



# Startups ≠ Small Businesses: A Policy Blueprint for Texas to Unlock High-Growth Capital

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## Executive Summary

Texas' economic strategy to attract innovative startups is undermined by a conceptual error: **failing to distinguish between small businesses and startups**. As state & local lawmakers and agencies pursue job creation, capital attraction, and innovation, they are using tools built for legacy industries, not the innovation economy. **A startup is not a small business**, and Texas must recognize this in statute, policy, and practice, or risk stagnating its leadership in technology and growth.

This white paper outlines a roadmap for structural reform:

1. Defining startups in Texas law,
2. Creating a dedicated Office of Startups and Innovation, and
3. Aligning tax, workforce, and capital policy to accelerate innovation, not bureaucracy.

## WHY LANGUAGE MATTERS IN LAW AND POLICY

The most cited and academically supported definition of a startup comes from Steve Blank: “*a temporary organization in search of a repeatable and scalable business model.*” This is not a branding issue, it’s a functional one. In contrast, a small business is typically an established operation with a known business model, serving a local or regional market, and optimizing for stable cash flow and profitability.

Blank’s distinction is not just academic, it is functional. Startups operate with fundamentally different risk profiles, growth trajectories, capital needs, and economic impacts than small businesses. They disrupt industries, scale exponentially, and typically aim for acquisition or IPO. Small businesses, on the other hand, are the backbone of local economies – think restaurants, dry cleaners, construction firms – often family-owned, steady, and embedded in their communities. A clear distinction is found in the notion of being temporary; that, while a startup venture is established as a legally operating entity, the stage of work is the determination of a viable company (where as a small business is the establishment of a known-to-be viable company).

Failing to distinguish these two enterprise types leads to flawed public policy: one-size-fits-all incentives, misaligned funding, and economic development strategies that miss their intended mark.

Here is a table that can help policymakers and agencies understand the critical differences between small businesses and startups.

Characteristic	Small Business	Startup
Business Model	Known and proven	Searching and unproven
Risk Profile	Moderate to low	High
Growth Objective	Sustain cash flow	Scale rapidly
Funding Sources	Bank loans, SBA	Angel, VC, SBIR/SBIC

Characteristic	Small Business	Startup
Revenue Model	Profit from day one	Delayed, scalable later
Market Scope	Local or regional	National/global
Duration of Uncertainty	Short	Extended
Exit Strategy	Operate indefinitely	IPO, acquisition
Policy Needs	Access to credit, tax breaks	R&D grants, equity capital

Policy, funding, and workforce programs that fail to distinguish between these two types of enterprise harm both in the long run.

## ECONOMIC IMPACT: STARTUPS DRIVE INNOVATION AND GROWTH

According to research from the Kauffman Foundation<sup>ii</sup> and the Brookings Institution<sup>iii</sup>, **high-growth startups are responsible for a disproportionate share of net new job creation.** Economist John Haltiwanger, in work published through the National Bureau of Economic Research, has repeatedly demonstrated that it is young firms – not necessarily “small” ones – that drive employment growth.<sup>iv</sup>

Further, startups are uniquely positioned to commercialize university research, deploy frontier technologies, and rapidly adapt to changing market conditions. The impact of companies like Moderna, which spun out of MIT and scaled in response to global health crises, or OpenAI, born of private capital but disruptive to entire labor markets, is not analogous to the impact of a local service business; no matter how critical the latter may be to community vibrancy.

Startups operate more like scientific experiments than commercial ventures, a framing that helps public institutions understand that risk tolerance, capital formation, and market readiness must be viewed through a different lens than traditional entrepreneurship or small business ownership.

## TEXAS ECONOMIC DEVELOPMENT MISALIGNMENT

The SBA-style model still drives most of Texas' state and municipal programs—despite their federal origins and 70-year-old design. Agencies like the Texas Economic Development & Tourism Office (EDT), the Texas Workforce Commission (TWC), and regional Development Corporations rarely distinguish startup activity from broader business creation. Why is this an issue? Take it from the SBA themselves:

*“SBA does not provide grants for starting and expanding a business.”<sup>v</sup>*

Programs such as the Jobs, Energy, Technology, and Innovation (JETI) incentives, while a start, cannot typically be utilized or deployed for startup-oriented outcomes due to the focus being on 10-year tax abatements on school district maintenance and operations (M&O) taxes. This is because most startups do not start with a brick-and-mortar operations, lease their office space, or utilize coworking spaces.<sup>vi,vii</sup> The Chapter 312/313 incentives are industrial-era tax breaks — ineffective for early-stage digital or life sciences companies — and lawmakers should expand the program to incorporate startups instead of only brick-and-mortar business.

## RECOMMENDATIONS FOR POLICY MAKERS

The **State of Texas**, and specifically **Austin**, has an opportunity to differentiate itself from **Silicon Valley** (CA) and **New York City** (NY) by creating intentional policy to attract and retain startups

### 1. Legislate Startup Definitions

By utilizing the following criteria, Texas would prove that it recognizes the fundamental difference between a small business and startup. Lawmakers should consider defining startups as:

- Age of >7 years
- “Temporary” business model that may or may not be competitive/sustainable

- Business is in the product or market discovery phase
- Not yet profitable or reliant as a % on investment capital

### 2. Establish the Office of Startups and Innovation

The Governor already has an office of “Economic Development and Tourism” which has at least 12<sup>viii</sup> incentive programs. Expanding to include a sub-office for Startups and Innovation would:

- Manage startup sector grant and equity programs
- Aggregate regional ecosystem data
- Align with university incubators and local venture programs

Additionally this role could create regional innovation officers who:

- Manage regional venture hubs
- Channel SBIR/STTR applicants through Texas Incubators
- Work with the TWC to reform workforce training for innovation roles

### 3. Modernize Franchise Tax Policy

Introduce a revenue-neutral sliding scale on the franchise tax, incorporating pre-revenue and VC-backed startup exemptions, while applying higher progressive tiers to mature, revenue-generating companies.

### 4. Distinguish and Support Capital Resource

Texas continues to treat all capital resources as if they are the same. Policymakers must recognize that:

- Angel Investors are distinct from Business Investors
- Venture Capital must have education and programming
- Guidance in fiscal policy that understands investor considerations

## THE STRATEGIC OPPORTUNITY FOR TEXAS

If we separate startup support from small business support, Texas can lead nationally in innovation governance. Notice with great import

that what is considered here is not “tech” — **tech is a misleading and inaccurate distinction of startups** in that startups are any innovative new business model distinct from the launch of a new business similar to what already exists. If Texas takes heed and adapts accordingly, it can:

- Unlock new taxable revenue from venture-scale outcomes
- Improve capital efficiency in economic development
- Equip Texas to lead in quantum, AI, space, biotech, energy, and defense tech

Without such clarity, Texas’ booming startup culture suffers under our own bureaucracy.

**Let’s not be the state that confused the engine of tomorrow with the storefronts of yesterday.**

## References and Endnotes

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- <sup>v</sup> *Grants*. (n.d.). U.S. Small Business Administration. <https://www.sba.gov/funding-programs/grants>
- <sup>vi</sup> Texas Comptroller of Public Accounts. (n.d.). *Jobs, Energy, Technology and Innovation Act (JETI)*. <https://comptroller.texas.gov/economy/development/prop-tax/jeti/>
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- <sup>viii</sup> *Incentive & financial programs*. (n.d.). <https://gov.texas.gov/business/page/incentives>