Black-Led VC Fund Case Could Hinge On Nature Of Grants

By **Kali Schellenberg, John Stapleton and Kenneth Trujillo** (January 29, 2024)

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On Wednesday, the U.S. Court of Appeals for the Eleventh Circuit is scheduled to hear argument in American Alliance for Equal Rights v. Fearless Fund Management LLC — a challenge under Section 1981 of the Civil Rights Act[1] to a grant program for Black women-led businesses.[2]

Initiated by the American Alliance for Equal Rights, founded by Edward Blum, the case is part of a wave of similar challenges[3] and raises a number of significant civil rights issues. Blum is notable for his role in the recent challenge to affirmative action that culminated in the U.S. Supreme Court's 2023 Students for Fair Admissions v. Harvard decision.

Organizations whose missions involve any manner of race-conscious funding should closely monitor this case, while recognizing that specific factors may distinguish it from their situations, including potentially whether their program is charitable in nature.

Fearless Fund is a venture capital firm co-founded by Arian Simone and Ayana Parsons, two Black women, to address the gap in venture capital funding for women of color — who in 2022, received a mere .13% of such funding.[4]

AAER is challenging the Fearless Strivers Grant Contest, which is run by Fearless Fund's philanthropic arm, Fearless Foundation, a 501(c)(3) nonprofit.

The grant contest is open only to Black women and selects a winner four times a year to receive a $20,000 grant, formal mentorship and tools to grow their business.

AAER argues that this grant program contravenes Section 1981's prohibition on racial discrimination in contracting because it excludes women who are not Black.

A ruling enjoining the Fearless Strivers Grant Contest would be widely viewed in the civil rights community as yet another attack on efforts to remedy stark racial divides in this country — ironically using a Civil Rights Law to thwart those remedial efforts.

However, even a ruling in favor of Fearless may set precedent that could adversely affect other civil rights goals.

For example, one of Fearless' arguments is that applying Section 1981 to its program would violate the First Amendment by compelling Fearless to alter the content of its intended speech, which is to convey that Black women-owned businesses are vital to our economy.

A broad First Amendment ruling insulating Fearless from suit could allow other groups, including racist or anti-LGBTQ organizations, to utilize the ruling for discriminatory purposes

lacking remediation value.

Additionally, Fearless contends that AAER lacks standing because it has not named members of its organization that have standing, instead referring to them anonymously as Owners A, B, and C, and has not provided concrete information as to their readiness to apply to the grant program.

A strict standing ruling could, in turn, be used to prevent civil rights organizations from bringing lawsuits to redress harm to marginalized populations in the future.

There are legal avenues around these potential pitfalls, including holdings specific to the history and purpose of Section 1981.

For civil rights organizations, the most helpful holding would be that Section 1981 was not intended to prohibit race-conscious remedial practices or policies, which would greenlight efforts like Fearless' grant program to correct deeply entrenched racial disparities.

However, if the Eleventh Circuit does not go that direction, another route would be to find that Section 1981 does not apply to charitable giving.

This argument, delineated in an amicus brief on behalf of 18 states and the District of Columbia, posits that while Section 1981 applies to commercial transactions and public accommodations, it was never intended to apply to charitable giving, which has traditionally not been viewed as posing an obstacle to full participation in economic life or the right to participate in the marketplace.[5]

None of the parties have identified an example where Section 1981 was applied to charitable giving, [6] and in fact, both parties appear to agree, in principle, that charitable giving is exempt from Section 1981.

Thus, the case may turn on whether the Fearless grant program is charitable.[7] AAER argues that Fearless is not donating money, but instead is running a contest in which winners are selected based on the strength of their business.

AAER focuses on the fact that entrants must agree to the official rules, which were explicitly labeled as a "contract."

The rules contain terms giving Fearless rights related to the use and disclosure of the ideas in the entry, the use of the entrant's name, image, and likeliness for public relations, and includes clauses mandating arbitration and releasing and indemnifying Fearless.[8]

Fearless argues that the foundation's grants are discretionary gifts that advance the organization's mission and confer no enforceable rights on contest entrants.

An amicus brief further fleshes out this argument, providing that whether an activity is charitable does not depend on if the funding involves a contract, or the money is given in the form of a grant, loan or investment.[9]

Rather, the salient point is whether the giving is aligned with the mission of the nonprofit, and that mission is consistent with recognized charitable purposes.

The U.S. District Court for the Northern District of Georgia did not directly address these arguments, but if the Eleventh Circuit does, any lines drawn as to charitable status could

heavily influence how programs like Fearless' are constructed in the future.

For organizations that are not 501(c)(3) nonprofits, such as for-profit companies running grant programs, or some community development financial institutions, it is unclear whether a favorable ruling on this basis would be applicable — though it could provide helpful clarity as to permissible structures for giving.

That said, a ruling grounded solely in the specific history and purpose of Section 1981 is inherently limited, and challenges under other relevant civil rights laws will persist.[10]

Thus, while Fearless Fund is an important and likely impactful case, the underlying lawfulness of using race-conscious efforts to remediate racial disparities will continue to be fought across the legal spectrum, and it may be several years before there is any real clarity for organizations operating in this space.

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[1] Section 1981 provides that: "All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts, to sue, be parties, give evidence, and to the full and equal benefit of all laws and proceedings for the security of persons and property as is enjoyed by white citizens, and shall be subject to like punishment, pains, penalties, taxes, licenses, and exactions of every kind, and to no other." 42 U.S.C. § 1981.

[2] The case comes to the Eleventh Circuit on a denial of a preliminary injunction by the Northern District of Georgia on September 26, 2023. The AAER appealed that same day, and on September 30, 2023, the Eleventh Circuit motions panel issued an injunction against Fearless Fund pending appeal.

[3] A similar case was also filed against Progressive Insurance alleging its grant program for black entrepreneurs violates Section 1981. See Roberts & Freedom Truck Dispatch v. Progressive Preferred Ins. Co. et al., No. 23-cv-1597 (N.D. Ohio 2023). More broadly, legal attacks on race-based diversity programs are intensifying. See, e.g., Law Firm DEI Efforts At Crossroads Amid '24 Litigation Threat, https://www.law360.com/pulse/articles/1779715; The Legal Battles Over ESG And DEI To Watch In 2024, https://www.law360.com/articles/1775017/the-legal-battles-over-esg-and-dei-to-watch-in-2024.

[4] American Alliance for Equal Rights v. Fearless Fund Management, LLC, et al., No. 23-13138, Brief for Appellees, Dkt. 63, pg. 1.

[5] The District Court did not directly analyze whether Section 1981 applies to charitable giving because it found that AAER had sufficiently shown that the Fearless Strivers contest

was contractual in nature, and therefore Section 1981 applied. See Am. All. for Equal Rts. v. Fearless Fund Mgmt., LLC, No. 1:23-CV-3424-TWT, 2023 WL 6295121, at *5 (N.D. Ga. Sept. 27, 2023).

[6] American Alliance for Equal Rights v. Fearless Fund Management, LLC, et al., No. 23-13138, Brief for Appellees, Dkt. 63, pg. 50 (citing Doe v. Kamehameha Schs., 470 F.3d 827, 889 (9th Cir. 2006) (en banc) (Kozinski, J., dissenting) (noting absence of any "case where section 1981 has been applied to a charity")).

[7] This determination is also relevant to Fearless Fund's First Amendment argument, which relies heavily on Coral Ridge Ministries Media, Inc. v. Amazon.com, Inc., 6 F.4th 1247 (11th Cir. 2021). See American Alliance for Equal Rights v. Fearless Fund Management, LLC, et al., No. 23-13138, Brief for Appellees, Dkt. 63, pg. 17-24. The Coral Ridge Court found that Amazon's decision to exclude an extreme religious organization from its AmazonSmile charity program was protected by the First Amendment and did not violate Title II's prohibition on religious discrimination.

[8] The nature of the contract is a disputed factual issue, as Fearless changed the terms of the rules after AAER filed suit. AAER contends that Fearless then changed the rules back to their original form, while Fearless rests its arguments on the updated version of its rules.

[9] See American Alliance for Equal Rights v. Fearless Fund Management, LLC, et al., No. 23-13138, Brief Of Professor Roger Colinvaux As Amicus Curiae In Support Of Defendants-Appellees And Affirmance, Dkt. 100.

[10] For example, organizations receiving federal funding, such as CDFIs, would also be subject to the Equal Protection Clause, Title VI, and potentially other federal laws and regulations depending on the nature of the financial product—e.g., if the extension of credit is involved, it may invoke the Equal Credit Opportunity Act. As such, it is imperative that organizations understand their potential exposure under the laws applicable to them, which courts may interpret differently than Section 1981.