SECOND CHANCE LENDING FORUM

PROSPERITY NOW



Second Chance Lending

CRIMINAL HISTORY, CREDITWORTHINESS, AND ACCESS TO SMALL-BUSINESS CAPITAL

A Policy Brief on Entrepreneurship, Credit Risk, and the Barriers Facing Business Owners with a Criminal Record

Second Chance Lending

Criminal History, Creditworthiness, and Access to Small-Business Capital

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About This Report

This report was developed by Prosperity Now in collaboration with the Collateral Consequences Resource Center (CCRC), following the Second Chance Lending Forum the two organizations convened on September 1, 2026, in Washington, D.C. The Forum brought together nearly 60 leaders from financial institutions, government, research, and community organizations to examine the evidence and practical challenges surrounding lending to entrepreneurs with criminal records.

Federal Reserve Board Governor Michael S. Barr delivered public keynote remarks. The subsequent discussions were held under the Chatham House Rule to encourage candid dialogue. This report draws on those discussions without identifying participants or attributing statements to them. Its findings and recommendations reflect the authors' independent analysis and should not be interpreted as endorsement by Governor Barr, the Federal Reserve Board, or other Forum participants.

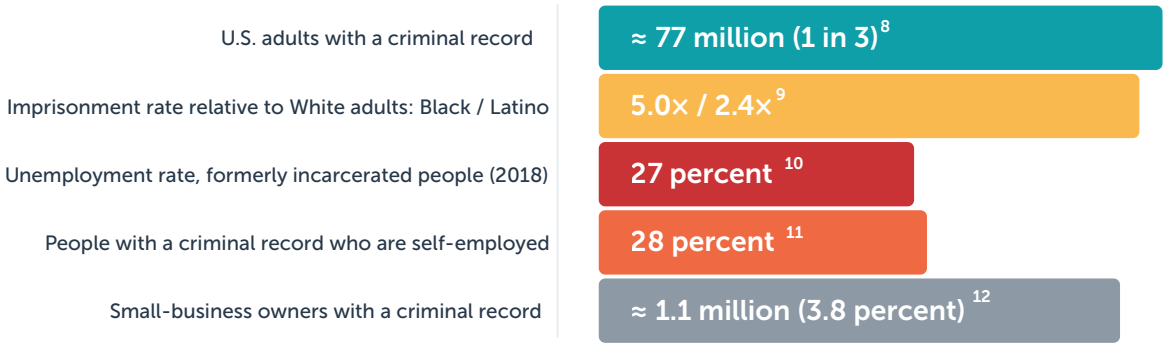
The report combines insights from the Forum with independent research, available lending data, and an examination of current policies and practices. We thank CCRC for its partnership in developing this work and the Forum participants for contributing their time, expertise, and perspectives.

Executive Summary

Many otherwise creditworthy entrepreneurs with criminal records face barriers to small-business financing rooted in screening practices, compliance uncertainty, and data gaps rather than validated evidence of repayment risk. The consequences of this exclusion are large. Roughly one in three American adults, about 77 million people, has some form of criminal record. Black and Latino adults are disproportionately affected by criminal justice involvement.[1] This paper uses the term "justice-involved" for this population because federal agency reports and research frequently use it as a descriptor. Nevertheless, this term is an imprecise description because the bulk of the intended population is not currently in the justice system, even though they continue to be affected by their prior involvement in it. People with criminal records face some of the steepest barriers in the labor market, with unemployment among a subset of this group, formerly-incarcerated people, estimated at 27 percent, a rate higher than the national rate during any period of the Great Depression.[2]

Because of obstacles to employment, people with criminal records are encouraged to turn to entrepreneurship to earn an income. Twenty-eight percent of individuals with criminal records are self-employed, and formerly incarcerated people are roughly 50 percent more likely to become entrepreneurs than people who have never been incarcerated.[3] Yet these entrepreneurs are about 19 percent less likely to obtain a loan for startup capital and about 21 percent less likely to obtain expansion financing than comparable owners without felony convictions.[4] Lenders often assume that a record signals elevated risk of default or reoffending. The available evidence does not establish that criminal history, by itself, reliably predicts repayment risk. The Small Business Administration (SBA) reported in 2024 "no evidence of a negative impact on repayment for qualified individuals with criminal history records."[5] Research suggests that expanding access to business capital for justice-involved owners can improve business outcomes and reduce subsequent criminal convictions.[6]

KEY FIGURES AT A GLANCE[7]



I. Introduction and Event Context

The Second Chance Lending Forum focused on a fundamental question during the convening: to what extent is criminal history being used, explicitly or implicitly, as a proxy for credit risk in small-business lending, and does the evidence support that practice?

This paper provides a summary of some of the takeaways and action steps recommended by participants at the Forum. It is written to support moving policy and practice from assumption to evidence, and from piecemeal conclusions toward a clearer action agenda. It draws on the research presented at the Forum, the introductory remarks of Federal Reserve Governor Michael S. Barr, government reports, and agency records obtained through the Freedom of Information Act. This paper recommends a coordinated agenda for improving access to small business capital to those with a criminal record which includes: building an evidentiary foundation through data collection; adopting individualized underwriting standards; resolving compliance uncertainty; and, above all, expanding the supply of training, capital, lines of credit, and technical assistance tailored to justice-involved entrepreneurs.

The paper proceeds as follows:

- Part II describes the size and racial composition of the population with criminal records and the barriers that population faces in the labor market;
- Part III explains why people with records are more likely than others to become entrepreneurs;
- Part IV describes the current lending landscape and the misperceptions about default, recidivism and reputational risk that lead lenders to deny credit;
- Part V reviews the evidence on repayment and recidivism;
- Part VI identifies where and why the system breaks down;
- Part VII examines the SBA's historical role in perpetuating exclusion and the limits of its recent reforms;
- Part VIII sets out what we know and what we still need to learn;
- Part IX presents a policy and action agenda; and
- Part X concludes.



II. Why This Matters: Scale, Demographics, and the Labor Market

Access to fair and affordable credit is foundational to entrepreneurship, business formation, and long-term wealth building. For many people with a criminal record, self-employment and small-business ownership are among the most viable paths to economic mobility, particularly when traditional employment remains constrained.[13] When lending decisions rely on unsupported assumptions rather than data, markets misprice risk, reinforce disparate outcomes, and foreclose productive enterprise. Therefore, the issue is to align the collective objectives of safety and soundness, fairness, and economic efficiency.

A. The Number of People with Criminal Records

The justice-involved population is enormous. In 2019, 2.1 million adults were held in U.S. jails or prisons and another 4.4 million were under community supervision; people are booked into jail more than 10 million times each year.[14] Almost 77 million adults, one in three, have a criminal record of some kind.[15] The Brennan Center estimates that 7.7 million living Americans have been imprisoned, another 12.1 million have felony convictions without imprisonment, and roughly 45 million have misdemeanor convictions.[16] All told, that equates to roughly 30 percent of the U.S. population, even without including the number of persons who have been arrested but were never charged or indicted.

A meaningful share of people who are justice-involved already owns businesses. RAND researchers, linking commercial business-ownership data to criminal history records, produced the first national estimate: approximately 1.1 million small-business owners, or 3.8 percent of all owners of firms with fewer than 500 employees, have a criminal record, and about 433,000 have a felony record.[17] Only 1.5 percent of

businesses have owners with felony convictions, compared with 8 percent of the adult population, a gap the researchers suggest may partly reflect the SBA's "long record of imposing restrictions on loans and other aid to small businesses owned by individuals with criminal history records."[18]

B. A Population That Is Disproportionately Black and Latino

Criminal convictions are unevenly experienced by U.S. racial and ethnic groups. Black adults are imprisoned at five times the rate of White adults, Latino adults at 2.4 times the rate, and Native American adults at 4.2 times the rate.[19] One in three Black men born in 1981 could expect to be imprisoned during his lifetime; for those born in 2001 the figure is one in five, an improvement that still leaves an extraordinary disparity.[20] As of 2010, an estimated 33 percent of Black adult men had a felony conviction, compared with 8 percent of all adults.[21] The Consumer Financial Protection Bureau (CFPB) observed that the financial consequences of justice involvement "fall most heavily on people of color, Black Americans in particular, and can continue long after a person is directly involved in the justice system."[22]

People with criminal records are disproportionately Black. An estimated eight percent of all U.S. adults have a felony conviction, compared with 33 percent of Black adult men.[23] By age 23, about 49 percent of Black men report having been arrested at least once, compared with 38 percent of White men.[24] Researchers caution that these figures reflect differences in punishment, not simply differences in behavior. Because arrest and incarceration rates differ substantially across racial and ethnic groups, criminal-history screening may disproportionately affect some communities. That is what happened under the Paycheck Protection Program (PPP), which was designed to provide funds to small businesses to aid in resilience in the aftermath of the COVID pandemic. RAND found that at least 24 percent of businesses excluded by the original PPP criminal-history rules were Black-owned, a share "that could be much higher if Black owners are overrepresented among owners with a missing racial status in the records."[25] Census researchers likewise concluded that the PPP exclusions had a disproportionate negative effect on Black and Latino business owners.[26] The CFPB has warned that, "given the stark racial disparities in arrests and convictions," lender use of criminal history "may raise serious fair lending concerns."[27]

C. The Difficulty of Reentering the Job Market

People returning from incarceration face some of the most severe employment barriers in the economy. The Prison Policy Initiative estimated in 2018 that formerly incarcerated people had an unemployment rate of 27 percent, nearly five times the rate for the general population, with even higher rates for formerly incarcerated Black women (43.6 percent) and Black men (35.2 percent).[28] At the Forum, Governor Barr emphasized the importance to the U.S. economy of financial inclusion for persons with a criminal record, particularly that this population have a fair chance to be employed or to start a business.[29] The Center for Economic and Policy Research estimated that employment losses associated with prior imprisonment or felony convictions reduced the number of employed Americans by 1.7 to 1.9 million in 2014, costing the United States an estimated $78 billion to $87 billion in annual economic output.[30]

Governor Barr noted that those who enter the criminal justice system suffer long-term economic consequences, including that the opportunity for employment propensity falls by roughly 7 to 26 percent after an initial criminal charge and "remains persistently low even six years later."[31] Incarceration further leads to lower employment and earnings; the Brennan Center estimates that imprisonment reduces annual earnings by 52 percent, a felony conviction without imprisonment by 22 percent, and a misdemeanor

conviction by 16 percent, for aggregate lost earnings of $372.3 billion each year.[32] White formerly imprisoned people see their earnings rise over time, while Black and Latino formerly imprisoned people experience a "relatively flat earnings trajectory."[33]

Employment-related discrimination is a central cause of this disparity. In a landmark 2003 study, White applicants without a record received callbacks 34 percent of the time and White applicants with a record 17 percent of the time; for Black applicants the rates were 14 percent without a record and 5 percent with a record.[34] Researchers in 2018 found similar results. Job applicants without records received 63 percent more callbacks than otherwise similar applicants with records.[35] Occupational licensing is another barrier to entry for job applicants: nearly one in five U.S. jobs requires a government license, and several states allow licensing boards to disqualify applicants regardless of whether the offense relates to the occupation.[36]

These obstacles to employment compound to substantially reduce economic opportunity. Federal Reserve survey data show that people with records report significantly lower financial well-being, reduced access to credit, and higher rates of being unbanked, gaps that persist after controlling for demographic and economic differences and widen with longer incarceration.[37] Notably, people who have been incarcerated are 16 percentage points less confident that they will be approved for credit, yet 10 percentage points *more* likely to have applied in the past year, which suggests that their exclusion reflects restricted supply rather than weak demand.[38]

III. Why People with Criminal Records Are More Likely to Become Entrepreneurs

The data consistently shows that people with criminal records start and run businesses at higher rates than the general population. Using Criminal Justice Administrative Records System (CJARS) data linked to Internal Revenue Service (IRS) tax records, researchers presenting at the Forum found that 28 percent of individuals with criminal records were self-employed and that justice-involved individuals were 22 percent more likely to rely solely on self-employment for their income.[39] Researchers using the National Longitudinal Survey of Youth 1997, found that formerly incarcerated people are significantly more likely to become entrepreneurs than people who have never been incarcerated; the CFPB, summarizing that research, reports that returning individuals are about 50 percent more likely to become entrepreneurs.[40] They also reported even higher rates for some groups, including an estimated 42 percent self-employment rate among Black women with criminal records, and a greater concentration of justice-involved owners in construction.[41] Governor Barr similarly noted that "roughly 20 to 30 percent of people with criminal records report being self-employed business owners."[42]

The research identifies several reasons for this pattern.

- **Entrepreneurship as a response to labor-market discrimination**. Researchers found that when employers were barred from asking about criminal history early in the hiring process, entry into entrepreneurship among formerly incarcerated people, especially Black individuals, declined, supporting the conclusion that discrimination in wage employment is an important driver of self-employment.[43] In other words, entrepreneurship among justice-involved people is born of necessity, not only preference.

- **Higher earnings**. Among formerly incarcerated individuals, those who started businesses earned an estimated 24 percent more annually than those in traditional employment.[44]

- **Autonomy and avoidance of screening**. Self-employment allows people to avoid employer background checks and to build a work history on their own terms. Research also points to autonomy, responsibility, social integration, and enhanced job skills as benefits.[45]

- **A bridge back to wage work**. Entrepreneurial experience shortens subsequent unemployment spells and improves later wage-employment outcomes, particularly for racial minorities and high-school dropouts, by building human capital, networks, and a positive signal for future employers.[46]

- **Community employment effects**. Businesses owned by people with records that have been in a training program during incarceration are more likely to hire others with records, extending the benefit beyond the original owner.[47]

If entrepreneurship is in significant part a response to blocked employment opportunities, then access to business capital is especially consequential for entrepreneurs with a prior criminal history. When capital is withheld from justice-involved entrepreneurs, the last viable path to economic self-sufficiency may be closed as well.

IV. The Current Lending Landscape

In principle, underwriting should distinguish between categorical exclusion and individualized assessment. In practice, justice-involved entrepreneurs encounter a system from which exclusion occurs early: sometimes at formal screening, sometimes through informal discretion, and sometimes through self-screening in anticipation of likely rejection. Many applicants never reach a meaningful evaluation of their actual business risk, repayment capacity, or broader financial profile.

A. Scale of the Problem

- Tens of millions of Americans have some form of criminal record.
- Direct data on credit denial rates by criminal history in small-business lending are limited or absent.
- Barriers appear at multiple points, including formal denial, undocumented discretion, and applicant self-selection out of the market.
- The resulting costs include suppressed business formation, lower household wealth, fewer jobs, and missed opportunities for economic participation.
- The absence of outcome data itself is a policy and market problem because it prevents evidence-based reform.

B. The Financing Gap

The most rigorous evidence confirms a substantial financing gap. Linking the Census Bureau's Survey of Business Owners to person-level criminal histories, researchers found that entrepreneurs with felony convictions are about 19 percent less likely to receive a loan for startup capital and about 21 percent less likely to receive a loan for expansion capital than similar owners without felony convictions.[48] Among businesses that had closed, owners with felony convictions were about 56 percent more likely to cite lack of access to capital as the reason.[49] Descriptive work by a researcher participating in the forum shows that

these constraints shape not only whether a business is started but also its legal form, size, industry, initial capitalization, longevity, and that formerly incarcerated founders rely disproportionately on personal and family resources.[50]
Business owners have described the problem more bluntly: "Banks won't even talk to us."[51]

C. Why Lenders Deny Credit: Perceived Risk of Default and Recidivism

Forum participants described how lenders that screen on criminal history typically rely on two assumptions: that a person with a record is more likely to default, and that the person is more likely to reoffend, jeopardizing the business, its collateral, and the lender's reputation. Neither assumption has been validated for small-business lending. The CFPB found "limited evidence to suggest that criminal history decreases creditworthiness," observing that government programs have imposed restrictions that "appear to be linked

Binary Screens

Many institutions treat a record as a yes-or-no variable, without regard to offense type, recency, relevance to the business, or evidence of rehabilitation. Criminological research shows that such screens are based upon skewed data and are inaccurate because risk varies dramatically with age, number of prior convictions, and time since the last offense.[53]

Credit scores that embed the consequences of incarceration

Incarceration itself causally reduces credit scores and access to mainstream credit.[54] A thin or damaged file may therefore reflect lost *opportunity* to demonstrate repayment rather than demonstrated poor repayment, and a lender that denies credit on that basis perpetuates the problem. As one researcher noted at the Forum, people with records often have lower FICO scores even though "they are doing everything right because they have not been able to participate in the formal financial system."

Reputational and regulatory caution

Participants at the Forum confirmed that lenders facing ambiguous "know your customer" expectations frequently default to exclusion as the lowest-risk posture. They default to not making the effort to do individualized assessments of credit risk because of overstated concerns about a potential mistake and the cost of complying with Bank Secrecy Act and Anti-Money Laundering requirements.

Signals from the federal government

For decades, the SBA's own eligibility rules treated criminal history as a disqualifying or suspect characteristic, and lenders used those standards as a proxy for acceptable underwriting well beyond the guaranteed-loan programs.



V. The Evidence on Repayment and Recidivism

The available evidence challenges the assumption that borrowers with criminal records are categorically poor credit risks. The strongest study to date used the PPP's criminal-history cutoff as a natural experiment. It found that loan eligibility improved business outcomes for owners with felony records and sharply reduced their likelihood of a new conviction. Direct evidence on how criminal history relates to conventional loan repayment, however, remains limited.

A. Repayment

The SBA's own finding. In adopting its 2024 reforms, the SBA stated: "SBA reviewed the relevant research and found no evidence of a negative impact on repayment for qualified individuals with criminal history records in any American business loan program."[55] That is a significant admission from the federal agency that for decades required extra scrutiny of these same borrowers.

The SBA's approval record. Data produced by the SBA to the CCRC in response to a Freedom of Information Act request show that, when applicants with felony convictions completed the character-determination process, the agency approved nearly all of them. Of the approximately 586 character-determination requests submitted annually in 2022 and 2023, the SBA declined only 17 to 23 per year, or 3 to 4 percent. Of 336 notices to lenders the SBA produced for November 2020 through December 2021, all but 12 approved the loan, an approval rate of 96.5 percent. The agency thus spent years guaranteeing loans to borrowers with felony records, which means performance data exist that could test repayment directly.

Evidence from employment. Studies of performance in analogous settings reinforce the point. In the U.S. military, enlistees admitted with felony-record waivers were no more likely than other enlistees to be discharged for negative reasons and were promoted more quickly and to higher ranks.[56]
Consumers report the same experience; as one formerly incarcerated person told the CFPB after a card

issuer closed his account on learning of his record, "Since I've been released from prison, my credit score has only risen."[57]

Program outcomes. Programs that pair capital with training show strong business results. Texas's Prison Entrepreneurship Program (PEP), which operates a community development financial institution (CDFI) lending subsidiary, reported that 57 percent of its graduates' businesses remained open, compared with 53 percent of all Texas businesses.[58] The SBA's own evaluation of its Microloan Program found that borrowers who received technical assistance and training reported larger growth and better survival than those without this assistance.[59]

B. Recidivism

PPP financing provides causal evidence of reduced reoffending. The most rigorous evidence comes from the PPP. Because the program's criminal-history rules turned on the precise timing of a felony conviction, researchers compared business owners just on either side of the eligibility cutoff. Eligibility increased receipt of PPP financing, improved business survival, revenue, and payroll, and substantially reduced subsequent criminal convictions.[60] In this specific PPP setting, the reduction in reoffending can be attributed to increased access to financing.

Entrepreneurship is associated with lower recidivism than wage work. Researchers found that entrepreneurship among formerly incarcerated people is associated with higher income and lower recidivism, with a larger decline in five-year reoffending than that associated with traditional employment.[61] PEP graduates had a three-year recidivism rate of 7 percent, compared with a 23 percent baseline for Texas men, although the populations are not directly comparable.[62]

Denying credit increases recidivism. Conversely, the reductions in credit availability that follow incarceration themselves increase recidivism.[63] Credit exclusion is thus not a neutral precaution; it can raise the very risk lenders seek to avoid.

Most people with records do not reoffend, and risk declines over time. Using multi-state administrative data spanning 1992–2021, researchers found that most people with criminal records do not reoffend and that recidivism risk declines substantially with time since conviction.[64] RAND's "reset" research shows that each additional year without a new conviction is positive information that should lower an individual's estimated risk, which makes fixed lookback periods crude and often inaccurate.[65]
As one researcher told the Forum, actual recidivism "is much less than the common perception of the general population," so banks can responsibly take this risk.

C. What the Evidence Does Not Yet Show

No published study yet answers the question most relevant to conventional lenders: whether and to what extent criminal-history information predicts delinquency, default, or charge-off *after* controlling for the credit, income, collateral, and business information lenders already hold. PPP loans were federally backed and largely forgivable, so their performance is not a clean test of commercial repayment risk. And because borrowers with records who do receive loans have survived multiple stages of selection, their repayment rates, even if favorable, would not alone establish that criminal history is unrelated to risk.[66] Participants at the Forum confirmed that most lenders have been excluding this population on the basis of an assumption no one has validated, while the best causal evidence shows that providing capital produces better business and public-safety outcomes. The burden should rest on those who would exclude, not on the excluded.

VI. Where and Why the System Breaks Down

The central breakdown in small-business underwriting is that criminal history enters the credit process in ways that are not transparently tied to demonstrable business risk.

A. Screening-Stage Exclusion

- Automatic or informal disqualification is built into application systems and underwriting checklists, often without explicit policy articulation.
- Most screening criteria are not calibrated to business risk: they do not distinguish by offense type, recency, relevance to the proposed business activity, or rehabilitation.
- Informal loan-officer discretion compounds formal screening and is rarely documented or auditable.

B. Underwriting Economics

- Individualized assessment of applicants with records imposes higher due-diligence costs that lenders cannot recover through pricing (because no data support it) or risk-sharing (because mechanisms are limited).
- The rational lender response is to exit the segment, not because the risk is too high but because the cost of proper assessment is too high relative to loan volume.

C. Anti-Money-Laundering and Bank Secrecy Act Compliance Friction

- Criminal records trigger heightened know-your-customer and customer-due-diligence scrutiny. Regulatory guidance on what is required, as opposed to what constitutes voluntary avoidance, is ambiguous.
- No clear safe harbor exists, so compliance officers default to exclusion as the lowest-risk posture.
- This is particularly consequential for banks and their CDFI partners, whose examination exposure makes regulatory uncertainty more costly.

D. Data Failures and Secondary Barriers

- There is no standardized disclosure of small-business lending by criminal history. Section 1071 of the Dodd-Frank Act may eventually provide application-level data for some financial institutions that make small-business loans, but the statute and its implementing rule do not require collection of criminal-history status. Under the CFPB's revised 2026 rule, covered lenders originating at least 1,000 covered transactions in each of 2026 and 2027 must begin collecting data on January 1, 2028, with initial reporting due June 1, 2029. Other institutions may have later compliance dates or fall outside the rule.[67]
- The data gap perpetuates conservative assumptions that persons with a criminal record are more likely to default, which in turn leads to continued exclusion and does not encourage small-business lenders to collect performance data that could challenge those assumptions.
- Secondary barriers compound the problem: credit-history gaps from incarceration, asset deprivation, collateral constraints, and state licensing restrictions that foreclose entrepreneurship before the credit question arises.[68]

E. How Different Parts of the Market Experience the Breakdown

- **Mainstream banks** employ standardized scoring, background-check requirements, and reputational-risk calculations that restrict lending to the justice-involved without any explicit exclusion policy.
- **Community banks and credit unions** have greater flexibility in theory, but thinner compliance capacity makes regulatory uncertainty more consequential, not less.
- **CDFIs and nonprofits** are the primary infrastructure for this population, by mission rather than market design, using character-based and relationship-based underwriting with integrated technical assistance; however, they are constrained by balance-sheet scale and cost-per-loan economics.
- **Fintechs** are theoretically advantaged by alternative data, but algorithms trained on historical exclusion may replicate bias, and fintechs have limited Community Reinvestment Act responsibility.

VII. The Small Business Administration: From Exclusion to Incomplete Reform

The SBA influences market norms far beyond its guaranteed-loan programs. Lenders use SBA eligibility standards as a proxy for acceptable underwriting, so the agency's treatment of criminal history has shaped lending practice throughout the small-business market. For decades, that influence pushed in the direction of exclusion.

A. How SBA Questions Perpetuated Discrimination

Until 2023, every applicant for an SBA 7(a) loan completed SBA Form 1919, which asked each owner of 20 percent or more (and certain other associates) whether they had been arrested in the past six months for any criminal offense and whether they had ever been convicted, pleaded guilty or nolo contendere, been placed on pretrial diversion, or been placed on parole or probation.[69] A "yes" answer required completion of SBA Form 912, the Statement of Personal History, and a detailed written narrative of each offense.[70] For felony convictions and certain other matters, the lender could not proceed on its own: it had to send the package, together with an FBI fingerprint check, to the SBA for a "character determination," and it could not disburse loan proceeds until the SBA issued written clearance.[71] Applicants who were on probation or parole were categorically ineligible.[72]

This process discriminated against people with records in three ways:

It deterred applications. The prospect of fingerprinting and FBI referral caused large numbers of applicants to abandon the process. According to information obtained by CCRC through a FOIA request, of the 907 applications with felony convictions referred to the FBI in 2020 and 2021, only 336 produced a decision notice, which suggests that roughly 63 percent withdrew; in 2023, 45 percent of the cohort withdrew.

It signaled that a record was a credit risk. Although the SBA approved more than 96 percent of the applicants who completed the application process in 2020 and 2021, it never publicly acknowledged this data. As one observer concluded during the Forum, the agency allowed people with a criminal history to believe they had little or no chance of getting approved for a guaranteed loan, when in fact they had very

good odds. Further, even when the SBA eventually eliminated questions related to criminal record from its own loan guaranty programs, in the commentary to those reforms the agency suggested to lenders that a criminal record was a credit risk to be guarded against through background checks.[73]

It excluded people during emergencies. In the spring of 2020, the SBA barred PPP relief to any business whose 20-percent owner was incarcerated, on probation or parole, subject to formal criminal charges, or had been convicted of any felony, placed on pretrial diversion, or placed on parole or probation within the past five years.[74] The rule initially disqualified an estimated 140,000 small-business owners, 212,000 businesses, and 343,000 employees.[75] A federal court found the application's criminal-history bar unlawful, and the rules were narrowed in 2020 and again in 2021, reducing the number of affected businesses by 95 percent.[76] The COVID-19 Economic Injury Disaster Loan program imposed similar restrictions.[77]

B. The 2023–2024 Reforms

In May 2023, the SBA revised its 7(a) standard operating procedures to eliminate the requirement that lenders refer applicants with felony convictions for a character determination.[78] In September 2023, it proposed to end most criminal-history inquiries in its business-loan programs, and on April 30, 2024, it finalized the rule, effective May 30, 2024.[79] The final rule replaced the three criminal-history questions on its application forms with a single question about current incarceration or indictment.[80] Under the amended regulation, a business is ineligible only if an associate "is currently incarcerated, serving a sentence of imprisonment imposed upon adjudication of guilty, or is under indictment for a felony or any crime involving or relating to financial misconduct or a false statement."[81] The rule also lifted the automatic bar on applicants who are on parole or probation, and the SBA cited research on the prevalence and viability of entrepreneurship among people with records as part of its justification.[82]

C. What Reform Did Not Accomplish

These reforms meaningfully expanded formal eligibility and signaled institutional intent. But the SBA stopped short of the steps needed to change lender behavior.

It expressly preserved lender screening. The final rule states: "Some lenders include conducting criminal history background checks and others do not. SBA's final rule revision does not impact a [l]ender's… authority or ability to continue to do so…."[83] Having found no evidence that criminal history harms repayment, the agency nonetheless left lenders free to use it as a screen in SBA-guaranteed lending.

It deferred guidance. The SBA acknowledged that "enforcement goes beyond the scope of this regulatory rulemaking" and promised to "provide future guidance on compliance in Standard Operating Procedures and training by specific programs."[84] Industry advisers told lenders simply to update their loan policies and to delete obsolete Form 912 procedures.[85] The SBA has since updated its Standard Operating Procedures, including SOP 50 10 8.1, effective October 1, 2026. However, the provisions addressing criminal history focus on eligibility and certain lender requirements rather than providing a comprehensive framework for evaluating otherwise eligible applicants with prior criminal records.[86] To the authors' knowledge, the SBA has not issued comprehensive guidance explaining how lenders should evaluate applicants with records, has not conducted lender training commensurate with the scale of the change, and has not engaged in outreach to tell justice-involved entrepreneurs that the rules have changed.

It collected no outcome data. No systematic collection of application, approval, and performance data by criminal-history status accompanied the reform, so the SBA cannot measure the reform's effect or share the repayment evidence that its own historical portfolio contains.

The result is that lender practice remains highly variable. The SBA is uniquely positioned to require outcome tracking, publish anonymized performance data, and set standards the market can adopt; it has not yet exercised that capacity.

VIII. What We Know and What We Need to Learn

Many participants in the Forum discussed how the exclusion of justice-involved borrowers is shaped by institutional practice and missing data rather than proven credit risk. This distortion in the market can be reduced or even eliminated with the following steps:

- Banks and credit unions have opportunities to revisit current practice and identify where screening or process barriers are broader than actual risk warrants.

- CDFI and nonprofit approaches show that criminal history can be treated as one factor among many within a holistic underwriting framework. Forum participants emphasized the importance of looking at "the entire human being" and at sustainability, affordability, and stability.

- Bank–CDFI partnerships may offer a pathway to scale, but compliance review and standardization remain significant barriers.

- Alternative data and cash-flow underwriting may help supplement thin credit files, but these tools require careful validation to avoid reproducing existing bias.[87]

The data is available to study constructive ways to better serve this population. Researchers would compare predictive models, one using ordinary underwriting variables, a second adding detailed criminal history, and a third adding post-record behavior, to measure how much, if at all, criminal history improves out-of-sample prediction of loan performance, and whether any predictive value fades with offense-free time. The necessary data exist in pieces: the SBA's historical character-determination files and loan-performance records, private lenders' internal data, credit-bureau files, and the CJARS/Census infrastructure used by researchers who presented at the Forum to analyze the experience and performance of small business owners with a criminal record. As the Forum's research panel concluded, the evidence gap may be less a problem of methodology than a problem of data access.

IX. Policy and Action Agenda

If the current system produces exclusion without sufficient evidence, the response should be to build better evidence, clarify expectations, and, most urgently, scale the capital and support that justice-involved entrepreneurs need. In his comments, Governor Barr observed that the difference between a good idea and a lasting business often comes down to three essentials: access to credit, access to business networks, and access to missing skills or technical assistance.[88] Each is in short supply for entrepreneurs with criminal records.

A. Build the Evidentiary Foundation

The following steps would allow researchers, the private sector and the government to better understand small business lending to persons with a criminal record:

- Researchers and lenders should explore opportunities to use small-business lending data, including data collected under Section 1071 of the Dodd-Frank Act where available, to better understand barriers to credit. Carefully designed research partnerships could examine lending outcomes by criminal-history status while protecting applicants' privacy and complying with applicable law.

- The SBA should analyze and publish, in anonymized form, the repayment performance of loans made to borrowers who went through the character-determination process, tracking the full funnel from application to repayment (see Section V(A) above).

- Small business lenders, credit bureaus, the SBA, and the Census Bureau should promote data research partnerships to link criminal-history and loan-performance data under appropriate confidentiality protections.

B. Reform Underwriting Standards

The following reforms would promote fair access to credit for all small business owners:

- Small business lenders should develop a model individualized-assessment framework, considering offense type, recency, nexus to the business, and rehabilitation for SBA adoption and voluntary lender use.

- Small business lenders should give weight to positive, current information, including offense-free time, business performance, and cash flow, rather than dated negative information.

C. Resolve Compliance Uncertainty

The following actions by federal regulators would promote both safe and fair lending to persons with a criminal record:

- FinCEN and the federal banking regulators should jointly clarify know-your-customer and customer-due-diligence expectations for justice-involved applicants and establish a safe harbor for documented individualized assessment.[89]

- Federal financial regulators should encourage lenders to review categorical criminal-history screening policies, assess whether those policies are supported by evidence of repayment or other legitimate financial risks, and document the basis for their lending decisions. Regulators should also clarify applicable fair-lending obligations and encourage consistent, individualized assessment.

D. SBA Guidance for Lenders and Entrepreneur Support Organizations (ESOs)

The SBA leadership could take the following actions to build upon its previous reforms:

Issue the lender guidance and training the SBA promised in 2024, making clear that criminal history, other than current incarceration or indictment, is not a proxy for creditworthiness in SBA programs.[90]

Pair eligibility reform with mandatory outcome-data collection and use loan guarantees as an active market-entry tool for lenders serving this population.

Conduct outreach through Small Business Development Centers (SBDCs), Women's Business Centers (WBCs), SCORE chapters, reentry organizations, and other ESOs so that entrepreneurs with records know they are eligible.

E. Expand Capital and Lines of Credit

Capital must be available in forms suited to the businesses that justice-involved entrepreneurs actually start, which are frequently small, service-based, and concentrated in industries such as construction and transportation. The following actions by the federal government and financial institutions would expand access to credit for small businesses, including those owned by persons with a criminal record:

- Expand CDFI Fund capitalization for CDFIs with documented reentry-lending records, including grants to offset above-average underwriting costs.

- Create dedicated loan-loss reserves and credit-enhancement pools, whether public, philanthropic, or bank-funded, that allow lenders to extend credit while the performance record is built. Make working-capital lines of credit, not only term loans, available to justice-involved borrowers. Revolving credit builds the credit history that incarceration interrupted and is essential for businesses with lumpy receivables, such as construction contractors.

- Support microloans and credit-builder products at the entry level, followed by graduated access to larger SBA 7(a) and 504 financing.

- Encourage banks to meet Community Reinvestment Act obligations through investments in, and partnerships with, lenders engaged in second-chance lending.

F. Invest in Training and Technical Assistance

Lending is most effective when paired with the training and networks that help a business succeed.[91] The SBA's own evaluation found that microloan borrowers who received technical assistance reported larger growth and better survival, and the PEP model demonstrates the power of combining training with capital.[92] The following steps would make the transition to the work force easier for persons with a criminal record, including those still incarcerated:

- **Begin before release**. Financial readiness should start as soon as people enter prison: opening bank accounts, obtaining identification, freezing credit files to prevent identity theft, and building a financial profile that lenders can evaluate on release.

- **Fund entrepreneurship training** that covers business planning, financial projections, bookkeeping, pricing, and loan packaging, with long-term evaluation to identify scalable practices.[93]

- **Provide wraparound support**. Transportation, childcare, and financial literacy contribute to the stability on which business success depends.

- **Connect entrepreneurs to networks**. Small Business Development Centers (SBDCs), chambers of commerce, and mentor networks provide the referrals, vendor relationships, and informal credit references that entrepreneurs with records often lack.[94]

- **Harness technology responsibly.** Cash-flow underwriting, financial coaching, and AI-assisted business planning tools may lower the cost of serving this market, provided they are validated for accuracy and fairness.[95]

G. Address Licensing Barriers

As described in Section II(C), many states impose licensing restrictions or even exclude persons with criminal records from obtaining a business license or being employed in numerous trades and professions. Licensing restrictions at the state and, in some cases, federal levels create an additional obstacle to reentry. Given these restrictions, reducing and eliminating licensing burdens where appropriate may lower recidivism and improve employment outcomes.[96]



X. Conclusion

The exclusion of justice-involved entrepreneurs from small-business credit reflects a system-design problem, particularly where criminal-history screens are not tied to demonstrated credit risk. Tens of millions of Americans carry criminal records that close doors in the labor market. Many respond by starting businesses, only to find that lenders, following decades of federal signals, treat their records as evidence of default and recidivism risk that the data does not support. The SBA's own records show that it approved nearly every applicant with a felony record who persisted through its process, and the best causal research shows that providing capital improves business outcomes and reduces reoffending.

The SBA's narrowing of its criminal-history questions in its loan guaranty programs was an important step, but eligibility alone has not changed market behavior. Without guidance, training, data, and dedicated investment in capital and technical assistance, the eligibility change made by the SBA risks being a change on paper alone. The purpose of the Forum, and of this companion policy brief, is to make these barriers more visible, more measurable, and more actionable. With stronger evidence, clearer regulatory expectations, and deliberate investment in training, capital, lines of credit, and technical assistance, the market can move toward a more accurate and equitable approach to justice-involved entrepreneurs, to the benefit of the entrepreneurs, their families, their employees, the communities they serve and the overall U.S. economy.

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