

2ndWind - Inclusive Ownership Transition for SMBs

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70 million people are between the ages 51 and 70 in the US, and own 2.34 million Small and Medium Businesses (SMBs) in the country, employing more than 25 million people^[1]. Small businesses are the backbone of the American economy and have generated 64% of new jobs annually in the US^[2]. Unfortunately, up to 70% of current owners will not be able to sell their businesses when they are ready^[3]. The large number of retiring owners, coupled with the uncertainty of successful exits, poses a threat to millions of jobs, and jeopardizes the owners' safety net for a comfortable retirement. Our Big Idea, 2ndWind, is a platform that introduces an easier and more inclusive ownership transition process for SMBs, facilitating sales for owners, pooling historically underserved buyers, and safeguarding a sustainable workforce by preventing SMBs from shutting down. Through fractional ownership, 2ndWind allows non-accredited investors^[4] to invest and co-own cash-flow-positive SMBs from retiring owners.

1. Problem Statement

“So, when are you coming back home to run our business? “The burden is now on you; we can’t do this forever.” These conversations always come up when one of our team members, Guan-Lun, talks with his parents. And he’s just one of the millions in this situation: a report estimated that 8 million privately owned businesses in the US will struggle for their existence, and \$10 trillion in business assets will be transferred by 2025^[5]. A 2021 study conducted by PwC indicates that only 30% of these businesses have succession plans^[6]. Additionally, research conducted by Wells Fargo in 2022 has shown that only 33% of family businesses are successfully passed down to the next generation.^[7]

Meanwhile, traditionally underserved groups struggle to enter the SMB market. Khanh’s family friends Sukhraj and Raj Kaur arrived in America from India at 32 to chase the American dream, hoping to build a better future for their children. Faced with language barriers, racial discrimination, and being discredited of their education and work experience in India, Sukhraj and Raj worked tirelessly at multiple blue-collar jobs - 12 hours a day and 7 days a week - while studying English in their free time. They slowly saved enough money to acquire a small grocery store business eight years later and supported their family of four in Stockton, CA.

Financially disadvantaged groups and non-accredited investors, including foreign workers, first-generation immigrants, and veterans, are excluded from this private investment market. Despite being 30% more likely than non-immigrants to acquire small business operations, first-generation immigrants often lack financial support from federal programs and financial institutions, having to rely on personally pooled funds from savings, friends, and family^[8,9]. In addition, despite being 45% more likely to operate and own small businesses than the average American^[10,11], veterans have cited a lack of initial capital as their biggest barrier, with another 46% stating challenges in understanding and efficiently utilizing community resources designed to help them^[10,11]. Acquiring SMBs from retiring owners could be a compelling way for these groups to achieve business ownership. However, non-accredited investors who lack financial stability and support from formal loan programs often struggle to pool sufficient capital to acquire these SMBs.

2. Existing Solutions

1. **SMB Marketplace: BizBuySell** - This is currently the go-to marketplace for brick-and-mortar businesses. The platform claims to have successfully sold over 100k businesses so far. The platform's two user personas are brokers and interested buyers; thus, it functions like an online directory of businesses that are up for sale and is primarily used as a “discovery” tool for buyers to connect with brokers. BizBuySell has only digitized the discovery stage, however, the actual evaluation of the company, Letter of Intent, NDA, contract, and final sign offs happen offline, usually facilitated by brokers who charge a 10%-15% fee to sellers. The high broker fee and requirement of proof of sufficient funding continue to reinforce existing high-capital barriers to entering the SMB market.
2. **No-broker Marketplace: Tupelo** - Albeit at a Seed stage, Tupelo has automated the entire process of SMBs’ acquisitions, targeting direct buyers and sellers. Tupelo helps eliminate the brokerage fee; however, high capital barrier to entry remains an issue for the SMB market.
3. **Transition SMB ownership to employees: Teamshares** - Teamshares is one of our closest competitors. They focus on getting businesses to be employee owned by gradually selling shares to them and letting the owner retire within 5-10 years. However, Teamshares mainly serves businesses with 10-15 employees, while 78.5% of American businesses have fewer than 10 employees^[12] and are consequently getting excluded. While Teamshares enables employees to buy into the businesses, they do not enable the broader financially disadvantaged communities to participate.

Current solutions in the SMB ownership transition space target traditional buyers and sellers in the SMB market, often relatively wealthy individuals with sufficient capital and loan support to fully acquire rather than partially acquire businesses. Existing companies have not provided sufficient tools to bring non-traditional, financially disadvantaged populations into the space. Populations that lack sufficient capital and partnership networks and are marginalized in the labor market are often unable to seek opportunities in the SMB market.

With 2ndWind, we aim to democratize SMB ownership and make it accessible to non-accredited and financially disadvantaged groups. We do this by streamlining fractional ownership - from creating co-owner agreements to eliminating liability for co-owner default - to make investments in SMBs accessible, enabling non-accredited investors to build credit and develop a new income stream. In addition, with a more efficient SMB marketplace and transition, we support the continued creation of job opportunities and prevent layoffs associated with SMB closures.

3. Proposed Innovations

2ndWind is a multi-faceted solution that will 1) ease the hardship of retirees by facilitating the sale of their business either wholly or in part, 2) help SMB employees gain ownership in their companies, and 3) enable financially disadvantaged groups and non-accredited investors to co-own the remainder of the company, completing the transition of SMB ownership. With a lower investment requirement than other marketplaces, 2ndWind’s initial target co-owners are current employees of the business and people who tend to have less intergenerational wealth, such as foreign-born workers, first-generation citizens, and veterans. As a marketplace, 2ndWind serves two major stakeholders: sellers and co-owners (buyers), and we break down the business into three sections:

1. **Sellers:** To identify potential sellers, 2ndWind applies supervised machine learning to source and value businesses. By aggregating businesses listings from SMB marketplaces (e.g. BizBuySell, Craigslist) with data such as categories and customer ratings from Google Maps, neighborhood population from the Census Bureau, historical traffic data from Korem or TomTom, and years in operation, 2ndWind can identify and contact top-notch local businesses pending sale and mitigate the “cold start” problem when introducing buyers to the platform. After receiving the tax return document from sellers, we will value these businesses with Relative (market prices) and FCF (Free Cash Flow) valuation models. The ideal seller persona will be a cash flow-positive business that has been owned and operated for over a decade, and the main reason for selling is retirement.
2. **Co-owners:** Current SMB employees will have the opportunity to buy shares from their employers. 2ndWind also provides the option of partial ownership for retiring owners, giving them the flexibility to liquidate a portion of their businesses. The remaining equity will be up for sale to verified buyers on our platform. Partial ownership also allows investors to monitor operations before committing a more considerable amount of their investment.
3. **Platform:** Once 2ndWind finishes due diligence for the business, with assistance from highly automated due diligence tools such as SignalX and ComplyAdvantage, and receives the signed Letter of Engagement from current owners, the platform will create a Limited Liability Corporation (LLC) as Special Purpose Vehicle (SPV)^[13] that pools investors’ commitments and then acquires the designated business on their behalf. To lower the down payment for co-owners, 2ndWind will also act as a guarantor to leverage SBA (Small Business Association) loans^[14] for each business we seek to acquire. This will be made possible with the help of private equity firms or other institutional investors that will back 2ndWind. For example, if an SBA lender approves an 80% loan, then the immediate out-of-pocket payment for co-owners will be the remaining 20%. Furthermore, by pooling a group of borrowers, 2ndWind can help reduce default risk^[15]. At the beginning of every acquisition contract, every co-owner will negotiate and agree to detailed operation terms and exit strategy.

Our Go-To-Market (GTM) strategy for target buyers is designed to be sensitive to the underserved communities’ increased experience with discrimination and decreased trust in institutions and authorities^[16]. Our field research found that the immigrant population, for example, tends to mostly rely on word-of-mouth and recommendations from trusted members of their communities; thus, engaging key opinion leaders from local community advocacy groups, who have been traditionally providing resource support to these underserved communities, will help us reach these financially disadvantaged populations. We also aim to leverage ethnic grocery store chains and non-English language radio stations for marketing. In addition, we will build partnerships with veteran service organizations, aiming to offer veterans a different path after discharge. To reach a wider population, we will make informative posts in different communities on social media (e.g. Reddit, Whatsapp). For example, “Acquiring A Small Business 101” in r/ small businesses, or “What Is Entrepreneurship Through Acquisition (ETA)” in r/ entrepreneurship to increase our brand awareness through different Subreddits.

4. Team Bios

Guan-Lun Liao started brainstorming the idea during the Summer of 2022 while he was interning at a Fintech venture capital firm and connected with Gurpreet Kaur Khalsa and Khanh Thai through the Berkeley Entrepreneurship network. Together, as a diverse team of three with international backgrounds, they have conducted initial customer discovery through the Startup Disco course led by Rhonda Shrader.

Gurpreet Kaur Khalsa: Gurpreet is a second-year student at the Berkeley School of Information. She is a Software Developer turned Product Manager. Her research interests include Responsible Machine Learning, Privacy, and Trust and Safety in consumer products. She is actively working on creating tools that can help Machine Learning practitioners create fairer algorithms, limiting harm toward marginalized communities in the healthcare space.

Khanh Thai: Khanh is a first-year Berkeley MPH student with experience in project management, regulatory compliance, market research, and operational strategies for healthcare research and start-up firms. She has experience working with underserved populations and designing culturally sensitive and equitable interventions to target social equity challenges for marginalized communities.

Guan-Lun Liao: Guan-Lun is a second-year Berkeley-Haas MBA student with experience in project management, business development, financial modeling, and data analytics at corporates, startups, and venture capital firms. Prior to Haas, he was an entrepreneur, scaled an early-stage smart aquaculture business from a team of 4 to 45, and raised \$2.2 million in capital.

6. References:

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