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# Supporting Small-Business Growth Can Help Americans Build Wealth

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# Introduction and summary

Small-business ownership is one of the surest pathways to wealth creation and economic mobility, and since the COVID-19 pandemic recession, Americans have been applying to start new businesses at historic rates. Small businesses play an important role in the U.S. economy, are responsible for nearly half of private sector employment, and have a major role in job creation. Polls show that people strongly associate owning their own business with achieving the American dream, and for good reason. According to a 2022 study published by the Federal Reserve Bank of Cleveland, from 2013 to 2016, business owners in the bottom wealth quintile moved up to the top quintile at six times the rate as the population as a whole. Thus, entrepreneurship is a viable pathway to opportunity even as the nation's small businesses face several headwinds.

Small businesses are struggling under the Trump administration's policies, with 75 percent of small-business owners surveyed reporting that the economy in late 2026 is "one of the hardest economies of their careers." First, tariffs are driving up costs across the board: Core producer prices (excluding the volatile food, energy, and trade services categories) rose at a yearly rate of 5 percent through September 2026, while overall producer prices also climbed 6.3 percent—the largest 12-month increase since December 2022. Center for American Progress analysis found that tariff costs for the roughly 234,000 small-business importers have more than tripled since President Donald Trump took office in January 2025, with the average small-business importer paying $426,000 in additional tariffs during the 18-month period from March 2025 through August 2026 compared with the preceding 18 months.

Second, the Trump administration has implemented changes that have reduced services to the nation's small businesses. As highlighted later in this report, the administration has curbed access to critical programs at the Small Business Administration (SBA) and other federal agencies, including raising fees and tightening lending standards. Rather than strengthening the programs that serve mom-and-pop small businesses, the SBA has proposed increasing across-the-board size standards that it uses to determine eligibility for capital access programs and

procurement preferences to allow larger businesses—including some businesses in the finance, insurance, and securities industries with more than $800 million in annual revenue—to qualify as "small" and thus compete with truly small businesses for federal contracts and SBA lending.

Third, the expiration of the Affordable Care Act's enhanced premium tax credits at the end of 2025 has put major strain on small businesses: CAP estimates that roughly 4.4 million small-business owners and self-employed people who relied on marketplace subsidies have faced an average premium increase of about $1,500 in 2026—out of a total of 5.2 million small-business owners and self-employed Americans who obtain coverage through the marketplace. Because these credits ease "job lock" by giving people an option for nonemployer health coverage and making it more affordable to strike out on one's own, their loss removes a key support for precisely the kind of job-creating entrepreneurship discussed later in this report.

Lastly, the boom in artificial intelligence (AI) carries both promise and risk for the nation's small businesses. AI adoption can enable solo entrepreneurs and mom-and-pops to grow faster than before, as new tools help them market their products and services; handle back-office functions; and manage their inventory in a faster, more cost-effective manner. But large corporations and wealthy small-business owners can also use AI to help them dominate markets and outcompete small businesses that lack the same resources, and small-business owners in industries at higher risk of automation could be put out of work.

Overall, while business formation has remained elevated since 2020, as laid out below, small businesses are now also failing at an elevated rate, and the share of these businesses that expect to hire employees has declined.

The Trump administration's primary policy tool for supporting small business is the 199A Qualified Business Income Deduction, made permanent by the One Big Beautiful Bill Act. The 199A deduction lets owners of "pass-through" businesses such as sole proprietorships, partnerships, and S-corporations subtract up to 20 percent of their business profits before calculating what they owe. These businesses are referred to as pass-throughs because they do not pay corporate taxes but instead "pass through" profits to the owner(s), who report them on a personal tax return. The 199A deduction is a poor fit for the problems described above: A deduction against profits does nothing for a business that is struggling to get set up and not yet profitable, and it does nothing to help an entrepreneur make the leap to hiring. Two-thirds of the benefits of 199A flow to owners earning more than $500,000, and 84 percent of the businesses that claim it have no employees at all.

A society serious about opportunity and economic mobility should make major investments in supporting small businesses, especially in light of the negative impacts of the Trump administration's tariffs, federal spending and health care cuts, and the opportunities and challenges posed by AI. To that end, CAP is calling for a bold agenda to support the nation's 36 million small businesses by:

- Replacing tax breaks that are rigged to favor wealthy business owners with tax reforms that help small businesses hire employees and that reduce tax filing burdens on mom-and-pop businesses.
- Investing to expand access to both lending and equity capital for underserved small businesses.
- Democratizing access to AI tools that can help small businesses grow.
- Creating new pathways to ownership for employees and entrepreneurs seeking to acquire existing small businesses.

By revamping the 199A deduction, which subsidizes wealthy business owners and costs more than $75 billion annually, and reinvesting those savings in mom-and-pop small businesses, CAP's plan would save small businesses $10 billion in tax preparation costs and time, provide $26 billion in relief to roughly 16 million small-business owners, help mom-and-pop small businesses cover the wages of more than 6 million workers each year, help 85,000 businesses become employers every year, expand access to capital to roughly 87,000 additional small businesses each year, and provide the capital and technical support that business owners need to transition ownership. (see Methodological Appendix)

Overall, CAP's agenda would cost roughly $52 billion annually, resulting in more than $20 billion in annual taxpayer savings over the current 199A policy while more effectively supporting mom-and-pop businesses. CAP's agenda for small businesses would help more entrepreneurs start, sustain, and grow their businesses, ensuring the American dream is within reach for generations to come.

# Entrepreneurship is booming, but small businesses face a host of challenges

During and after the COVID-19 pandemic, entrepreneurship reached record levels, but small businesses face a host of emerging challenges, such as tax rules that favor the wealthiest business owners over mom-and-pop businesses, unequal access to capital, the rise of AI, and a wave of looming retirements that will reshape small-business ownership. In this report, CAP adopts the same definition of a small business that the SBA used in 2022: an independently owned and operated enterprise not dominant in its field of operation that falls below certain headcount or annual receipts thresholds based on its North American Industry Classification System (NAICS) code. Additionally, CAP uses the broader definition of a small business used by the SBA Office of Advocacy: "an independent business having fewer than 500 employees."

## Business ownership is a pathway to opportunity and wealth

Strong evidence exists on the link between business ownership and wealth generation. Business equity is the second-largest source of household nonfinancial assets in the United States, behind only the primary residence. CAP analysis of the Federal Reserve's 2022 Survey of Consumer Finances finds that business equity accounts for roughly 34.3 percent of families' nonfinancial assets, compared with 45.5 percent for the family home. And this relationship grows with household net worth, as 47.9 percent of families in the top 10th of net worth hold business equity, compared with 11.3 percent of families in the third quartile. (see Methodological Appendix) Additionally, a recent CAP analysis found that pass-through business income is the fastest-growing component of income of the top 1 percent of wealthiest Americans, surging more than 1,000 percent since 1980 and far outpacing wages. By 2022, the top 1 percent drew roughly one-quarter of their income from pass-through businesses. Overall, nearly $7 in $10 of all pass-through business income flows to the top 1 percent.

Communities that historically have lower rates of business ownership also see disparities in wealth. For example, a National Community Reinvestment Coalition analysis of the 2022 Survey of Consumer Finances data found that nearly one-quarter of the gap in average net worth between white and Black households is attributable to differences in business assets alone and estimated that raising the share of Black households holding business assets by 10 percentage points would increase average Black household wealth by more than $53,000. Median net worth among Black business owners is roughly 12 times that of Black non-owners. In other words, the communities with the most to gain from the mobility that business ownership confers—twice the rate of upward movement and six times the rate of movement from the bottom fifth to the top fifth, as found by one study—experience lower rates of business ownership.

## Entrepreneurship has boomed in the 2020s, but fewer businesses plan to hire

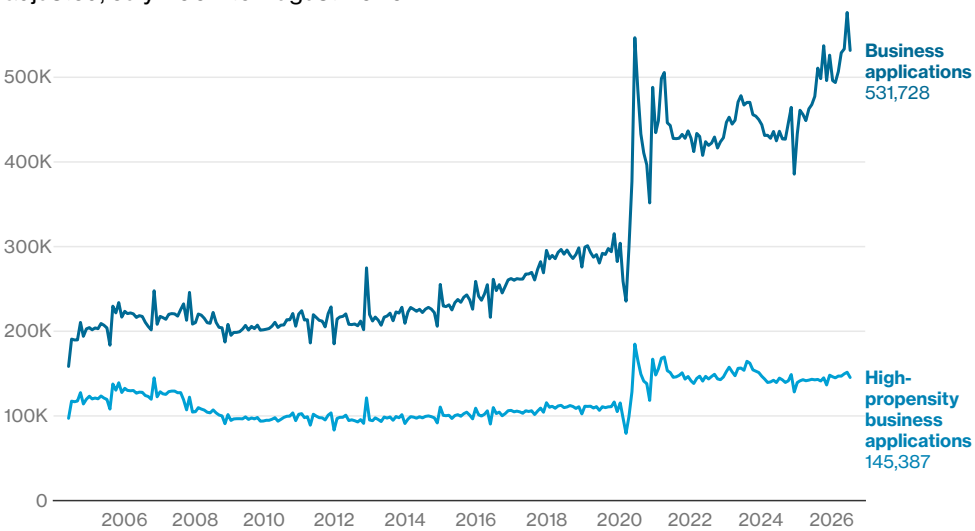
Americans are starting new businesses at historically high rates. According to the U.S. Census Bureau, in 2025, Americans filed 5.6 million applications for a federal tax identification for a new business—the highest level on record—continuing a trend of elevated business formation since 2020. Last year, Americans filed an average of 470,000 new applications per month, a rate that was 60 percent above the level in 2019, before the pandemic. Through the first half of 2026, new business applications averaged about 514,000 per month. In September 2026, Americans filed approximately 535,000 business applications—the highest monthly total so far this year. The number of business applications classified as having a "high propensity" to have payroll in the future—which the Census Bureau defines as businesses that are incorporated, have a date upon which they plan to pay wages, or are within an industry with a high likelihood of hiring, such as retail, construction, or restaurants and hospitality—also hit historic highs during this period. However, a much lower percentage of new businesses are high-propensity employers than in the past, pointing to a rise in single owner-operator businesses. Figure 1 below shows the trend in business formation dating back to 2004, which is when the Census Bureau began collecting these data.

These applications continue to result in actual business formation at an elevated rate, as shown in Figure 2 below. But business closures have also risen. While establishment deaths fell during the influx of emergency pandemic relief programs such as the Paycheck Protection Program in 2021, they have since climbed to reach near-parity with new business births through the end of 2024. Overall, businesses have been closing at elevated rates since the end of the pandemic.

FIGURE 1

## Americans are starting businesses at historically high rates

Monthly business applications and high-propensity business applications, seasonally adjusted, July 2004 to August 2026



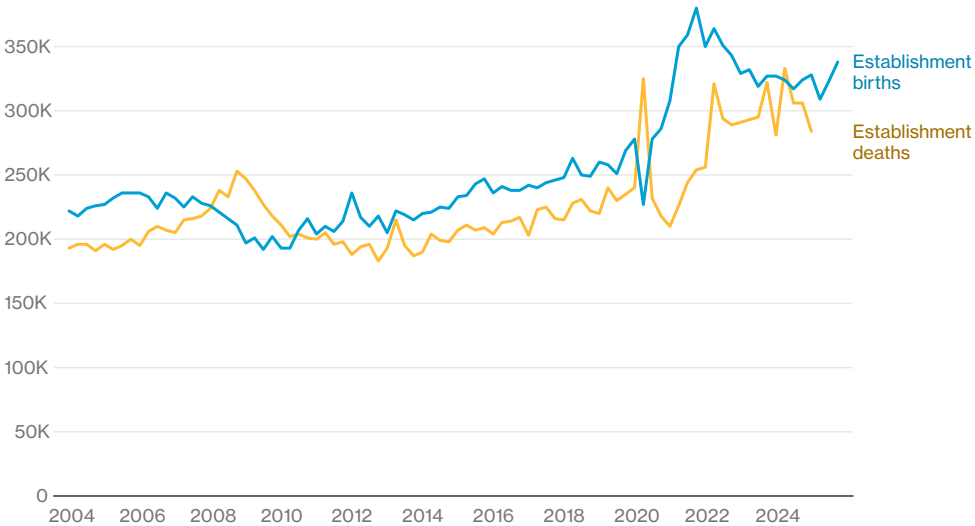

*Notes: "High-propensity business applications" are those the Census Bureau judges likely to become employers—applications that are incorporated, indicate a planned first-wages date, or fall in an industry with a high rate of transition to employer status. In January 2026, the Census Bureau narrowed that definition, retroactively excluding incorporated internet-sales applications, so the whole series shown here is on the new basis and is not comparable with high-propensity figures published before 2026.*

Source: U.S. Census Bureau, "Business Formation Statistics," Press release, October 14, 2026.

FIGURE 2

## Business formation has remained elevated since the beginning of the pandemic, but closures have caught up

Quarterly private sector establishment births and deaths, seasonally adjusted, 2004 to 2025



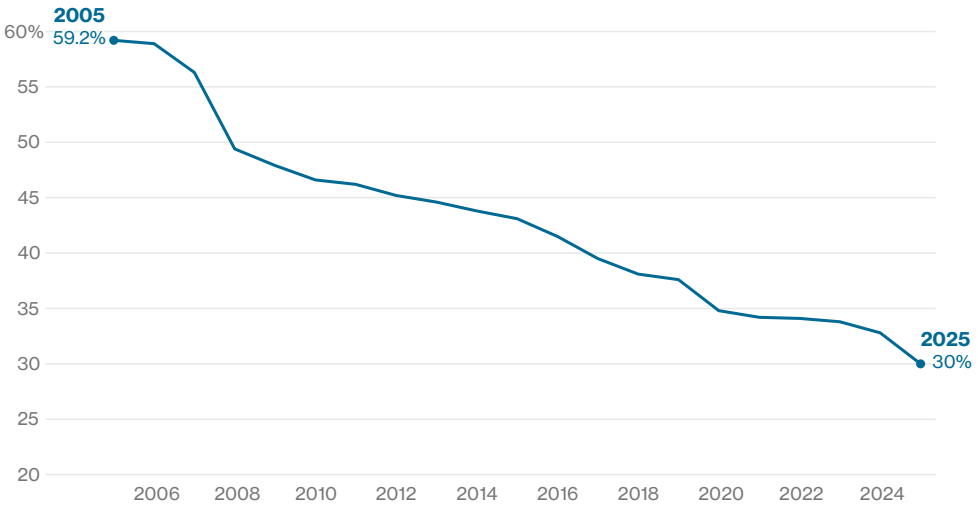

*Notes: An "establishment birth" is a business location with employees appearing in the data for the first time; an "establishment death" is one that disappears. The Bureau of Labor Statistics publishes establishment deaths three quarters behind births, so the deaths line ends at the first quarter of 2025, while births run through the fourth quarter of 2025. National Business Employment Dynamics series are published quarterly and rounded to the nearest thousand.*

Source: U.S. Bureau of Labor Statistics, "Business Employment Dynamics" (last accessed October 2026).

FIGURE 3

## A shrinking share of new businesses are likely to hire

High-propensity applications as a share of all business applications, annual average, 2005 to 2025



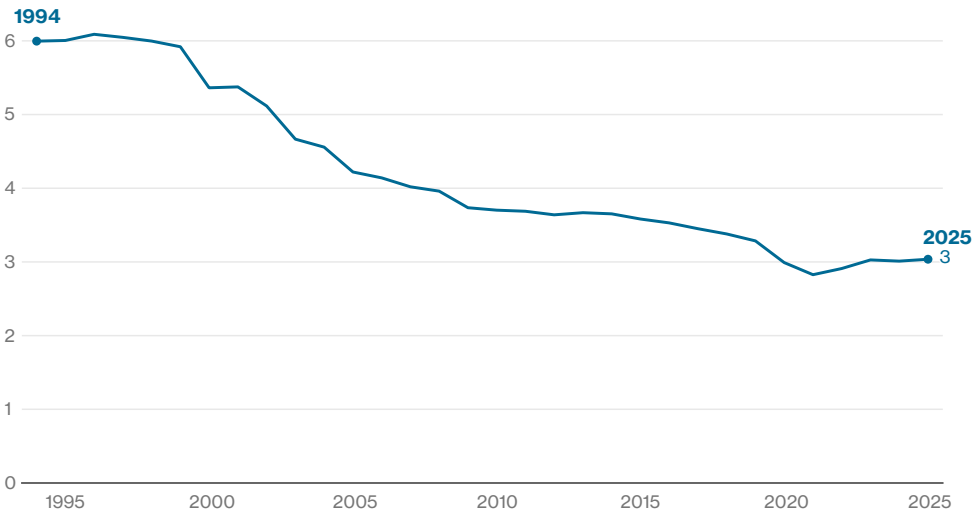

*Notes: Figures are based on CAP analysis of data through August 2026, as published September 17, 2026. Only complete calendar years are plotted. 2004 and 2026 are excluded due to only partial-year data.*

Source: U.S. Census Bureau, "Business Formation Statistics" (last accessed October 2026).

FIGURE 4

## New businesses start with about half as many workers as in the 1990s

Average employees per new establishment in its birth quarter, annual average, 1994 to 2025




*Notes: Figures are based on CAP analysis of data published on July 29, 2026. Each year is the average of its four quarterly observations of the ratio of employment gained from establishment births to the number of establishment births.*

Source: U.S. Bureau of Labor Statistics, "Business Employment Dynamics" (last accessed October 2026).

Additionally, the composition of the business formation boom tells a more complicated story. While the overall number of high-propensity applications has climbed, they have made up a declining share of business applications writ large. The high-propensity share of all applications has fallen almost every year since 2005, from nearly 60 percent of applications then to under one-third in 2025, as shown in Figure 3.

As the share of business applications likely to have payroll has declined, so too has the number of jobs created per startup. The average number of jobs created per new business has declined by half over the past three decades, falling from an average of six jobs in 1994 to three jobs in 2025, as shown in Figure 4.

These trends in part prompted the Census Bureau to change its data series on business formation: In February 2026, it removed incorporated internet-sales applications from its high-propensity business category after finding that these businesses rarely transitioned into businesses with employees.

## The Trump administration's tax policies favor wealthy business owners over mom-and-pops

Small businesses are benefiting little from the Trump administration's tax agenda. Instead of investing in new, growing, dynamic small businesses, the sweeping changes contained in the One Big Beautiful Bill Act (OBBBA) have flowed to the wealthiest subset of already-successful businesses.

The OBBBA made permanent the Qualified Business Income Deduction in Section 199A of the Internal Revenue Code and increased the types of business income qualifying for the deduction. The primary beneficiaries of the 199A deduction are high-income business owners. According to two different Joint Committee on Taxation analyses of the provision, of the $75 billion-plus in yearly tax benefits bestowed by 199A:

- Half of the benefits in recent years have gone to business owners who earn more than $1 million annually, and this trend is projected to continue going forward.
- Two-thirds (65.5 percent) of the benefits go to people making more than $500,000.
- Only 6 percent of the benefits go to small-business owners making less than $150,000, even though they make up the majority of business owners.

The 199A Qualified Business Income Deduction delivers benefits to the business owners with the largest profits, instead of incentivizing employment or economic growth. One of the only academic studies of 199A showed that it had "little evidence of changes in real economic activity" and no measurable changes in employment, similar to studies of previous pass-through business tax rate changes. In fact, 84 percent of the businesses through which individuals claimed the deduction had no employees, underscoring that 199A is not supporting job creation, just lowering taxes on profitable businesses.

The value of a tax deduction such as 199A increases with a person's marginal income tax rate, so 199A provides greater benefits for high-income business owners in higher tax brackets. For example, a married household earning $900,000 in annual income that includes $50,000 of qualified business income gets about triple the tax savings as a married household earning $90,000 in annual income. Instead of targeting aid to businesses that need support, the primary effect of this provision is often to lower a business owner's marginal tax rate to below the rate paid by their workers.

The deduction is also inequitable in the benefits it provides along racial and ethnic lines. A Treasury Department analysis found that white families received 90 percent of the benefits of the pass-through deduction while making up only two-thirds of families, compared with Black families, who were 11 percent of families but received just 2 percent of the benefit, and Hispanic families, who made up 15 percent of families and received only 5 percent.

Proponents of the 199A deduction have argued that since the corporate tax rate was cut from 35 percent to 21 percent in 2017, pass-through businesses also deserved a tax cut at the same time. They point to industry-funded studies finding positive economic results of the deduction, which conflict with the neutral peer-reviewed research cited above. However, because the deduction only applies to profits (business revenues minus expenses and investments), it can only benefit already-profitable businesses. The deduction, by definition, offers no help to a firm in the pre-profit stage of starting up and reinvesting all its revenue to grow its business. Most new businesses and all struggling businesses fit into this category and receive little, if any, help from 199A. In contrast, because tax deductions are more valuable the higher an entity's income, the most profitable businesses, which have already made it big, benefit most from the pass-through deduction. These are the businesses that least need government aid.

## Access to capital is uneven, with insufficient investment and working capital, and the Trump administration has made things worse

As more Americans have applied to start new businesses, far too many cannot get the capital they need to open their doors, make payroll, and grow. According to the Federal Reserve's 2025 Small Business Credit Survey, among businesses that applied for financing in 2025, about 49 percent of small businesses had a financing shortfall or unmet funding needs, while 25 percent of small businesses that applied for loans received all the funding requested. The share of small businesses that obtained all the financing that they needed remains below pre-pandemic levels. The same survey found that more small businesses seek financing for working capital, which is funding to cover everyday operating expenses, than they do for expansion or new opportunities.

Working capital is often more challenging for small businesses to obtain. A line of credit that businesses can use to cover operating costs such as payroll and inventory, sometimes with a limited amount of collateral, requires a more rigorous level of oversight than a term loan secured by real estate or equipment. This combination makes such loans unattractive to lenders, making these loans harder to access for younger firms, thinner-margin businesses, and entrepreneurs in underserved communities. Reduced access to traditional lenders has led more businesses to turn to online or other nonbank lenders: The share of businesses seeking credit from online fintech lenders climbed from 17 percent in the 2020 survey to 29 percent in the 2025 survey. These loans come at a higher cost: 6 in 10 borrowers who access online lenders reported in 2025 that their costs were higher than expected—due to high interest rates and unfavorable repayment terms—compared with about one-third of the borrowers at small or large banks.

The capital access challenges are more significant for minority- and women-owned businesses. An analysis of Federal Reserve 2025 Small Business Credit Survey data from the National Bankers Association found that only 16 percent of Black applicants received the full amount of capital they sought from large banks, compared with 48 percent of white applicants. Nearly half of Black applicants at large banks received no capital. Women-owned businesses report depending more on personal savings, online lenders, and personal credit cards and relying less upon lines of credit than men-owned businesses. Uneven access has had an impact on business confidence when applying for loans, with 32 percent of Black or African American-owned businesses, 21 percent of Hispanic-owned businesses,

and 16 percent of women-owned businesses that did not apply for loans citing discouragement as their primary reason—much higher than white- or men-owned businesses. Additionally, minority- and women-owned businesses face higher interest rates and stricter collateral requirements, which end up costing minority-owned businesses an additional $8 billion in interest costs annually.

Another barrier is the smaller loan size typically sought by women- and minority-owned businesses, which is less attractive to lenders because the costs of loan origination and servicing are fairly fixed while the income earned by interest is lower on smaller loans. In the Federal Reserve's 2025 Small Business Credit Survey, 71 percent of women-owned employer firms, 74 percent of Black or African American-owned firms, and 69 percent of Hispanic-owned firms sought less than $100,000 in financing, compared with 54 percent of men-owned and 58 percent of white-owned firms. At the top end, men-owned firms were more than twice as likely as women-owned firms to seek $250,000 or more, and white-owned firms more than twice as likely as Black-owned firms. This is why the SBA in 2023 finalized a rule (since changed by the Trump administration) to simplify the process for 7(a) loans below $500,000, including by allowing participating lenders to use their own underwriting processes instead of the SBA's lengthier process, and it specifically pointed to the hours of time per loan saved by the reforms.

There are also stark differences in the ability of minority- and women-owned businesses to secure equity investment, or the selling of partial ownership of the business to bring in more capital, which is particularly helpful to new businesses. Women and minority entrepreneurs capture a fraction of venture capital. Companies with at least one female founder took in about 20 percent of venture capital deal value in 2024 in the United States, and startups with all-women founding teams received only about 1 percent to 2 percent—near their lowest share since 2016. Black-founded startups received an estimated 0.4 percent of all U.S. venture dollars in 2024, down from a recent peak in 2021, and Latino-owned startups received less than 2 percent of venture funding in 2025.

The Trump administration has worsened this inequitable access to capital by reducing funding to agencies that support small businesses. The SBA cut 43 percent of its workforce, or about 2,700 of 6,500 positions. The administration also directed the Treasury Department's Community Development Financial Institutions (CDFI) Fund, the Minority Business Development Agency (MBDA), and several other entities to eliminate their nonstatutory functions and reduce statutory ones to the minimum required by law. The MBDA, which operated a nationwide network of Business Centers that helped clients secure capital and contracts, has been effectively dismantled after a sharp staffing decline. The CDFI Fund faces similar hurdles, with the

Trump administration attempting to eliminate staff and withhold funding.

The administration has also adopted policy changes that constrain access to capital, especially for women- and minority-owned businesses. The Trump administration's SBA restored lender fees and tightened underwriting in 2025 and 2026 by raising minimum credit scores, adding citizenship and residency requirements, and reinstating more stringent underwriting. Senate Democrats found that these changes contributed to a 46 percent decline in SBA lending from June to August 2025, with the smallest-dollar borrowers and underserved entrepreneurs among the hardest hit. As research from Brookings documents, this combination of staff cuts, slowing of deployment of funds, and policy changes to capital access, contracting, and business development support is deepening disparities in access to capital.

## The Trump administration's tariffs are costing small businesses

Small businesses have been hit hard by the Trump administration's tariff agenda. CAP analysis of tariff revenue data from the U.S. Treasury Department's Daily Treasury Statements and importer data from the U.S. Census Bureau's "A Profile of U.S. Importing and Exporting Companies, 2023-2024" finds that, due to the Trump administration's tariffs, the tariff costs for the nation's roughly 234,000 small-business importers more than tripled over the most recent 18-month period (from March 2025 through August 2026) compared with the preceding 18 months. The average small-business importer paid $426,000 in additional tariffs from March 2025 through August 2026 compared with the preceding 18-month period—equivalent to about $24,000 more per month. These costs reached small businesses in all 50 states and Washington, D.C. Several states faced estimated average additional tariff costs exceeding $200,000 per small-business importer, with Texas, Kentucky, and New Jersey recording average burdens of more than $300,000 per importer.

Although the U.S. Supreme Court ruled in February 2026 that the International Emergency Economic Powers Act (IEEPA) did not allow for the imposition of tariffs, the decision did not significantly deter the administration's trade agenda. Instead of abandoning its tariff policy, the Trump administration imposed similar across-the-board tariffs using Section 122 of the Trade Act of 1974. When the Section 122 tariffs expired on July 24, the administration shifted to another tariff authority to impose its tariffs: Section 301 of the Trade Act of 1974—this time justifying its 10 percent to 12.5 percent tariffs on 60 countries on the grounds that they were not enforcing bans on forced labor in their supply chains.

After the Trump administration's initial IEEPA tariffs were struck down, businesses faced significant uncertainty over whether and how they could recover the duties they had paid. U.S. Customs and Border Protection began issuing eligible IEEPA refunds, but the government's appeal of the Court of International Trade's refund order left open whether all importers would be made whole. Small-business advocates warn that lengthy court battles could leave small-business importers struggling to recover their refunds, especially those that lack the resources to pursue claims. By the end of August 2026, the government had paid out $115 billion in refunds nationwide, but most processed refunds reportedly went to large importers, while small businesses continued to face delays and burdensome applications.

## Small businesses are increasing adoption of AI tools, but progress is unequal

AI adoption has increased rapidly across the economy in recent years, including for small businesses. According to a U.S. Chamber of Commerce study, 58 percent of surveyed small businesses reported using generative AI in 2025, more than double the rate in 2023, with most adopters noting that limits on their access to AI tools would negatively affect their bottom lines. A separate survey from the U.S. Chamber of Commerce Foundation found that "[h]alf of all workers at small businesses already use AI at work," primarily to improve productivity through tasks such as writing, research, coding, and creative work, rather than fully automating human labor.

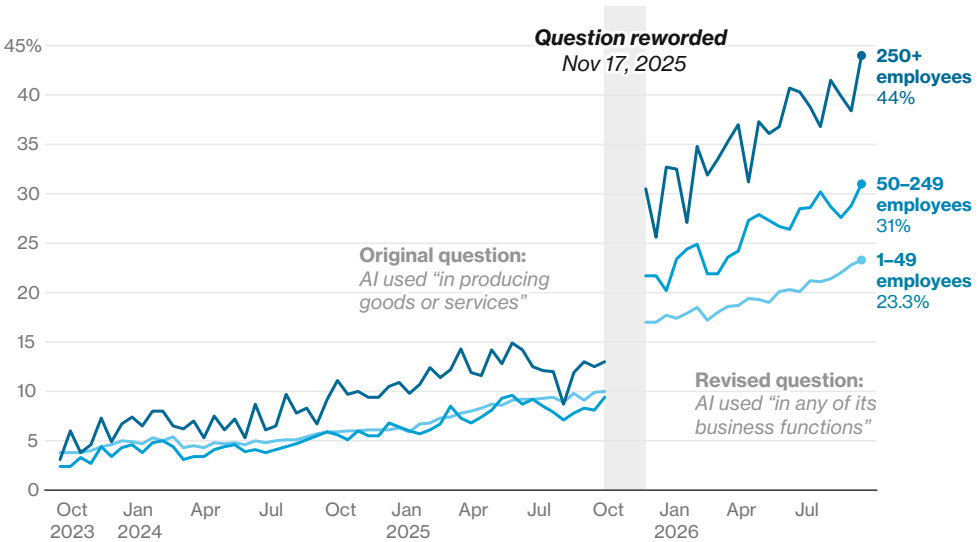
These industry surveys may overstate or understate the use of AI, however, as many firms are still in the experimental phase, and adoption has been widely uneven across business types and sectors (some of which may not be regularly surveyed on their AI usage). Nationally representative data from the Census Bureau's Business Trends and Outlook Survey—which contains a first-of-its-kind AI supplement that asks businesses about their usage of AI—highlights these trends. As Figure 5 shows, only 23.3 percent of businesses with fewer than 50 employees report using AI in any of their business functions—as opposed to 44 percent of firms with 250 or more employees—highlighting that small businesses lag large firms in successfully adopting AI and incorporating it into their business processes. While some of this may reflect firm size in and of itself—a large firm is more likely to have some employees who use AI—it likely also reflects the fact that large firms have greater financial and technical resources and better access to skilled workers who can facilitate AI adoption.

Moreover, as Figure 6 shows, small-business AI adoption has varied widely across sectors, keeping pace with larger firms in some industries but falling far behind in others. In two of the industries where small businesses are most highly repre-

FIGURE 5

## Small businesses lag large firms in adopting AI

Share of businesses using AI in any business function, by number of employees, biweekly census survey cycles from September 2023 to September 2026




*Notes: The Census Bureau revised this question in November 2025, from asking whether AI was used in the past two weeks for "producing goods or services" to whether it was used in the past two weeks "in any of its business functions." It also began a new series because the reported level shifted. The two segments are therefore drawn as separate lines. No data were collected between October 1 and November 13, 2025, because of the government funding lapse. Size groups are weighted by the number of firms in each published size class, from the Census Bureau's Statistics of U.S. Businesses (SUSB). Because the SUSB does not publish exact firm counts just above or below the 250-employee boundary, but rather reports the number of firms in the 200- to 299-employee bucket, the authors assume a log distribution of firm counts by size to divide this group; this yields an estimated 55 percent of firms in the bucket having 200 to 249 employees and 45 percent having 250 to 299 employees.*

Sources: U.S. Census Bureau, "Business Trends and Outlook Survey" (last accessed October 2026); U.S. Census Bureau, "Statistics of U.S. Businesses (SUSB) Tables" (last accessed October 2026).

sented—real estate and leasing and construction—large firms have adopted AI far more than their small counterparts, while in others, including accommodation and food services, the gap is smaller (in part because adoption is lower across the board).

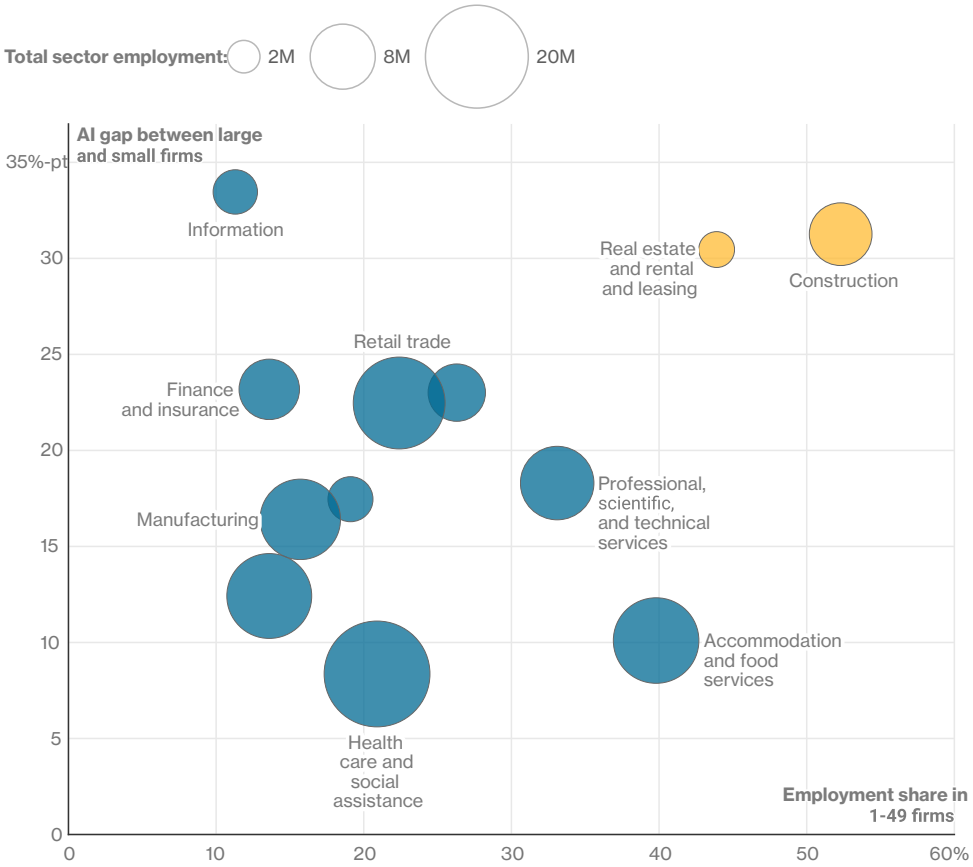
Yet another way progress in AI adoption has varied is across different demographic groups of business owners. Younger business owners, particularly Millennials and Generation Z males, report the highest adoption rates, while Baby Boomer owners continue to adopt AI at substantially lower rates. (see Figure 7) As AI tools became more widely available after 2022, adoption increased among both male- and women-owned businesses. However, adoption increased more in absolute terms among male-owned businesses, widening the gender gap in AI adoption from 0.3 percentage points in 2019 to 2.5 percentage points in 2025.

Early evidence suggests that AI can benefit small businesses, although much of it is based on owners' self-reported experiences. In a 2023 survey, more than 80 percent

FIGURE 6

## In some small-business-heavy industries, large firms are far ahead on AI uptake

AI adoption gap between the largest and smallest firms against small firms' share of industry employment, for select industries, November 2025 to September 2026




*For a full breakdown of data for each sector, see the online version of this report.* ***XX PERMALINK NEEDED XX.***

*Notes: Each bubble is one sector, sized by total employment. AI adoption is pooled across 22 biweekly survey cycles using the current question's wording, collected from November 17–30, 2025, through September 7–20, 2026. Sectors appear only where the Census Bureau published usable estimates for both the smallest and largest firms in at least nine of those cycles. Size groups are weighted by the number of firms in each published size class, from the Census Bureau's Statistics of U.S. Businesses (SUSB). Because the SUSB does not publish exact firm counts just above or below the 250-employee boundary, but rather reports the number of firms in the 200- to 299-employee bucket, the authors assume a log distribution of firm counts by size to divide this group; this yields an estimated 55 percent of firms in the bucket having 200 to 249 employees and 45 percent having 250 to 299 employees.*

Sources: U.S. Census Bureau, "Business Trends and Outlook Survey" (last accessed October 2026); U.S. Census Bureau, "Statistics of U.S. Businesses (SUSB) Tables" (last accessed October 2026).

of small-business AI users believed the technology added value to their operations. More recently, the Small Business & Entrepreneurship Council's 2026 Small Business Technology Use Survey found that 66 percent attributed revenue gains to AI, while owners reported saving a median of 5 personal hours and 11.5 employee hours per week. Research also links AI adoption with increased efficiency, innovation, lower costs, and revenue growth. For small businesses, the benefits include

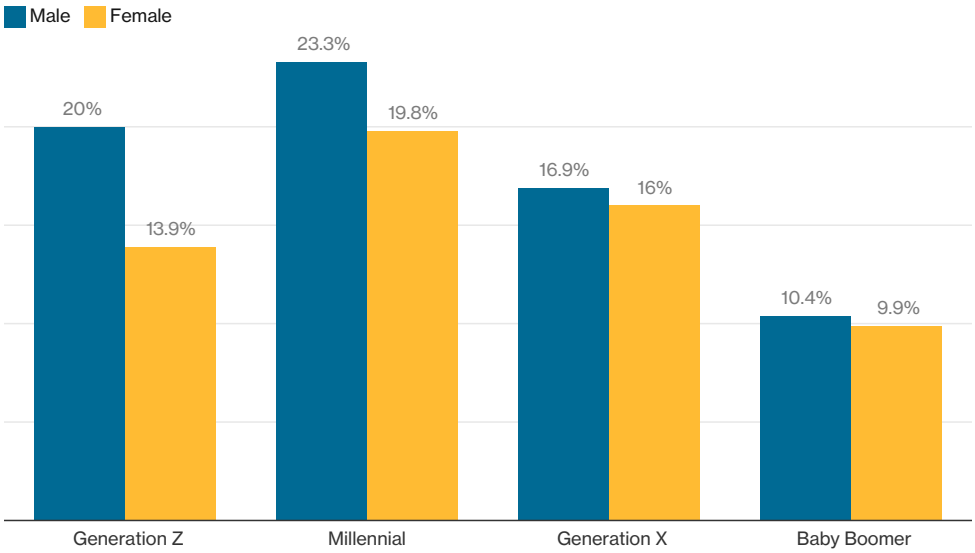
improved operations, marketing, customer engagement, and decision-making. In a randomized study involving 453 professionals, those who used ChatGPT completed writing tasks 40 percent faster and produced work that received 18 percent higher quality ratings. Although this experiment was not specific to small businesses, it illustrates how AI could help resource-constrained firms improve productivity.

At the same time, AI is contributing to the emergence of smaller, leaner businesses. AI-native firms—startups or small businesses that integrate AI into their core busi-

FIGURE 7

**AI adoption is higher among men across every generation**

Share of small-business owners who adopted AI, by owner gender and generation, 2025




*Notes: The sample consists of firms active in 2025. A firm is considered an AI adopter if it paid for at least one AI service. Owner generation is based on the youngest owner's age; firms without owner-age information are excluded.*

Source: Chris Wheat, Chi Mac, and Andrea Passalacqua, "The AI Adoption Gap: Gender and Generation Among Small Business Owners" (New York: JPMorganChase Institute, 2026).

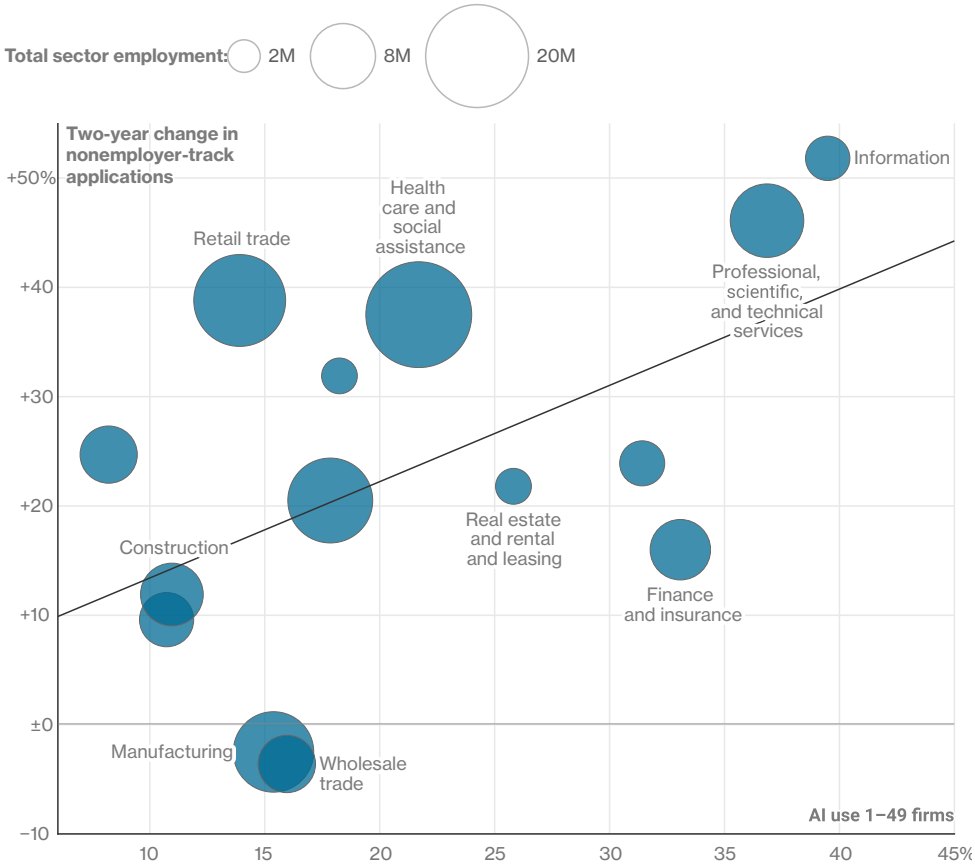
ness functions upon firm creation—can build their operations around these tools and run leaner or scale more efficiently. A 2026 working paper by researchers at INSEAD and Harvard Business School found, "Relative to non-AI startups in the same industry-cohort, AI-native firms are 25% smaller." Indeed, as Figure 8 shows, industries where small-business AI adoption is the highest are generally also those where the number of nonemployer-track business applications grew the most over the past two years.

These patterns suggest that unequal access to AI-driven productivity gains may

FIGURE 8

## Small-firm AI use is highest in the industries adding the most new nonemployer businesses

AI use among firms with 1 to 49 employees versus the change in nonemployer-track business applications, by sector, November 2025 to September 2026




*For a full breakdown of data for each sector, see the online version of this report.* ***XX PERMALINK NEEDED XX.***

*Notes: Nonemployer-track applications are all business applications minus high-propensity applications—that is, those the Census Bureau judges likely to become employers. Each point compares the 12 months ending August 2026 with the same 12 months two years earlier, not seasonally adjusted. AI adoption is pooled across 22 biweekly survey cycles using the current question's wording, collected from November 17–30, 2025, through September 7–20, 2026. Sectors appear only where the Census Bureau published usable estimates for both the smallest and largest firms in at least nine of those cycles. Accommodation and food services is excluded because the Business Formation Statistics classify every application in that sector as high-propensity by rule, making its nonemployer track total zero by construction. Bubbles are sized by sector employment. The relationship is correlational and should not be read as causal.*

Sources: U.S. Census Bureau, "Business Formation Statistics" (last accessed October 2026); U.S. Census Bureau, "Business Trends and Outlook Survey"; U.S. Census Bureau, "Statistics of U.S. Businesses (SUSB) Tables" (last accessed October 2026).

persist despite the increasing accessibility of AI technologies. While AI may enable some new and AI-native firms to operate more leanly and scale more efficiently, existing small businesses may not benefit equally. If these gains prove large, they could allow larger firms to outcompete smaller businesses—especially in industries where small businesses are currently overrepresented—while in other cases they

may cause businesses owned by older Americans, women, and other underrepresented groups to fall behind.

## Millions of Baby Boomer business owners will retire in the coming years

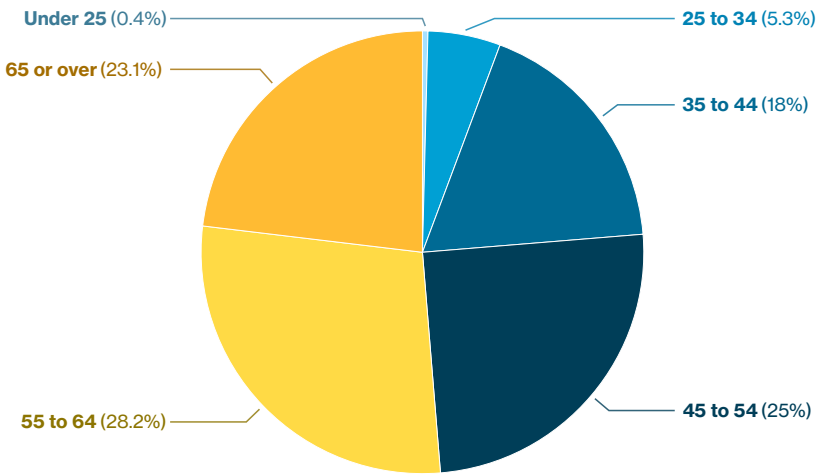
Although record numbers of Americans have engaged in entrepreneurship in recent years, about 6 million small and medium-sized businesses owned by Baby Boomers are expected to need to transition ownership by 2035 as their owners retire. In 2023, half of small businesses with employees were owned by an individual over age 55. (see Figure 9) Many of these businesses are financially healthy, integral keystones of their local economy, yet a Gallup Poll from September to October 2024 revealed that 52 percent of business owners over age 55 reported they were considering closing the business entirely or did not have a plan once they retired. Communities everywhere will feel the effects of the Silver Tsunami as Baby Boomers retire, leaving small businesses to either transition ownership or die out.

Small businesses owned by individuals 55 years old or older are critical to local

FIGURE 9

### Half of small businesses are owned by those near retirement age

Percentage of small-business owners with employees, by age of owner, 2023




*Notes: The Small Business Administration finds that 99.9 percent of businesses are small businesses, so the authors assume that this portion is applicable to small businesses surveyed in the Annual Business Survey.*

Sources: Authors' calculations based on data from U.S. Census Bureau, "Annual Business Survey: Owner Characteristics of Respondent Employer Firms by Sector, Sex, Ethnicity, Race, and Veteran Status for the U.S., States, Metro Areas, and Counties: 2023" (last accessed October 2026); U.S. Small Business Administration Office of Advocacy, "Frequently Asked Questions About Small Business 2026" (last accessed October 2026).

economies not only because they create jobs in communities but also because they are more likely to report that other businesses are their customer base, underscoring how critical these small businesses are in the supply chain ecosystem. As owners retire and shutter their small businesses, communities will feel the economic effects. Small businesses are boons for local economies, with $0.68 of every $1 spent at a small business going back into the community and generating an additional $0.48 of local business activity. A 2026 analysis from the McKinsey Institute for Economic Mobility revealed that rural economies are more likely to have higher exposure to the negative shocks of these business closures, as they are more likely to have older business owners and the highest business exit rates.

One option for the transition of these businesses to new ownership is through employee stock ownership plans (ESOPs), which are tax-qualified retirement plans that invest in employer stock and allocate shares to employee accounts over time. ESOPs are associated with higher productivity, improved firm performance, and lower layoff rates. Additionally, ESOP participants have higher compensation, better benefits, and substantially greater retirement wealth than non-ESOP workers in the United States. In 2023, there were 6,525 plans, representing more than 15 million participants and holding estimated assets of $2 trillion. There are incentives at each level of government to support the creation of ESOPs; however, barriers remain, such as education and awareness, as well as access to capital to support the business transition. Several fixed costs in establishing an ESOP trust prevent formation; these are covered in the policy recommendations below.

Another option for business succession is through "entrepreneurship through acquisition" (ETA), which is the process by which a third-party individual buys an operating business from an owner, usually backed by a search fund. ETA business transitions can keep local businesses in operation and often occur in industries such as services, software, technology-enabled services, health care, and education. In such transfers, the seller can retain an ownership stake in the business to allow their license or client base to be used to maintain the business. ETA is a viable option for those wanting to become entrepreneurs while avoiding the volatility of early start-ups. Data on ETA deals are less available than data on ESOPs. In 2023, there were 29 ETA transactions from search funds, according to the 2024 Stanford Graduate School of Business Search Fund Study, down from the record high of 40 acquisitions in 2021. In total, Stanford found that 296 companies were acquired by search funds from 1984 to 2023 in the United States and Canada.

Sellers and buyers face barriers in the business transition process. Most business

owners do not have plans for business succession in place; 85 percent of business listings with the intent to sell do not sell due to inaccurate valuation, underscoring a national need for business succession planning and guidance. On top of these challenges, the Trump administration recently made policy changes that make business succession more difficult.

The Trump administration's SBA has changed the standard operating procedures (SOP) it provides to its lenders to add significant personal risk for sellers and add several barriers to accessing capital. Under the latest guidance in SOP 50 10 8.1, sellers are forced to choose between retaining some equity in their company in exchange for offering a personal guarantee on the buyer's debt and departing from the company 24 months after the sale. Generally, the SBA has required anyone who owns 20 percent or more of a business receiving a 7(a) loan to personally guarantee it, meaning that their own assets, including personal savings and often a home, are on the line if the business defaults. Under the Trump administration's SOP 50 10 8 changes, the SBA required sellers who want to retain equity of any amount to personally guarantee the SBA 7(a) loan for two years, which adds an unnecessary layer of personal risk for a seller who previously could retain a small ownership interest to facilitate the transfer by permitting the use of their licenses, client lists, and more.

Moreover, the Trump administration's revisions to the SOP made it much more difficult for sellers to help finance buyers when the 7(a) lender required an equity injection. Previously, the SOP required at least a 10 percent upfront equity injection (effectively a down payment), and the seller could loan the buyer the entire amount (a "seller's note") and begin receiving debt payments from the buyer as soon as two years later. Under the Trump administration and SOP 50 10 8, the SBA has essentially closed this door, requiring a 10 percent equity injection, capping sellers at financing half of that amount, and requiring that the seller receive no payments on that loan until the SBA loan is paid off—referred to as being on full standby—which is typically 10 years but can be up to 25 years.

# The CAP agenda to expand small-business ownership to build wealth

CAP proposes a broad and bold agenda to help more Americans seek opportunity and wealth generation through entrepreneurship and job creation. This agenda would expand access to capital, encourage and support job-creating new businesses, reduce tax filing headaches for mom-and-pops, and help transition millions of businesses owned by retiring entrepreneurs. This agenda could be funded by greatly restricting or eliminating the inequitable 199A pass-through business deduction, which sends roughly two-thirds of the more than $75 billion in tax relief it provides each year to business owners who earn more than $500,000 in annual income.

## Replacing tax breaks that are rigged to disproportionately favor wealthy business owners by instead focusing benefits on mom-and-pop businesses

Instead of subsidizing the most profitable and well-connected businesses, tax policy should reduce filing burdens for small businesses that struggle to compete with larger businesses that can better afford sophisticated tax advisers. Small-business tax policy should also encourage job creation and the establishment of strong, sustainable small businesses.

At a fiscal cost of $49 billion per year, the following two tax reforms would benefit about 18 million small businesses, overwhelmingly those that earn less than $250,000 in annual income, while sparking the creation of 630,000 jobs at small, new employers. This would represent a stark departure from the 199A Qualified Business Income Deduction. That deduction has an annual cost of more than $75 billion targeted at the wealthiest businesses, with no evidence that it creates any jobs. Business owners making less than $500,000 per year would receive roughly twice as much aggregate support from CAP's proposals as they do under the current 199A deduction.

TABLE 1

**Compared with current policy, CAP's proposals cost less, simplify tax filing, and provide more support to nonwealthy business owners**

Comparison of the Big Beautiful Bill's 199A pass-through business deduction versus CAP's proposed small-business tax policies

| | 199A pass-through business deduction | CAP-proposed Standard Small Business Deduction and Small Employer Jump-Start Credit |
|---|---|---|
| 2026 annual cost | $76 billion | $49 billion |
| Small-business jobs created | 0 | 630,000 |
| Annual support for businesspeople making over $500,000 | $50 billion | Less than $10 billion |
| Annual support for businesspeople making under $500,000 | $26 billion | More than $49 billion* |

**This figure includes tax savings and $10 billion in saved filing time and costs.*

Source: Original CAP analysis of new tax proposals, as described in Methodology section, and authors' calculations based on data from Lucas Goodman and others, "How do business owners respond to a tax cut? Examining the 199A deduction for pass-through firms," Journal of Public Economics 242 (2025): 105293; Thomas A. Barthold, "Memorandum re: Distributional Analyses of Extension and Modification of Section 199A," Joint Committee on Taxation, June 2, 2025.

## Small-business tax filing made simple and easy: The Standard Small-Business Deduction

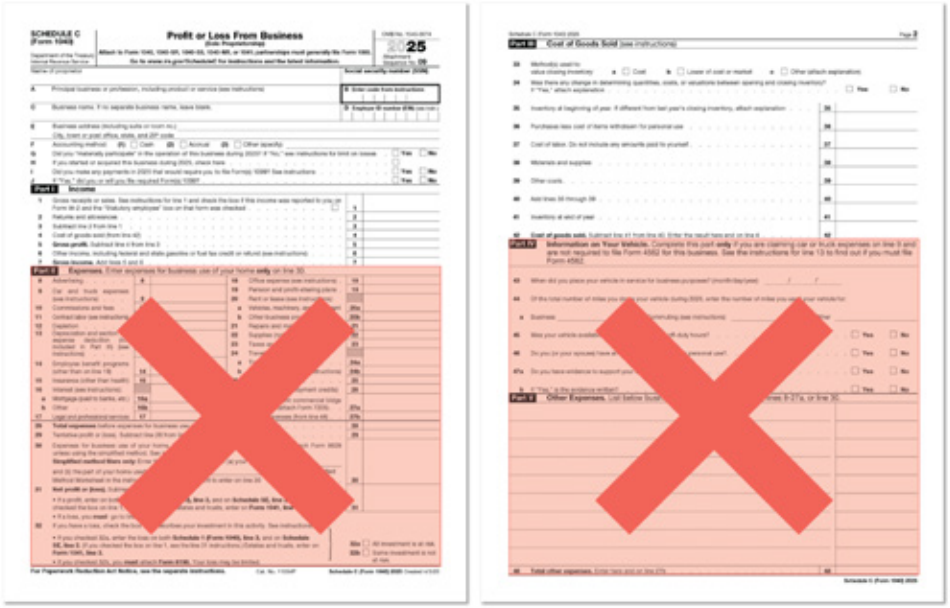
Tax filing is a major burden on many small businesses, especially for startups and small businesses without accountants. Per IRS estimates, small businesses on average spend 21 hours filing taxes yearly, at an average cost of $610 for related out-of-pocket costs for tax preparation and other services. Rather than demanding that small-business owners become experts in tax preparation or pay for expensive services to file taxes, the U.S. tax code should provide small businesses with an expedited, simple way to file. This would make it easier for small and new businesses to form and operate, as well as allow small-business owners to focus on running their businesses.

CAP proposes that small businesses be given an expedited tax filing option: a "Standard Small-Business Deduction" that can allow them to quickly and easily file taxes without needing to keep drawers of receipts, calculate vehicle mileage and asset depreciation, or worry about an IRS audit of those expenses. The Standard Small-Business Deduction would allow most small businesses to automatically write off 65 percent of their modified net income (business receipts minus the cost of goods sold and wages). As long as all calculations are made correctly, this would greatly decrease the possibility of an IRS audit, saving time for both the IRS and small-business owners. And small businesses would no longer need to pay for most tax preparation services.

FIGURE 10

## A Standard Small Business Deduction would greatly simplify tax filing for small businesses

Businesses that file a tax return using Schedule C: Sole proprietorship would no longer complete three of the five sections if they took the Standard Small Business Deduction



*Note: A majority of businesses file using Schedule C. Business owners with an S corporation with a single owner would also have a greatly simplified Form 1120-S if they used the Standard Small Business Deduction. Businesses filing using other forms would not be eligible.*

Source: CAP rendering.

Under CAP's proposal, a business owner filing the standard Schedule C form would no longer have to fill out Parts II, IV, and V for their sole proprietorship business. Instead, they would just fill in "Part I: Income," subtract "Part III: Cost of Goods Sold" plus wages paid, and finally deduct 65 percent of the remaining as the Standard Small-Business Deduction. (see Figure 10)

This proposal could save an average business owner or self-employed person $305 in out-of-pocket costs and 10 hours per year by cutting in half the amount of time spent on tax preparation and reducing the need for tax preparation services. At $37.81 per hour, this would be total average savings of about $680 yearly for businesses that take the Standard Small-Business Deduction. Research suggests that under this policy, even small businesses that could deduct more than 65 percent after the cost of goods sold and wages would sometimes still be better off due to the time and filing cost savings.

Similar to a proposal from University of North Carolina School of Law professor Kathleen DeLaney Thomas and a previous national proposal, CAP's proposal would allow most businesses to write off 65 percent of their modified net income while ensuring that businesses can still choose to continue calculating their taxes in the traditional manner. CAP estimates that the majority of small-business owners and self-employed individuals would be able to take advantage of this proposal, but to prevent abuse and to direct this program where it is needed most, there should be some restrictions:

- Businesses would be capped at writing off 65 percent of expenses after the cost of goods sold and non-owner employment costs, or $300,000 of modified net income, whichever is less.
- Businesses that have very low overhead expenses, such as specified service trades or businesses (SSTBs), real estate agents, engineers, and architects, would be limited to writing off only 15 percent of modified net income or $70,000, whichever is less.
- Businesses must file as either a sole proprietorship (using Schedule C on Form 1040) or as an S-corporation with one taxpayer owner.
- After business owners' overall adjusted gross income exceeds $375,000, their ability to use the deduction for their businesses would begin to phase out.

A Standard Small-Business Deduction of 65 percent of revenue after cost of goods sold and wages is consistent with the average level of deductions by these businesses in the tax data. CAP's analysis of IRS Statistics of Income data finds that in 2022 the average sole proprietorship with net income had deductions equal to 68.5 percent of its revenue, and this ratio has been relatively stable over time. After subtracting the cost of goods sold and wages, sole proprietorships deducted about 57 percent of their revenue. S-corporations with net income deducted more, about 83 percent overall and 74 percent after deducting cost of goods sold and wages. CAP's proposal attempts to approximate this overall average deduction level by setting the Standard Small-Business Deduction at 65 percent for most businesses and 15 percent for low-overhead businesses.

In addition, IRS data indicate that more than 60 percent of S-corporations have only one owner, so most would be eligible for the Standard Small-Business Deduction. It may also be appropriate to include C-corporations that have only one owner. CAP's analysis of C-corporation tax returns indicates that including them under similar rules would have only a small effect on cost and the number of businesses covered.

However, certain industries have fewer deductions than average and would be limited to deducting 15 percent of modified net income under this proposed Standard Small-Business Deduction. Many industries restricted to only deducting 15 percent of modified net income are referred to in the tax code as SSTBs and include fields such as health, law, consulting, and financial services, which have lower overhead costs than fields such as manufacturing or food service. Giving them the standard 65 percent write-off would be excessive since these industries less frequently have write-offs that large. SSTBs already have limited deductions under the 199A deduction. In addition, professions such as real estate agents, engineers, and architects have very little overhead and should also be limited to 15 percent. These restrictions help contain costs without unduly burdening most businesses, allowing the overall Standard Small-Business Deduction to be a higher percentage than it would otherwise be.

To prevent fraud or gaming of the new Standard Small-Business Deduction, businesses would need to file as a sole proprietorship or an S-corporation with a single individual owner to access this benefit. Since businesses such as partnerships can own other businesses, and often facilitate complicated tax avoidance schemes, they would not qualify for the deduction, and eligible businesses would not be able to deduct against K-1 income received from partnerships. However, current partnership owners could reorganize their business as an S-corporation or as a sole proprietorship to access the deduction. Finally, income limits on the deduction would ensure the benefit is targeted to the middle- and working-class business owners and self-employed people who need support the most.

Based on 2022 Statistics of Income data, CAP estimates that 25 million small businesses would be eligible to take this deduction out of the total 36 million. Most of the remainder would be businesses that had negative income or were organized as a partnership. Those businesses could take the deduction in a later year when they had net income or had reorganized as an eligible business type. CAP estimates that about 16 million businesses would take this deduction in a given year, delivering $26 billion in direct tax relief to businesses, plus $10 billion in relief from tax filing fees and time spent preparing returns.

In all, this proposal would provide $36 billion in yearly benefits to the millions of small-business owners making less than $500,000 per year, while avoiding subsidizing business owners with incomes above $500,000, who are the primary beneficiaries of the 199A deduction. The Standard Small-Business Deduction would provide certainty and tax relief to the business owners who need it most, instead of those who need it least.

### The Small-Employer Jumpstart Credit

Small businesses are responsible for half of all new job creation in the economy, and young, new businesses are especially important for economywide job creation. Unfortunately, job creation by new small businesses ("startups") has been falling in recent years, and current public policy does not effectively encourage business owners to transition from being a sole operator to being an employer.

The vast majority of small businesses employ no one other than their owner, but businesses that become employers are much more likely to survive than those that do not. Despite accounting for only about 3 percent of overall employment, startups have historically accounted for 20 percent of gross job creation in the country. Furthermore, advances in AI are creating fears that hiring could slow for targeted occupations in the coming years. It is clear that small businesses are crucial for American job creation but that few small businesses make the leap to employing workers. A crucial question for the future of American job creation and small-business dynamism is: How can more small businesses be encouraged to employ workers?

However, becoming an employer involves risks for entrepreneurs. In addition to the cost of recruiting, training, and paying a new employee, businesspeople must take on new legal liabilities, record-keeping requirements, and taxes. These burdens can be substantial and prevent business owners from taking otherwise economically beneficial actions. To counter these concerns, CAP recommends further replacing the 199A deduction with a new tax policy that will boost hiring by lowering employers' cost of initial hires: canceling employer-side payroll taxes for new employers. This tax break could help encourage employers to make the leap to employing workers and keep the pipeline of small-business growth strong.

Federal payroll taxes amount to 7.65 percent of wages paid for most workers, discounting unemployment taxes. Businesses hiring their first nine employees should be relieved of paying their side of payroll taxes for the first two years that a worker works for that employer. This would be an instant savings for an employer off each payroll check, capped at $7,500 per employee per year, saving them about 5.7 percent of the total costs of a new employee. (Wages are 74 percent of total compensation costs at small employers.) The U.S. Department of the Treasury would transfer an amount equal to the tax forgone to the Social Security and Medicare trust funds, which these payroll taxes fund.

A small business that pays its workers the national average for a business with fewer than 50 employees ($27.68 per hour in May 2026) would save $85 every week, or $4,400 yearly per worker, from this policy. CAP estimates that this program's

benefits would flow to 2 million businesses, helping them hire and retain workers, and would subsidize the employment of more than 6 million workers at a yearly cost of $23 billion.

The main effect of this program will be to spark 85,000 new small employers and to grow overall small-business employment by 630,000 jobs. By lowering the cost of employing the first several workers, this program would make it easier for employers to grow. Since most small businesses employ no one other than the owner, there is a vast pool of potential employers that could hire if given the right incentive. CAP derives this estimate using the results of a similar Belgian program that expanded the number of new small employers by 31 percent. CAP's Small-Employer Jumpstart Credit would target businesses that need support to grow, leading to a more dynamic small-business sector.

### Small-Employer Jumpstart Credit, by the numbers

**29.8M**
Small businesses with no employees but the owner

**7.65%**
Employer payroll tax reduction under the Small-Employer Jumpstart Credit (for two years)

**85K**
more small businesses would become employers yearly with the Small-Employer Jumpstart Credit

**630K**
jobs would be created at small businesses under the Small-Employer Jumpstart Credit

**28%**
Proportion of all employers that would receive a benefit under the Small-Employer Jumpstart Credit

Sources: Small Business Administration Office of Advocacy, "Frequently Asked Questions about Small Businesses" (2026); authors' calculations based on U.S. Census Bureau, "Business Dynamics Statistics: Firm Size: 1978-2023." See the Methodological Appendix for further details.

There is a long history of business and employment subsidies that have been ineffective at creating jobs. The Small-Employer Jumpstart (SEJ) Credit is designed to avoid the pitfalls that have made other programs ineffective. First, unlike the Work Opportunity Tax Credit, which evidence shows does not create jobs, firms are able to know in advance that their hires are eligible for the SEJ Credit. Second, unlike the Employee Retention Tax Credit, which had an incredibly high cost per job retained because employers claimed the credit years after employment decisions were made, the SEJ Credit can be deducted from a business's books in real time as a payroll tax suspension after new employers form. Third, distinct from state job creation programs that reward hiring and not net job creation (and therefore incentivize firms to lay off workers and hire new ones for the same roles), the SEJ Credit only applies to the first few jobs created at a business; businesses are not eligible if they are already employers. Fourth, unlike profit-based incentives such as the 199A Qualified Business Income Deduction, the SEJ Credit directly incentivizes employment instead of cutting taxes on profits in the misguided hope that profits will trickle down to workers.

Finally, the Small-Employer Jumpstart Credit is directly modeled on policies that academic research has found to be an efficient way to create jobs and new small-business employers. A similar Belgian program, which began in 2016, canceled employer Social Security taxes for firms hiring their first employee. Researchers find that this increased the number of new small employers in Belgium by 31 percent, driven by preexisting nonemployers hiring a new employee in response to the tax exemption. The study finds no evidence that existing employers closed firms and reopened them to claim the credit, though a prudent U.S. policy should include safeguards to limit the ability of employers to do this. Another study examines a French payroll tax cancellation for small employers hiring new low-wage employees, and finds that firms increased employment expenditures by $4 for every $1 in reduced labor costs from the tax cut, resulting in a cost per new job of only $19,000 in lost tax revenue (converted from euros to dollars and indexed for inflation).

Extrapolating from these studies' findings and applying them to the most recent Business Dynamics Statistics from the Census Bureau,* CAP estimates that of the 2 million businesses that would participate yearly in the Small-Employer Jumpstart Credit, 160,000 would be new employers that would not have hired their first employee without this incentive. The credit would result in 630,000 additional jobs at America's smallest businesses yearly and would subsidize more than 6 million small-business jobs yearly overall. This would come at a yearly cost of $23 billion, or $35,800 per new job, which compares very favorably to the programs discussed above and is in line with or better than other estimates of the cost per job of government tax and spending programs.**

There is also suggestive evidence that an incentive such as this can make it more likely that America's small businesses survive and thrive. According to one Census Bureau study, small businesses that become employers are 2.5 times more likely to survive over eight years than those that have no employees but the owner. While many aspects can drive these findings, it is clear that the most successful small businesses are the small minority that hire employees. In contrast, the current 199A deduction creates no new jobs because it subsidizes profits, not employment, and flows primarily to businesses that have already achieved high net incomes. American tax policy should follow the evidence on how to grow small-business jobs and encourage the factors that lead to success in small businesses.

## Investing to expand access to both lending and equity capital for small businesses

Capital is an essential ingredient for entrepreneurship. Fewer than half of small-business loan applicants receive all of the financing they seek, and the gaps are largest for the youngest firms, the smallest loans, and women and minority entrepreneurs. CAP recommends that roughly $3.1 billion of the revenue saved from eliminating the 199A deduction be invested in the following initiatives to address capital gaps.

### A public option for working capital

The federal government's flagship small-business lending program overseen by the SBA does not fully deliver the product that small businesses need most. The SBA's long-standing line-of-credit offerings have never attracted lenders: SBA Express lines carry only a 50 percent guaranty, significantly less than the protection lenders receive on standard 7(a) term loans, while the SBA's CAPLines program's fee structure and monitoring requirements have made it, in the SBA's own assessment, an unpopular option among lenders and borrowers alike.

The Biden administration recognized these challenges and launched the 7(a) Working Capital Pilot Program in 2024 to offer competitively priced credit lines and reduce small businesses' dependence on credit cards and other costly funding sources. Initial uptake for the program has been slower than anticipated, as it has delivered roughly $150 million in lending since its August 2024 launch—less than half of the SBA's own first-year projection of $337 million for fiscal year 2025. Industry reports suggest that the uptake may be limited in part because lenders are wary of the program's compliance requirements.

With insufficient access to affordable working capital products, small businesses are turning to costlier substitutes. According to one report, only about 8.5 percent of small businesses report that working capital loans from banks are readily available, and many report considering turning to credit cards. The merchant cash advance industry—the products of which can carry effective annual rates several times those of a bank loan—has grown into a market that industry analysts estimate at roughly $20 billion in the United States, projected to reach nearly $33 billion by 2032. Merchant cash advance debt had become so pervasive among SBA-eligible borrowers that "graduating" from a merchant cash advance into a lower-cost SBA loan was a common lifeline until the Trump administration's revisions of June 2025 to the agency's revised SOP made merchant cash advances and factoring agreements ineligible for 7(a) refinancing. This change undermined one of the

goals of the Working Capital Pilot, which was to reduce small businesses' dependence on credit cards and other costly funding sources. Lending industry executives warn that the SBA's recent tightening will drive more borrowers to pricier nonbank lenders.

Given the challenges with creating a competitive market for working capital lenders offering affordable lines of credit through the SBA's traditional tool of guaranteed lending, CAP recommends authorizing the SBA to originate working capital lines of credit and small working capital term loans directly to creditworthy businesses that private lenders decline to serve. This public option for working capital should offer small lines of credit not offered by the private market, with loans of up to $150,000 for most businesses and $1 million for manufacturers, delivered through the modernized online application infrastructure that the SBA built during the pandemic.

The CAP proposal is similar to one the Biden administration proposed and the House Committee on Small Business approved in September 2021, envisioned as a direct 7(a) loan product that would serve as "a public option if businesses can't access capital through the private market." At the time, the House Committee on Small Business approved nearly $4.5 billion over 10 years to fund the program. CAP recommends an annual subsidy for this program of $450 million, sufficient to support roughly $5.8 billion in annual direct lending, reaching nearly 69,000 small businesses each year.

### A new subsidized 'Main Street Advantage' loan

The Trump administration has made loans for the smallest businesses, which are disproportionately women- or minority-owned, more expensive. CAP recommends that policymakers reverse the Trump administration's lender fees, tightened underwriting, and restriction on the ability of lawful permanent residents to access the SBA 7(a) and 504 programs. And policymakers should go further to expand access to capital through the establishment of a subsidized tranche of loans targeted at communities that have historically faced capital gaps.

Beyond merely removing the Trump administration's restrictions on SBA loans, CAP recommends a permanent "Main Street Advantage" tier within 7(a) that waives all upfront guaranty fees and annual servicing fees on loans of $500,000 or less; raises the government guarantee to 90 percent on loans of $150,000 or less, up from the standard 85 percent; and buys down interest rates by 2 percentage points on loans to businesses in low- and moderate-income communities or rural areas and to veteran-owned firms. These elements expand access to the small loans that businesses in

these communities need by addressing the fact that banks have curtailed these loans because the fixed origination and servicing costs make small loans the least profitable for traditional financial institutions to make.

Providing subsidies for small SBA loans of $500,000 or less will expand access to credit, particularly for women- and minority-owned businesses. The efforts of the Biden administration's SBA to streamline the process for making small loans for 7(a) lenders helped drive the agency's tripling of the number of loans to Black-owned businesses and doubling of loans to Latino- and women-owned businesses in fiscal year 2024 compared with fiscal year 2020. CAP recommends $650 million per year in subsidy for this program. This would support roughly 62,000 loans and $10.6 billion in small-dollar lending annually, of which approximately 12,000 loans represent new lending that would not otherwise occur.

### Create a Small-Business Strategic Investment Fund

CAP recommends that the federal government expand access to equity capital by establishing a strategic investment fund that receives $2 billion in annual funding that would make equity investments in small businesses with promise. This fund should have two subcomponents, as laid out below, and be coordinated via a Small-Business Investment Fund task force convened by the White House National Economic Council that includes as members the secretaries of defense, commerce, the treasury, and energy as well as the administrator of the SBA.

First, Congress should make permanent the Treasury Department's State Small Business Credit Initiative (SSBCI), which provides funding to jurisdictions to support loan and venture capital programs for small businesses, and fund it at a level of $1 billion per year with a stronger emphasis on state venture capital programs. The SSBCI, first established by the Small Business Jobs Act of 2010 and reauthorized in 2021 by the American Rescue Plan (ARP), has directed nearly $10 billion to states, territories, and Tribal governments, which have stood up 335 separate credit support and investment programs. As of the most recent reporting from the Treasury Department as of June 2026 jurisdictions have allocated $8.9 billion and deployed more than $4.3 billion, with the Treasury Department projecting that the program will "catalyze up to $10 of private investment for every $1" of federal funding. States participating in the SSBCI as authorized by the ARP, sometimes referred to as SSBCI 2.0, allocated about 36 percent of their federal funds to support equity and venture capital programs. CAP recommends that half of this new, annual funding for the SSBCI go to support equity investments. At $1 billion annually, the SSBCI would support roughly 5,200 transactions with about 4,800 small businesses each year, catalyzing $3.7 billion in private financing and helping create or retain more than 60,000 jobs per year.

Second, Congress should create an equity investment program within the SBA's Small Business Investment Company (SBIC) program and provide it with $1 billion in funding per year. The SBIC program has been in place for more than 65 years and provides government-guaranteed leverage to privately managed investment funds, which combine it with private capital—typically up to $2 of SBA leverage for every $1 raised privately—to make equity and long-term debt investments in small businesses. While the SBIC program has a strong track record of providing early financial support to small businesses that grew into global businesses, including Apple, Costco, FedEx, Intel, and Whole Foods, the program is more advantageous to small businesses with positive cash flow due to the requirement that the privately managed funds accessing SBA leverage make semiannual interest payments. This condition leads these funds to prefer to invest in cash-flow-positive small businesses that can help the funds service the debt to the SBA.

During the Biden administration, the SBA sought to address this mismatch by creating the Accrual Debenture and a new "Accrual SBIC" license, which allow equity-focused funds to let interest accrue and repay the SBA out of investment proceeds rather than through semiannual payments. To qualify, a fund must devote a meaningful percentage of its financings to equity investments. This requirement is intended to draw venture and growth-equity managers into the SBIC program, in which equity-oriented funds accounted for only about 18 percent of financings made by Debenture SBICs—the leading category of SBIC—made from fiscal years 2017–2021. But the reform changed the timing of repayment, not its cost: Like the SBIC program as a whole, the Accrual Debenture SBIC must maintain a 0 percent subsidy rate—meaning the program must pay for itself overall without appropriated funds for subsidized loans or investments—so it cannot offer the deeper subsidy that would draw funds into the markets that private capital passes over. Small businesses would benefit from a national program that offers zero- and low-cost leverage to funds that invest equity in underserved markets and small manufacturers.

CAP recommends that policymakers establish an "Invest in America" SBIC that would receive $1 billion per year in funds to provide patient capital to small businesses in areas of low and moderate income as well as targeted industries such as manufacturing. At this funding level, the SBA could support $11 billion in annual investment capacity, reaching more than 1,500 small businesses each year with equity investments and helping close access gaps for women- and minority-owned startups.

## Democratizing access to AI tools that can help small businesses grow

CAP recommends three new policy initiatives to democratize access to AI for small businesses. First, Congress should invest in dedicated technical assistance to help small businesses better adopt AI. CAP recommends providing additional funding to support AI adoption to the SBA's Small Business Development Centers (SBDC) program, which is a $150 million program for FY 2026 that provides free counseling and training to small-business owners through 63 lead centers, with at least one in every state, that collectively anchor a network of more than 900 local service centers. Providing small businesses with access to experts in AI would enable more to evaluate their businesses to determine where AI can help them strengthen their business, whether through the adoption of AI scheduling tools, inventory forecasters, customer service assistants, or other future tools. CAP recommends an investment of $15 million per year to ensure that each of the 63 lead centers has a full-time expert on staff with funds to offer additional support across the country. This would build upon the America's SBDC AI U initiative, a Google-funded effort to deliver free AI education and coaching to entrepreneurs through the SBDC network, by providing public dollars.

Second, the SBA should also more aggressively leverage its co-sponsorship authority to negotiate partnerships with leading AI companies that put free and discounted tools directly into the hands of small businesses. The Small Business Act gives the SBA unusually permissive authority to conduct joint activities with for-profit companies for the benefit of small businesses, representing an exception to the general constraint on federal agencies from accepting private contributions or associating with commercial products. Under this authority, the SBA can negotiate agreements to allow private entities to contribute funding or other resources, subject to guardrails against co-sponsor profit, conflicts of interest, and the appearance of SBA endorsement. In past years, the SBA has used this authority to negotiate training curricula, counseling on the use of technology, and an annual convening of small-business success stories from across the country. The SBA could use this authority to obtain reduced-cost software subscriptions or training curricula that entrepreneurs could use to support their businesses.

Lastly, CAP recommends that the federal government take steps to ensure the public and small businesses have access to frontier AI models through some form of public option. Frontier AI models are "highly capable general-purpose AI models that can perform a wide variety of tasks and match or exceed the capabilities present in today's most advanced models." Access to the most advanced frontier

AI models may end up a key requirement for success in the markets of the future, but potentially high costs or restricted access may limit the ability of small businesses to compete. OpenAI, which has called access to foundational AI models the "Right to AI," previews a potential future where access to advanced AI models is critical to participation in society or is the equivalent of a necessary utility.

A frontier AI model public option—that is, a government-created or government-supported frontier AI model with access guaranteed to the public—could guard against the cost of ever-advancing AI models becoming out of reach for small businesses and the public. A healthy competitive market may make a public option unnecessary, but the government should prepare for a public option in case the trends and incentives for technology to concentrate in a few providers leave Americans and small businesses in a vulnerable position. A frontier AI public option could take several potential forms: The government could train and release its own frontier AI model for public use, it could run qualifying open-weight models on public infrastructure, or it could contract with existing frontier AI developers for access and special rates for the American public and small businesses as described above.

## Creating new pathways to owning businesses for employees and entrepreneurs seeking to acquire existing small businesses

The federal government should take a more active role in supporting and encouraging the numerous business transitions that will occur because of the Silver Tsunami. CAP recommends a three-pronged approach that eliminates barriers to business transitions to meet the surging wave of business transitions.

### Reduce the transaction costs for business transitions

To address the costs that come with business transitions, CAP recommends a tax credit to alleviate the fixed costs that can stop ESOP transactions before they start. This program would be modeled after state advancements in encouraging ESOP business transitions via tax incentives, such as Colorado's Employee Ownership Tax Credit, and would provide a fully refundable tax credit for a portion of the costs of business transitions for ESOP transactions. CAP's proposal would provide a credit worth up to 50 percent of the conversion costs, up to a $100,000 tax credit per transaction. Establishing an ESOP trust requires a trustee, an independent appraiser, and plan administration—all excluded from SBA 7(a) loans. Most ESOP deals range from $250,000 to $500,000. While there are several tax advantages to ESOPs, upfront costs remain a barrier, and this tax credit would support the creation of new ESOPs.

An average of 269 ESOPs were created annually from 2019 to 2023, the latest year for which data are available. Assuming this trend continues and that 95 percent of new ESOPs apply for the tax credit, the annual cost would be an estimated $26 million. This is a conservative estimate, as several elements in CAP's proposal would boost the number of ESOPs created annually, thus increasing uptake of the tax credit. The federal government has an opportunity to reduce the upfront transaction costs of transitioning a business over to its employees, support more business transitions, and expand opportunities for employee ownership.

ETA buyers face a parallel problem, needing capital to search for eligible businesses, conduct valuation research, and complete a Quality of Earnings analysis well before a purchase closes. CAP recommends that policymakers consider expanding the proposed tax credit to address barriers to startup capital for ETA purchases alongside additional specified eligibility criteria to target applicants most in need of assistance, such as buyers underrepresented in ETA transactions. Additionally, other elements of CAP's proposal would ease barriers to start-up capital for ETA transactions and boost business acquisitions.

### Revise and update the SBA's standard operating procedures to encourage business transitions

Updates to the SBA's SOP under the second Trump administration have placed several new barriers to ESOP creation and ETA acquisitions. Reversing them would be virtually costless and would have major implications for the future of business transitions. CAP recommends four changes to the SOP.

First, the SBA should create a program that helps cover the 7(a) personal guaranty requirement for sellers looking to retain partial ownership in a company after selling it to a worker co-op or an individual buyer. This can be accomplished through a program that provides sellers with funding to acquire reinsurance or through a direct subsidy to the 7(a) program.

Second, the SBA should address the barriers to seller financing put in place by the Trump administration. CAP recommends that the SBA allow seller notes to cover up to 75 percent of the 10 percent SBA loan required equity injections to reduce the upfront capital buyers must bring to closing. Rather than requiring sellers to wait the full life of the loan—typically a decade or more—before collecting, seller notes should have a five-year standby period.

Third, the SBA should modify the newly added Quality of Earnings (QoE) requirement for business purchases valued above $3 million to reduce duplicative spending on behalf of the lender and buyer. This new requirement is especially challenging for

ETA transactions. Instead of requiring only lenders to seek a QoE, the SBA should require that buyers also be a named party in the QoE report alongside the lender. QoEs are traditionally sought out by buyers, so this new requirement risks duplicative reports commissioned by both parties, which would cost upward of tens of thousands of dollars.

Fourth, the SBA should reverse changes made in SOP 50 10 8.1 that restricted change of ownership transactions from using 7(a) small loans standards. Under the current SOP, business acquisitions using 7(a) loans, regardless of the loans' size, are subject to stricter underwriting requirements and longer timelines for loan approvals.

### Technical assistance to ease business transitions

CAP proposes that the SBA develop an office dedicated to business transitions, funded at $80 million annually. The funds would be used to establish a federal headquarters as well as an office in each state. Remaining funds for this office would be aimed at providing education and awareness of business transition options and planning, offering technical support for ownership transitions, and providing avenues to connect available businesses with interested owners. In a Gallup poll released in 2025, more than half of small-business owners planned to close their business or were unsure about their business' future once they retire; the SBA Office of Business Transitions could provide succession guidance on planning and readiness to business owners who are ready to retire in the short term. Additionally, the SBA Office of Business Transitions could provide in-house assistance or contract with preexisting private firms to connect buyers with business owners looking to transition to support the creation of ETA transactions.

In addition to education and technical support from the SBA Office of Business Transitions, CAP suggests that the office work alongside the Treasury Department's State Small Business Credit Initiative or the SBA's Small Business Development Centers to provide regional and targeted small-business transition support. Existing SSBCI and SBDC programs have technical assistance capabilities and funding that, alongside the SBA Office of Business Transitions, could be directed to catalyze small-business transition ownership deals nationwide. The SBA should utilize these networks to deliver its transition readiness curriculum.

# Other small-business priorities

In addition to the initiatives designed to boost entrepreneurship and build wealth laid out above, CAP recommends that policymakers consider the following as additional options for strengthening and supporting small businesses.

- **Invest in paid leave.** Creating a national guaranteed paid family and medical leave program would be a powerful investment to help small businesses recruit employees, reduce costly turnover, and boost productivity. Without a public program, small employers are on their own and at a competitive disadvantage to larger, better-resourced employers who can afford to provide those benefits out of pocket. A federal paid leave program, building on successful state programs, would level the playing field to enable small businesses to compete for employees.

- **Restore and fund the MBDA.** Congress should fully fund the MBDA at a level matching its mandate under the bipartisan infrastructure law. While a court has enjoined the Trump administration's efforts to terminating the employment of virtually all MBDA staff, the agency needs appropriations and staff to function again. Under the prior administration, MBDA business centers helped minority-owned businesses secure more than $2.6 billion in contracts and $1.5 billion in capital.

- **Preserve small-business lending data.** Policymakers should require the full implementation of Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which required the Consumer Financial Protection Bureau (CFPB) to establish a comprehensive dataset on small-business credit applications, including by race and gender of owner, to prevent and identify illegal discrimination in small-business lending. In 2023, the CFPB finalized a rule to implement this requirement. The Trump administration's CFPB narrowed this rule in May 2026 by raising the reporting threshold for financial institutions to fall under the rule from 100 to 1,000 originations, and cutting the small-business definition from $5 million to $1 million in annual revenue. The Center for Responsible Lending estimates that the change in reporting threshold alone exempts roughly 90 percent of depository institutions from tracking these data. Congress can ensure the intent of this law is fulfilled by codifying into the law the 2023 CFPB rule.

# Conclusion

Americans are starting businesses at the highest rate on record, and they're doing so amid sweeping tariffs, rising health insurance premiums, and a credit market that leaves nearly half of applicants short of the capital they seek. At the same time, there are worrying signs that hiring among these businesses is slipping. That seeming conflict between an entrepreneurial boom and mounting obstacles to business ownership is a central challenge for policymakers. One option is to keep spending tens of billions of dollars per year on a tax deduction that sends two-thirds of its benefits to business owners earning more than $500,000 and flows overwhelmingly to firms with no employees at all—or those resources could be redirected toward small businesses that actually need them, by simplifying the tax code; rewarding job creators; expanding access to capital, investment, and AI tools; and expanding employee ownership of small businesses. CAP's agenda would ensure that the more than 36 million small businesses nationwide have the tools they need to succeed and that more Americans have the opportunity to pursue the American dream through entrepreneurship.

** Specifically, Cockx and Desiere (2024) find that "the elasticity of the probability to hire the first employee with respect to the labor cost is –2.39," which the authors apply to job creation statistics from the Census Bureau and wage data from the Bureau of Labor Statistics. Cahuc, Carcillo, and Le Barbanchon (2019) find an employment elasticity of -4 with respect to the change in labor cost.*

*** See $50,000 cost per job from the 2009 American Recovery and Reinvestment Act; $30,000 cost per job for the effect of direct government spending on hiring; $40,000 cost per job of general tax cuts for the bottom of the income spectrum; and $20,000–$50,000 cost per job for bonus depreciation for equipment. Cost-per-job figures are not adjusted for inflation between the study period and today.*

# Methodological appendix

## Tax policy proposals

### Standard Small-Business Deduction

In order to estimate how revenues would be affected by the Standard Small-Business Deduction (SSBD), CAP used Statistics of Income (SOI) data from the IRS for tax year 2022 (the most recent year which contained all the information needed to produce this estimate). CAP took the distribution of S-corps and sole proprietorships by business receipts, which includes the cost of goods sold and wages paid, as well as total deductions. Those amounts were adjusted downward in line with separate SOI reports on the amounts reported by these business types with net income (assuming only businesses with net income would take the SSBD). CAP then produced an average deductions figure post-cost of goods sold and wages, by size of business income. For segments of businesses likely to be under the income thresholds of the proposal, CAP assumed that the average deduction amount would increase to just under 65 percent overall, or by a nominal amount (5 percent) for parts of the distribution that were already above 65 percent in deductions, on average. The resulting amount was increased to 2026 dollars by the Congressional Budget Office's reported growth in net business income within the individual income tax from 2022 to 2026. Finally, the authors assumed a tax rate on the increased deductions of 14 percent, in line with the overall average rate on individual income and in light of the income restrictions in this proposal.

### Small-Employer Jumpstart Credit

In order to estimate the revenue effects of the Small-Employer Jumpstart Credit, CAP used the U.S. Census Bureau report "Business Dynamics Statistics: Firm Size: 1978-2023." This report gives information on the number of new employers by year and the number of workers hired by size and age of employer. CAP used an average of job creation by category of employer from the years 2023 and 2019. CAP assumed that small businesses pay workers in line with Bureau of Labor Statistics (BLS) survey data and that 77.8 percent of workers stay at the same employer for more than a year, per BLS data, which lowers average per-employee wages paid to $47,500. CAP modeled a decrease in the cost of wages of 7.65 percent, which

is a 5.66 percent decrease in the cost of a new employee, per BLS data that wages make up 74 percent of total compensation costs at small employers. The elasticity of becoming a new employer with respect to the change in compensation cost is -2.39, per Cockx and Desiere's 2024 study of a similar Belgian payroll tax cut. The authors use this elasticity to produce an estimate of how many businesses would be induced to become employers yearly by the incentive, as well as to estimate a partial number of new jobs created. Authors assume a 10 percent yearly death rate of businesses. For hires after the first employee, the authors used Cahuc, Carcillo, and Le Barbanchon (2019), who found an elasticity of employment of -4 with respect to the overall change in payroll costs induced by a payroll tax decrease. The authors applied this to the average change in payroll costs by new employer size and the number of jobs created by new and small employers yearly. Because overall hiring in 2025 was about 10 percent lower than hiring in 2019 and 2023, jobs numbers are all reduced by 10 percent from the Census data. Authors assume 95 percent takeup of this program. Cost amounts include both the cost of newly induced employment and the baseline costs for subsidizing all new jobs that are created already.

## Credit programs

To estimate the impact of the credit programs proposed in this report, the authors use a Federal Credit Reform Act (FCRA) basis, which appropriates the cost of lending based on the net present value of expected future cash flows over the life of the loan. In the Office of Management and Budget's Federal Credit Supplement, the subsidy rate for federal lending programs is broken into four key components: the default rate net of recoveries, (plus) interest rate subsidies, (minus) fees, (plus) any other subsidies. The authors follow this approach to estimate a subsidy rate for each program, then combine this with the funding amount to estimate the total amount of capital extended as a result of the subsidy (or vice versa, combining with the total amount of capital extended to estimate a funding level). The authors then combine this with information about the relationship between lending amounts and quantities of businesses reached to estimate the reach of these programs.

### A public option for working capital

The authors use a $450 million annual appropriation (based on the House's previous proposal of $4.5 billion over 10 years) and assume a subsidy rate of 7.7 percent. This corresponds to the charge-off rate of 7(a) loans under $150,000 that are not backed by collateral and are revolving from the 2010–2019 cohorts—a comparable pool for this program. The authors then model the program's subsidy as fully offsetting default risk, enabling revolving credit to be delivered at the cost of funds.

This is likely conservative, as it assumes no recovery rate for loans in default. Dividing $450 million by this subsidy rate yields total annual direct lending of more than $5.8 billion. The authors then assume an average loan amount of $85,000, meaning the program would reach nearly 69,000 businesses per year. This is a conservative assumption when benchmarked against the average size of 7(a) loans under $150,000 in fiscal year 2025, which is $75,037 (and would therefore support a larger number of loans).

### Main Street Advantage

The authors use baseline loan amounts measured from SBA 7(a) loan-level data, using fiscal year 2025 funded approvals and excluding canceled loans. This baseline comprises 49,754 loans under $500,000, totaling $8.48 billion in gross lending: 31,178 loans of $150,000 or less ($2.34 billion gross, $1.66 billion guaranteed), and 18,576 loans of $150,001 to $500,000 ($6.14 billion gross, $4.27 billion guaranteed). Note that both groups of loans have an average effective guarantee rate of approximately 70 percent.

The authors assume a 25 percent increase in lending in response to the change in generosity induced by this program. An increase of this size has precedent: Beginning in FY 2014, the SBA temporarily set both the upfront guaranty fee and the annual service fee to zero on 7(a) loans of $150,000 or less, similar to the fee relief that this proposal would make permanent. In FY 2014, the number of 7(a) loans of $150,000 or less rose 25 percent from a year prior, while larger 7(a) loans, which received no fee relief, were flat, rising 0.8 percent. Therefore, the authors estimate CAP's plan would support approximately 62,000 loans (12,400 beyond the current level), with total lending of $10.6 billion.

Two of the four components, the annual service fee and the interest rate buydown, are charged against balances outstanding rather than against originations, so the authors first estimate how long each dollar lent remains outstanding. The authors infer this from the FY 2027 Federal Credit Supplement, which reports 7(a) annual fees worth 2.04 percent of principal in net present value against a published annual rate of 0.55 percent, implying 3.7 outstanding years per dollar originated across the program. The authors then estimate each component as follows:

1. **Upfront guarantee fees forgone.** The SBA charges this fee on the guaranteed portion of the loan rather than the full amount, at 2 percent for loans of $150,000 or less and 3 percent for loans above. On the smaller band, the lender may retain up to one-quarter of the fee; the authors assume only three-quarters is federal revenue. Manufacturers, food supply chain businesses, and businesses in rural areas borrowing $700,000 or less already pay a 0 percent upfront fee,

so their share of dollars—17.3 percent and 15.8 percent in the two bands—is also excluded. Applying these rates to guaranteed dollars grown by the 25 percent volume response gives $26 million forgone on the smaller band and $135 million on the larger, yielding approximately $161 million forgone in total.

2. **Annual service fees forgone.** The SBA charges 0.55 percent annually on the outstanding guaranteed balance, which as noted above is equivalent to 2.04 percent in present value terms when accounting for average outstanding years per dollar. Multiplying guaranteed originations (grown by the volume response) by this amount yields an annual cost of approximately $151 million.
3. **Additional expected loss.** The authors multiply the approximate 20 percentage-point change in the guarantee rate (from 70 percent to 90 percent) by the lifetime charge-off rate of 7(a) loans up to $150,000, which is 6.4 percent in the FY 2010–2019 cohorts. To allow for less stringent screening at a higher level of guarantee, the authors conservatively multiply this factor by 1.15. This equals 1.5 percent of lending in that band (grown by the volume response), yielding an annual cost of approximately $43 million.
4. **Interest rate buydown.** This portion applies to the borrower's entire balance rather than only the guaranteed portion and is calculated on gross dollars lent. Using the steady-state outstanding years estimate of 3.7, the authors calculate a steady-state outstanding balance of approximately $39.3 billion. The buydown covers businesses in low- and moderate-income (LMI) communities and rural areas, as well as veteran-owned firms. In 2025, rural borrowers accounted for 9.5 percent of dollars in loans of $500,000 or less, measured by matching borrower ZIP codes in 7(a) data to U.S. Department of Agriculture Rural-Urban Commuting Area codes. Among the remaining 90.5 percent of dollars, the authors apply a 26.9 percent LMI share based on Federal Financial Institutions Examination Council tract income data from 2026. Lastly, among the remaining borrowers, the authors assume that 5.4 percent are veteran-owned, in line with the Annual Business Survey's national 2022 estimate. This yields a total covered share of approximately 37 percent. Note that this may be a modest overestimate, as veteran-owned firms are likely disproportionately represented in LMI and rural areas, thus slightly overestimating the program cost. Multiplying this by the predicted steady-state balance and the 2 percentage-point rate buydown yields an annual cost of approximately $294 million.

These four components total approximately $650 million annually, which, against the $10.6 billion in lending supported, implies a subsidy rate of 6.1 percent.

### State Small Business Credit Initiative

The authors estimate the impact of this program by scaling realized figures reported in the Treasury Department's A Summary of Participating Jurisdictions 2022 and 2023 Annual Reports. Over that period, jurisdictions expended approximately $750 million, supporting nearly 3,900 transactions with more than 3,600 small businesses and generating $3.2 billion in new financing of which $2.8 billion was private. The report estimates that these investments were expected to create or help retain more than 46,000 jobs—20,600 created and 25,500 retained. Scaling these figures to a $1 billion annual appropriation yields 5,200 transactions, 4,800 small businesses, $3.7 billion in private financing, and more than 61,000 jobs.

### Invest in America SBIC

The current SBIC program operates at a zero credit subsidy rate, with all its costs recovered through fees. The authors assume that this program would buy down the net present cost of debenture funding to investment vehicles by 2 percentage points. To calculate the cost of this, the authors use the 2027 Federal Credit Supplement, which reports that annual fees on SBIC debentures are worth 2.8 percent of principal in net present value. The SBA's annual charge for debentures in fiscal year 2026 was initially set to 0.344 percent per year. Dividing one by the other gives a present-value factor of 8.14, meaning that each 1 percentage point of annual cost is worth 8.14 percent of principal in present-value terms. At a 2 percentage-point subsidy, this yields a subsidy rate of 16.28 percent, and thus each $1 billion committed would support approximately $6.1 billion of below-market leverage.

To estimate investment capacity and businesses reached, the authors scale the SBA's reported results over fiscal years 2021 through 2024. According to the 2024 SBIC Program Overview Report, over those years, the SBA issued an average of $4 billion in debenture commitments annually, and debenture SBICs invested an average of $7.1 billion in 997 small businesses per year—$1.79 billion of investment and 252 businesses per $1 billion of leverage committed. Applied to $6.1 billion of leverage, this yields roughly $11 billion of annual investment capacity, reaching about 1,550 small businesses annually.

## AI technical assistance

The authors use the May 2025 median salary of $101,860 for management analysts (Standard Occupational Classification, or SOC, 13-1111), reported in the BLS Occupational Employment and Wage Statistics, to ground the estimate for AI advisers at the 63 lead SBDCs. The authors further assume that benefits add an additional

63 percent to labor costs, in line with the ratio for state and local government in the BLS Employer Costs for Employee Compensation series for March 2026. This yields a total investment of $10.5 million annually, leaving $4.5 million of the total $15 million appropriation for training materials and other shared resources that can be distributed across the network's more than 900 local service centers.

## Business-equity ownership

To estimate business-equity ownership and its contribution to family wealth, CAP analyzed the Federal Reserve Board's 2022 Survey of Consumer Finances (SCF) Summary Extract Public Data using SCF survey weights. CAP calculated the shares of families' aggregate nonfinancial assets represented by business equity and primary residences. CAP also estimated business-equity holding rates among families in the top 10 percent of the net-worth distribution and those between the 50th and 74.9th percentiles. Definitions of the asset categories are available in Appendix B of the Federal Reserve's 2022 SCF report, and construction of the Summary Extract variables is documented in the Federal Reserve's variable-construction program.

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