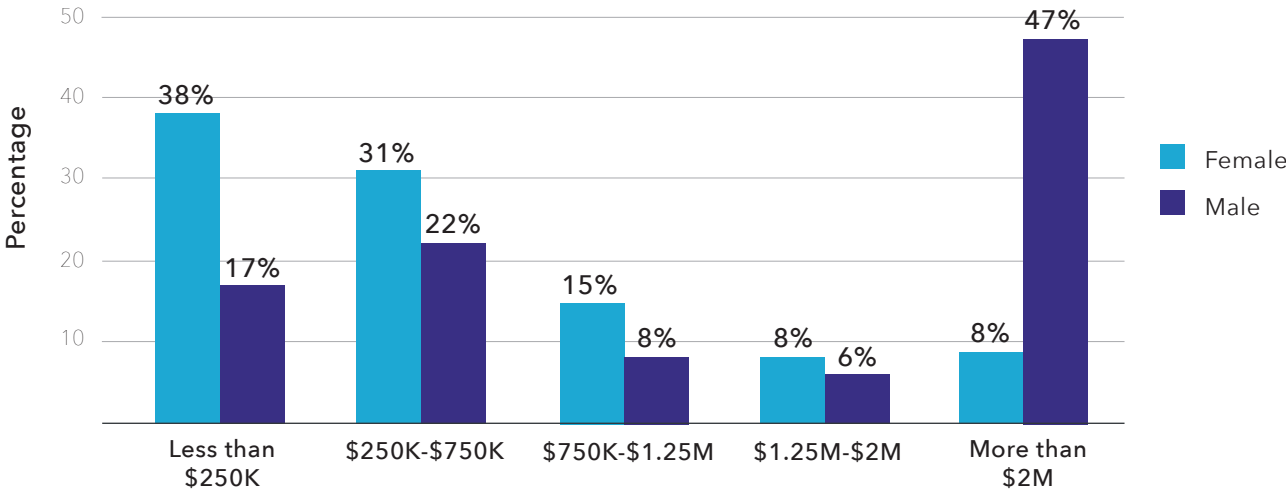
While the companies started by both male and female entrepreneurs in our sample were by and large still small companies, it is noteworthy that 12% of the companies owned by men were over \$5M in annual revenue compared with just 3% of firms founded by women. All the firms over \$20M in size were male founded.

ANNUAL REVENUE



The bigger gap between the male and female entrepreneurs comes when we examine the amount of funding raised by each. While a very similar proportion of the entrepreneurs had raised funding - 37.5% of men and 38% of women - the amounts raised were vastly different. Whereas over half of the men had raised over \$1.25M, nearly 40% of the female founders received less than \$250K.

CAPITAL RAISED



This capital gap has been identified in reports by the National Women’s Business Council (NWBC) and the Entrepreneurship Database program at Emory University that includes 2,352 ventures that participated in accelerator programs<sup>7</sup>. The NWBC report that used the Kauffman Firm Study data tracking nearly 5,000 businesses launched in 2004 through 2011<sup>8</sup> and found that, on average, men start companies with twice as much capital as women (\$135,000 vs. \$75,000) and that outside equity generates a much smaller percent of the capital women use to start their own business – 2% of their resources vs. 15% of their male counterpart’s pool.

Similarly, the Emory University data brief shows that, even though mixed gender teams outperformed all male teams on both revenue generation and number of employees, these teams received substantially less equity funding to achieve this growth than the all male teams – about a third less. All women teams fared far worse in the access to equity equation, receiving 31% of what the all male teams did and less than half what mixed gender teams received. In fact, when all sources of outside capital were considered – equity, debt and philanthropy – all women-owned firms still received only 68% of the amount all-male firms raised. This lack of capital, combined with substantially less entrepreneurial experience, is reflected in the underperformance of these firms.



## Gender is the larger factor in the big data

Research has shown substantial effects of founder gender on startup funding levels and the likelihood of receiving funding at all. Our own survey data supports these findings. While our proxy measure for gender, a name-based classifier, is a decidedly imperfect metric, it does reveal a strong difference in funding for those with more stereotypically female names. Startups with female-named founders secured on average 29% (±9%) less funding than startups with male-named founders. This eclipses the difference we found between gay and straight founders, and cannot be explained by industry differences.

<sup>7</sup> “Entrepreneurship & Acceleration: Questions from the Field” data brief, Entrepreneurship Database Program, Goizueta Business School, Emory University, August 2015

<sup>8</sup> “Access to Capital by High-Growth Women-Owned Businesses”, National Women’s Business Council, Susan Coleman, D.P.S. and Alicia Robb, Ph. D. April 2014



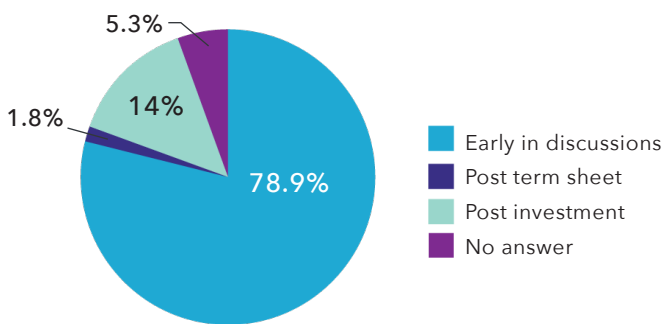
## RELEVANCE AND RELATIONSHIPS

Two thirds of our panel had either received funding or anticipated receiving it in the next 12 months. So we asked them, did you come out to your prospective investors? 63% were “out” to investors, the vast majority of whom came out early in discussions (79%). But a significant 37% had not chosen to come out to investors. We asked why? Nearly half said they didn’t consider it relevant with an additional 12% saying they thought being out might hurt them in the process.

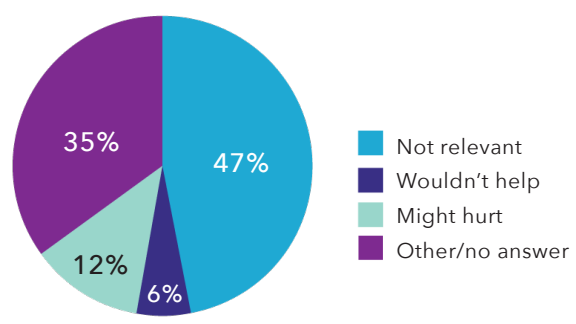
*This was a close tie between ‘it was not relevant’ and ‘I thought it might hurt my chance of getting funding.’ One of our major investor groups is a military-academy graduate only angel investor group. As a lesbian, I thought it was best to leave my sexual orientation out of the conversation. Moving forward, I would like to be more open about this.*

– Lesbian survey participant

WHEN DID YOU COME OUT TO YOUR INVESTOR?



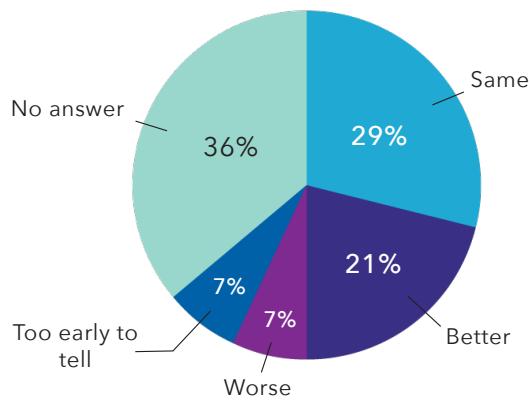
WHY DIDN'T YOU COME OUT TO YOUR INVESTOR?



This idea that one’s sexual orientation is a “private” matter that is not relevant in business is a common one. After Tim Cook came out as a gay man, a substantial portion of the social media comments, tweets and shares asked the question, “Why would he do this?” with two subtexts clear: 1) “no one should care, it is a private matter” and 2) “I don’t want to hear about it, he should keep it to himself.”

**HOW IS THE LGBT FOUNDED COMPANY DOING RELATIVE TO YOUR PORTFOLIO?**

(42 of 87 investors)



Is sexual orientation relevant to business performance? In our survey of investors, we asked the 42 investors with LGBT founders how the performance of those entrepreneurs' companies compared to the rest of their portfolio companies. While over one third of the investors chose not to answer this question, the results from the remaining two thirds were as you might expect culling out any individual companies from a portfolio - a mixed response of same, better, worse and too early to tell.

However, comments from both entrepreneurs and investors in our interviews expressed some areas where having an out LGBT founder could be relevant to the actual execution of the business. Some expressed it as a potential advantage - especially if the company's target customer base focused on or included the LGBT community.

*"I wasn't sure how the self-identification would go during my first chat with investors, but it was treated like any other data point. Almost as though I didn't need to call it out, but it was certainly helpful per the LGBT wedding niche my business looks to expand within." - Lesbian survey participant*

*"Our company addresses LGBT markets, so it's an asset to be gay." - Lesbian survey participant*

*"As we grew our company, we became more comfortable with telling our story and explaining who we are in the company. We started to see that it played in our favor. It's more relatable. We are working with underserved people who struggle to support themselves. As an LGBT person, I can speak for that with empathy and it played in our favor but only after we became comfortable with who we are as a company because that was not the case at the beginning." - Lesbian entrepreneur interviewee*

On the other hand, one entrepreneur whose business is specific to the LGBT community indicated that this fact made it more difficult to get investment.

*"I haven't found it easy to get venture capitalists interested although I don't think it's discrimination as much as just the business model we are working on... The whole thing is pretty gay. The way it comes up are that people, particularly investors, have said, 'I don't understand that niche market so I am not going to be able to invest.' So that's hard because with the vast majority of venture capital and wealth of our country being controlled by straight white men that makes it really challenging for somebody if their criteria are harder to understand from a personal perspective of what we are doing." - Lesbian entrepreneur interviewee*

And one investor expressed some concerns that it could impact the ability of the company to attract talent: *"If it would effect their ability to recruit; I wonder if it would effect their ability to recruit. I guess that would be a factor too." - Midwest VC interviewee*

So, being “out” might or might not impact the performance of the company depending on the market, location and focus of the business. But there were two areas that came up in the research where there is clear relevance to whether or not an entrepreneur chooses to be “out” about identifying with the LGBT community. The first was around the question of diversity.

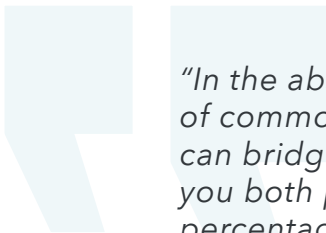
Nearly half of our surveyed investors invest with diversity in mind which begs the question – how can the LGBT community participate in and benefit from efforts to increase diversity if it does not self-identify? Recently Intel Capital announced a \$125 million diversity investment fund for women and minorities but did not include the LGBT community in that definition. As GeekWire reported, “According to the company’s announcement, it was not considering LGBT startups because they didn’t fall under the federal government’s definition of ‘underrepresented minorities.’ ‘We wanted to keep it simple and consistent,’ Intel’s Lisa Lambert told VentureBeat. ‘There is not a lot of visibility around LGBT. It is murkier because it is not a required disclosure.’”<sup>9</sup> And Intel isn’t the only such fund. Comcast’s Catalyst Fund is aimed at women and minorities, AOL’s BBG Fund is for women and the Indiana Diversity Investment Fund supports women, minorities and veterans.

As one of our survey participants put it,

*“It would be super great if LGBT entrepreneurs were capable of receiving diversity consideration for Government grants or loans.” – Gay survey participant*

But this will not happen until and unless entrepreneurs are willing to self-identify and more research is done to establish that the LGBT community belongs in the diversity conversation.

The second area where “out” becomes relevant is in the investor matching processes and the role of trust. A plethora of academic and business research has established the importance of trust in business relationships; it has additionally demonstrated that trust is easily granted to members of a shared affinity group. This plays a distinct role in venture investment as well. One study indicates that having a shared ethnicity nearly doubles the chances of getting an investment from a particular investor – even though shared ethnicity was associated with worse investment outcomes.<sup>10</sup> This issue was raised by one of our interviewees directly.



*“In the absence of a strong network of LGBT investors, there is a gap of common experience. So common experience is something that can bridge a gap between people. You went to the same college; you both play volleyball. I don’t know what the representation percentagewise is among institutional investors and LGBT individuals. Based on my experience, my guess is that it’s not very representative. So this creates a chasm in common experience between LGBT entrepreneurs and prospective investors.”*

*– Gay entrepreneur interviewee*

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<sup>9</sup> <http://www.geekwire.com/2015/out-in-tech-what-its-like-to-be-lgbt-in-an-industry-struggling-with-diversity/>

<sup>10</sup> “Ethnic Matching in the U. S. Venture Capital Market”, Ola Bengtsson and David Hsu, *Journal of Business Venturing*, September 2014


The only way to overcome the disadvantage of difference is communication and relationship building. In our interviews with five early stage investors – four male and one female – every single one of them stated that a good personal rapport was critical to a strong business relationship.

*“I invest in things that I think should exist, things created by people whose values and goals I share. Value rapport and personal rapport are tremendously important.” – NY Angel interviewee*

*“With few exceptions, rapport is almost everything.” – Midwest VC interviewee*

*“In the end people will only confide in people they trust. They will reach out to people with whom they like speaking and spending time. It’s all about having a genuine relationship with them.” – Silicon Valley VC interviewee*

*“I definitely socialize with our founders outside of work-oriented meetings because of the familiarity you have with each other. I would like to build a more informal environment with them so when formal stuff comes up at work, we would have a more comfortable environment and you will have better ideas.” – NY VC interviewee*



***“Generally you want to think that you are going to like them [the founder]. You are going to spend a lot of time with the person. You are going to be in the trenches with them. If you get the feeling that you aren’t going to like them early in the deal you probably shouldn’t do the deal. An investment is like a mini marriage.”***

*– Midwest VC interviewee*

In fact, more than one investor indicated that if they don’t get a good feeling about the entrepreneur they would pass on a deal.

*“In terms of founders we haven’t invested in, we get excited about the business, get excited about where it might go, but when you get to the true colors of the founder, you just sit there. You’re just like ‘this is not comforting.’ You also have to be open and honest about it.” – NY VC interviewee*

When asked to tell us about the founders in their portfolios, they knew a lot about them – including marital status, gender and ethnicity. But when it came to sexual orientation they were less clear. In response to the question “Do you have a sense of the number of openly LGBT founders you have in your portfolio?” we heard a variety of answers.

*“None that I know of.” – Midwest VC interviewee*

*“I suspect a couple, but not a huge number.” – NY Angel interviewee*

*"I know two openly LGBT people in the portfolio. But it is not something we actively track." - Midwest VC interviewee*

*"I think, when I filled out the survey, I said one. But now I can't recall who she or he was."  
- Silicon Valley VC interviewee*

Is this because they haven't invested in LGBT entrepreneurs? Or, is it because some or all of the LGBT entrepreneurs in their portfolios have chosen not to come out? And, if that is the case, what impact does that have on the trust and rapport so critical to the founder-investor relationship? We also spoke with ten founders - six male and four female - who had chosen to obtain outside capital about sharing their own LGBT identity with their investors. For the majority of them the capital was essential for the survival of their young companies. For others it was important in driving growth that could not have been achieved without the investment. Eight out of ten of our founders described their relationships with their current investors as close.

*"I have a great relationship with them [my investors], business and personal. Businesswise we have grown from the beginning when it was a colder relationship. You know. They were my investors; they were my colleagues; they were my partners; now they are my friends."  
- Lesbian entrepreneur interviewee*

*"Our lead investor led seed and stayed around. I feel strongly that he is investing for success. He has our back, gives us good advice and direction. I feel we have really good relationships with all of our investors." - Gay entrepreneur interviewee*

*"I have personal relationships with him and two other investors, actually three others, whom I am friends with. They invested knowing my personal life. For two of them, my affiliation with the LGBT community is completely irrelevant. They know me personally and they are my friends." - Lesbian entrepreneur interviewee*

*"I have an investor with whom I have a relationship other than professional. We became friends. Probably one or two. We are friends; we go for drinks together but nothing special. We are just friends that hang out." - Gay entrepreneur interviewee*

The other two considered the relationship as more distant.

*"We have a pretty good relationship... I will meet with them regularly. It's almost always to talk about business." - Gay entrepreneur interviewee*

*"For me it's kind of like a very formal relationship. I report to them every quarter." - Gay entrepreneur interviewee*

For half of the interviewees, being "out" was not a consideration. Their investors knew they identified as members of the LGBT community either through personal network connections or clear signals in their LinkedIn profiles and resumes.

*"They know I am LGBT. It's fine. But it's definitely not something that I would feel comfortable discussing." - Lesbian entrepreneur interviewee*

*"People usually know about it prior to the call... I am part of the LGBT network." - Gay entrepreneur interviewee*

For others it came up during the process and people responded very differently when that happened.

*"It absolutely comes up. Investors investigate people especially in earlier stages. So as the investors get to know me, it comes up that I have a husband. Inevitably, depending on how the conversation is unfolding, I am wearing a wedding ring, he would ask about my wife and I had to correct him and say it's a husband. It absolutely comes up." - Gay entrepreneur interviewee*

*"A big part of it at that time was that they assumed I am one way not the other and I didn't really care. Maybe I was a little uncomfortable and said, 'I don't have a girlfriend,' sort of giving a white lie." - Gay entrepreneur interviewee*

While some ease into the conversation when they feel safer.

*"I didn't volunteer [that he was gay] because for me I am very selective of the information I give out when I first meet somebody. I think that over a period of time as I develop a relationship with them, I won't have a problem having my partner come with me to London to meet with them and have dinner with them. And it's not going to be a surprise. I think at the beginning, when I am meeting someone for the first time, I am very hesitant about just giving all types of information out because I need to test the situation first." - Gay entrepreneur interviewee*

There are clearly still risks associated with being "out" in the business world - in 28 states it is legal to fire an employee simply for being a member of the LGBT community, three more if you are transgender. A 2014 study by the HRC indicated that 53% of LGBT workers in the U.S. hide their sexual identity at work.<sup>11</sup> While another study by Deloitte and New York University indicated that 83% of LGBT persons "cover" some part of their sexual identity at work.<sup>12</sup> LGBT entrepreneurs do not seem to be immune to these pressures. But in the investor-entrepreneur relationship, "coming out" - being authentically and wholly present in the relationship - seems to be a critical step required to overcome the trust barrier of difference.

*"But there is a certain honesty you will have to have with potential investors that establishes trust with that person. If that isn't there, I would imagine, you are not going to get the investment. So for me, like I said, just to be myself." - Gay entrepreneur interviewee.*

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11 "The Cost of the Closet and the Reward of Inclusion", HRC, May 2014

12 "Uncovering Talent, A New Model of Inclusion," Kenji Yoshino, NYU School of Law, and Christie Smith, Deloitte University Leadership Center, December 2013

# IMPLICATIONS FOR STAKEHOLDERS

## LGBT FOUNDERS

- “Out” is relevant. Possibly to business performance in both positive and negative ways. But certainly to the early-stage entrepreneur-investor relationship. While it is not necessarily appropriate to “test” investors by announcing upfront, “I’m LGBT and I’m raising capital,” it does behoove LGBT entrepreneurs as they build relationships with potential investors to be authentic and forthcoming about personal aspects of their lives as they come up in conversation. That authenticity helps create trust that can strengthen the business connection going forward.
- Perhaps one way to avoid having to find a way to elegantly insert the coming out process into conversations is to publicly signal LGBT affiliation in social media profiles like LinkedIn by using membership in organizations like StartOut or the LGBT Chamber of Commerce. Knowing that investors use these data sources in their due diligence process allows that information to be tacitly conveyed prior to discussions.
- More role models are needed. Aside from Peter Thiel and Michael Kors there are few very visible successful LGBT entrepreneurs showcased in the popular media. Millennials are less inclined to be “out” at work than older, more established LGBT workers with only 5% of LGBT young people ages 18 to 24 being totally open at work versus 32% of LGBT people ages 35 to 44. Evidence shows there is still a penalty to be paid for this openness – almost 40% of LGBT workers report discrimination and harassment when they are “out” at work, compared with the 10% who experience the same challenges while closeted<sup>13</sup>.
- LGBT founders need to consider broadening the industries they choose to innovate in. With over half of LGBT founders focusing on internet/media and consumer goods/recreation startups, they find themselves competing in industries with relatively low cost of entry, lacking in intellectual property barriers to entry and receiving only 6% of angel dollars and 14% of VC investment.

## INVESTORS

- It’s time to include the LGBT community when thinking of diversity in investment. Our research shows we are an active source of emerging high-growth businesses. An LGBT inclusive diversity policy can help attract deal flow and increase return on investment.
- For investors, funds and syndicates interested in LGBT diversity within their portfolio companies, it may be necessary to actively signal this acceptance of LGBT founders to lower the risks of LGBT people in coming out during the process.
- Given that young LGBT people in general tend to migrate towards states and municipalities with higher levels of tolerance for difference, investors seeking LGBT entrepreneurs would do well to expand their geographic parameters to source opportunities in New York and the Great Lakes regions in particular where LGBT entrepreneurs are over-represented relative to current investment dollars.

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13 “A Survey of LGBT Americans”, Pew Research Center–Social & Demographic Trends, June 2013

## POLICY MAKERS

- Policy makers seeking to capture a share of new job creation driven by high-expectation entrepreneurs should create LGBT-friendly environments. Otherwise they are driving away an active segment of job creators and damaging their local economies.

## STARTOUT

- StartOut can leverage these research findings to help spur national and local conversations about the LGBT community as job creators, rather than just a market whose dollars to target. The ultimate goal is to affect positive change at a systemic level for our community and society as a whole.
- StartOut needs to continue, past this inaugural report, with its research program delving further into topics to reduce “murkiness” around our community such as:
  - How do LGBT founders perform when compared to the general population of founders?
  - What are the implications of being “out” as a founder?
  - Is the LGBT community more or less likely to start high-growth businesses?
  - Why are LGBT entrepreneurs choosing the Internet/media and consumer goods/recreation industries so frequently at the expense of other opportunities?
- To address the “double tax” related to gender (being both a woman and lesbian), StartOut should continue its investment in lesbian mentorship and find ways to help our female members bridge the financing gap.
- And finally, we can seek means to encourage members to pursue hard sciences, potentially creating focused access to capital programs for underrepresented industries, “STEM for LGBTs”.

## CONCLUSION

In recent years, the LGBT community has gained substantial positive representation and visibility in politics, entertainment, Corporate America and even professional sports, culminating in the June 2015 Supreme Court Decision legalizing marriage in all 50 states. While there is much to celebrate there is more work to do. In 28 states it is legal to be fired for identifying as LGBT - and transgender people are at risk in three more. In May of 2016, states filed suit against the Obama Administration challenging its directive to allow transgender students to use restrooms and other facilities that match their gender identities - a calculated backlash against the progress achieved with Marriage Equality.

Since the mid-twentieth century demographers have struggled to gain an accurate picture of the number of LGBT people in the United States. These data remain elusive today. In 2011, The Williams Institute produced a report estimating that 3.5% of adults identify as LGBT<sup>13</sup> while a 2015 study conducted by the Public Religion Research Institute found that 7% of Millennials identify as LGBT<sup>14</sup>.

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14 *“How Race and Religion Shape Millennial Attitudes on Sexuality and Reproductive Health”, Robert Jones and Daniel Cox, Public Religion Research Institute, March 2015*



While the collective buying power of U.S. LGBT adults is estimated at \$884 billion much less is known about our community's contributions to driving economic growth. This report is a beginning point in the economic discussion of the important role LGBT entrepreneurs play in American entrepreneurship.

## ABOUT STARTOUT

Economic equality is a critical step along the continuum of progress for the LGBT community. While LGBT people are often stereotyped as being affluent the reality is the opposite; 21% of LGBT people have an income of less than \$12,000 per year, versus 4% of the general population<sup>15</sup>. The LGBT community has made political strides, yet the economic playing field is not level for our community when compared to the rest of Americans.

To date many LGBT entrepreneurs have encountered unequal access to key resources needed to advance their businesses including a lack of visible role models, an inability to locate mentors, or being denied access to capital.

Founded in 2009, StartOut's mission is to enable economic empowerment for our community through entrepreneurship. We do this by supporting LGBT entrepreneurs and the next generation of business leaders. With six chapters and a growing constituency across the U.S., we hold educational and inspirational events; connect qualified LGBT entrepreneurs to investors; provide mentorship for lesbians and enable digital and in-person networking for our members.

Through our events, networking platform and research program, we will continue to enable LGBT entrepreneurship in the U.S. and shine a light on any inequalities that hinder progress for our community.

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<sup>15</sup> "Paying an Unfair Price: The Financial Penalty for Being LGBT in America", Center for American Progress & Movement Advancement Project, November 2014