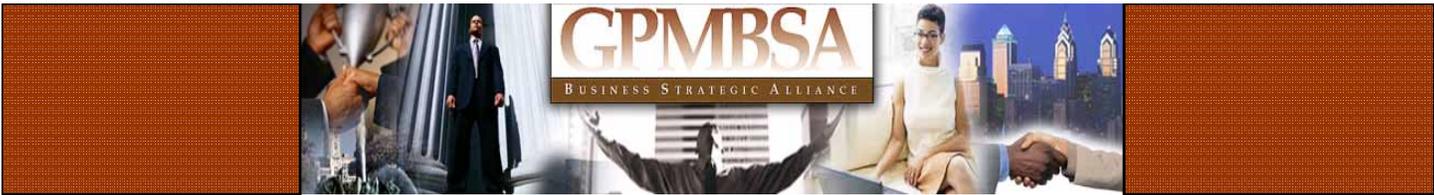


Succession Planning for Minority-Owned Enterprises:



The Need to Prepare the Next Generation of Minority Business Owners

April 2006



SUPPORTERS



Philadelphia Industrial Development Corporation



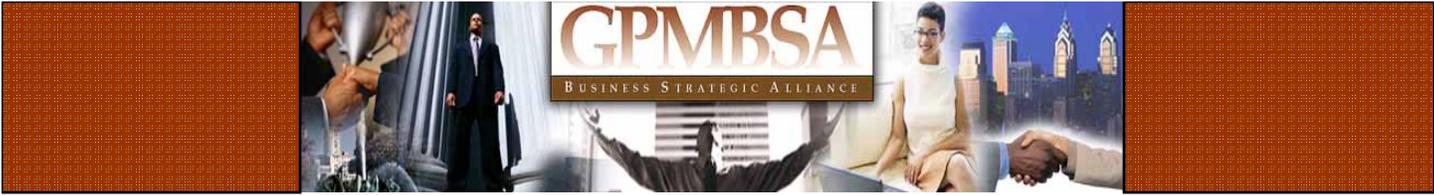
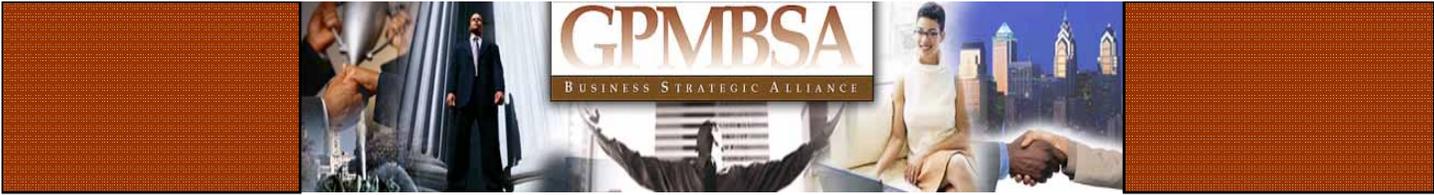


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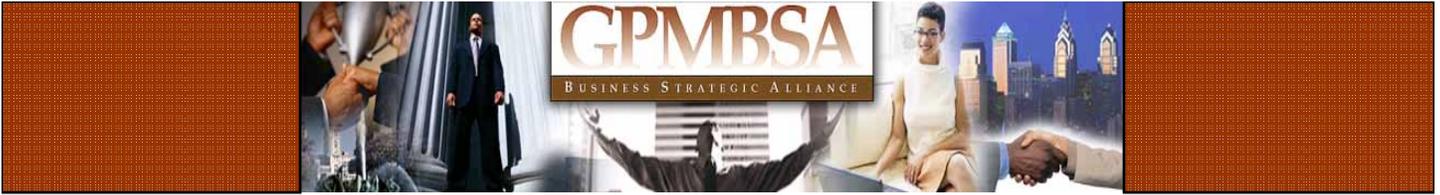


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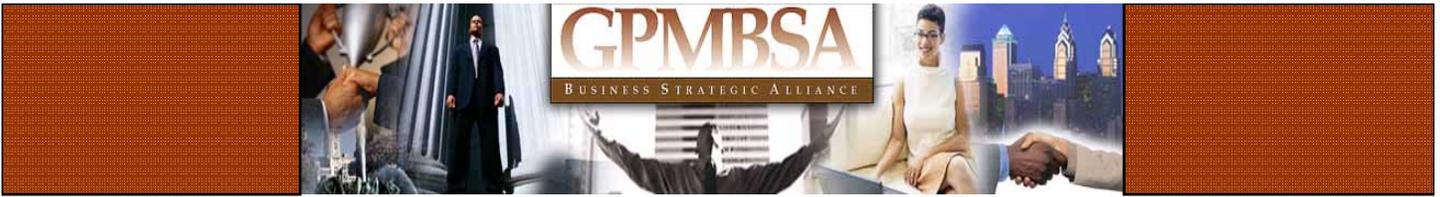
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- Women’s Business Development Center



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INDIVIDUAL CONTRIBUTORS

- Allen Square, University of Pennsylvania, Wharton School
 - Danielle Cameron, University of Pennsylvania, Wharton School
 - John Jenkins, University of Pennsylvania, Wharton School
 - Kenneth Gamble, Universal Companies
 - Lanxton Washington, L. Washington & Associates, Inc.
 - Leslie Esdaile-Banks, Author/Economic Development Consultant
 - Lubo Sarvas, Drexel University LeBow College of Business
 - M. Therese Flaherty, Wharton Small Business Development Center
 - Nicholas Lamberson, Drexel University LeBow College of Business
 - Rebecca Pedersen, Drexel University LeBow College of Business
 - Sagar Patel, Drexel University LeBow College of Business
 - Sidney Johnson, Supreme Janitorial & Maintenance Co.
 - Willie F. Johnson, PRWT Services, Inc.
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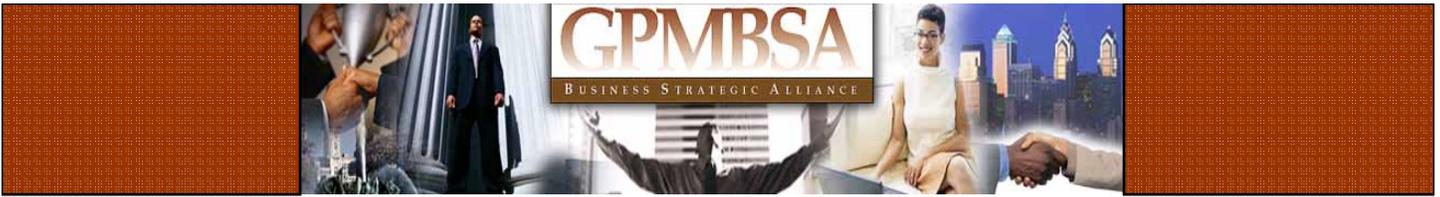
EXECUTIVE SUMMARY

The Greater Philadelphia Minority Business Strategic Alliance (GPMBSA) has compiled this report, “*Succession Planning for Minority-Owned Enterprises: The need to Prepare the Next Generation of Minority Business Owners*,” to address the issue of Succession Planning for minority-owned businesses in the Greater Philadelphia Region. It is hoped this report will (a) heighten awareness in the minority entrepreneurial community, (b) generate solutions for retaining and transferring minority-owned businesses in the community, (c) motivate government officials and corporate America to allocate funding and other resources to address the problem, and (d) invite sponsors, partners and others concerned with minority business issues, on a local, regional and national level, to participate and confront this emerging challenge.

The minority business economic development community has historically placed great emphasis upon, and many resources towards, assisting business start-up and growth. Many mature minority businesses have operated long enough and have survived the substantial obstacles that cause approximately 56% of business start-ups to fail within the first four years.¹ These are businesses that have grown to become institutions within the economic infrastructure of their communities. These are also, generally, the larger minority-owned businesses that create jobs for minorities and others. These businesses significantly impact the community--economically and socially, while providing goods and services to major corporations.

Succession Planning can help established minority business owners who want to exit the business upon retirement or in an emergency. The plan is to have the business continued by either a family member or an interested and qualified minority entrepreneur who would buy the business at the fair market value.

Beyond helping to create and service start-up and growing minority businesses in the region, there is another emerging challenge. Minority businesses that were established in the Northeast corridor during (and shortly after) the advent of Civil Rights are now mature, and as the business creators approach the exit door to retirement, they are confronted with a dilemma. **These mature business owners are faced with the challenge of passing their businesses to other minority entrepreneurs, selling to non-minority buyers or closing shop.**



Most minority-owned businesses are first generation owned. Many of these business owners do not have children who are both qualified and interested in maintaining the family business. In addition, there is no readily available market of minority buyers who have either the financial resources to seek traditional financing, or who are interested in acquiring and managing the minority firms.

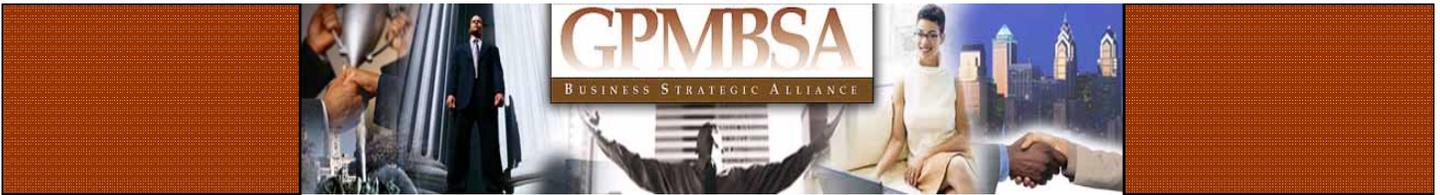
Minority is defined by the U. S. Census Bureau as socially and economically disadvantaged groups, which are all non-White classifications for race and ethnicity. These include Black or African American, Asian, Native American, and Hispanic or Latino of any race.

What complicates the sale (and continuation) of minority-owned firms is the fact that even if mature minority business owners were able to locate buyers for their enterprises, the economic value and social benefits derived from those businesses would be greatly diminished if these businesses are not passed on to other minority owners. Many of the existing contracts and relationships of minority-owned businesses were built upon their “minority business enterprise” status.

In order to maintain these contracts and relationships, these businesses must remain under minority ownership. Many mature minority-owned firms have successfully leveraged special government/corporate programs (such as the Small Business Administration (SBA) Federal 8 (a) program, State/City DBE/MBE certifications, and Corporate Supplier Diversity certification programs, etc.). Most of the successful ones have developed the experience and capacity to compete competitively on the open market. However, many of the minority business contracts continue to be based on existing relationships and minority-owned business status.

These businesses also continue to face many of the challenges inherent to minority-owned firms. This is due to a number of reasons that have already been researched and documented in the Milken Institute’s research report on “The Minority Business Challenge.” The Milken report points to the lack of access to capital, technology, and markets (among other barriers), as critical elements that have hindered these firms from general expansion, despite their overall success metrics.²

If a mature firm loses its “minority ownership” designation through a management change via selling the business to a new, non-minority owner, years of contract awards and relationships will evaporate. As a result, the business value would be significantly diminished.



Ironically, the same challenges that the mature minority business seller faced also confront the potential minority business buyer. In short, most potential minority buyers do not have the individual financial capacity to purchase the businesses being sold at the fair market value. The mature minority businesses therefore, are of less value to non-minority buyers (who may have the financial capacity to acquire these businesses) if the minority-based contracts are lost. This “Catch 22” scenario presents a challenge for the seller and the interested minority buyer. In addition, most of the social benefits of being a minority-owned business would be lost.

For a maturing minority-owned business to achieve its maximum social and economic potential and community impact, there needs to be a succession plan in place. Based on the findings of this report, the succession plan must involve passing of the business to another minority owner.

Additionally, most minority-owned first generation small businesses are micro-businesses that create few jobs beyond employing the entrepreneur and one or two family members. However, ***the focus of this report is on mature businesses that employ a substantial number of minorities and others.*** These mature minority-owned firms have vast institutional knowledge and are solid employers within the minority community. Most of the “Top Ten” minority businesses in the Philadelphia Region, as published in the 2004 Philadelphia Business Journal, are at this “at risk” stage of their life cycle. These businesses add economic stability to endangered community sectors and significantly contribute to the overall regional tax base.

We trust this report will bring to the forefront the significant contributions of mature minority-owned companies to the local, regional and national economy; explore the impact of having to close these businesses; and highlight the need to facilitate the passing of these companies, through succession-planning strategies, to the next generation of minority business owners.

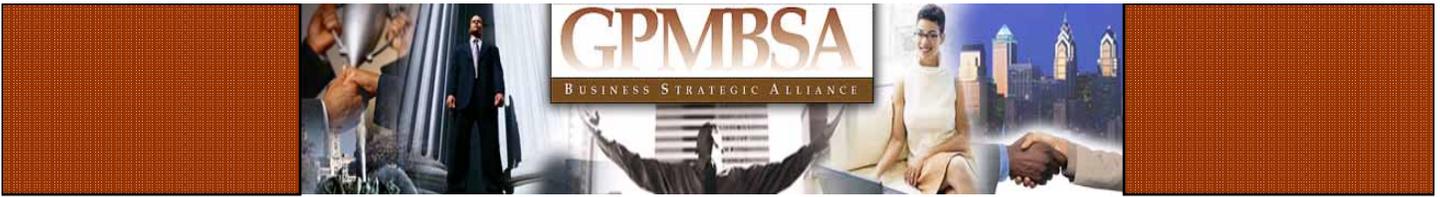
Philadelphia-NJ Primary PMSA (also referred to in this report as the “Greater Philadelphia Region”) as defined by the U.S. Census Bureau, includes five counties in PA (Bucks, Chester, Delaware, Montgomery and Philadelphia) and four counties within New Jersey (Burlington, Camden, Gloucester and Salem).

John Milligan

Marjorie L. Anderson

GPMSA Board Chair

GPMSA Executive Director



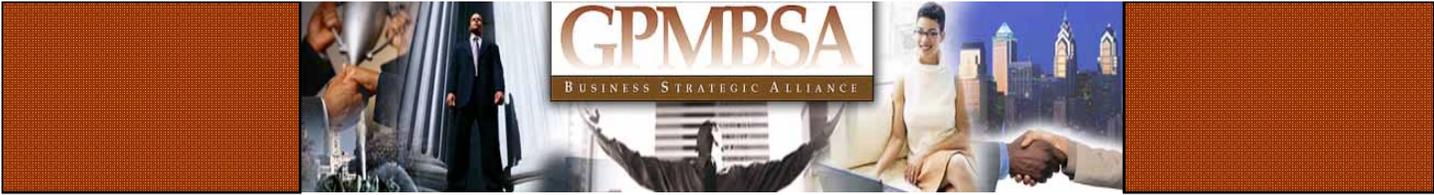
INTRODUCTION

Entrepreneurship is an important driver of a healthy economy. Unfortunately, jobs are departing the U.S., and the country should look to entrepreneurs for employment opportunities and industry innovation. It is a misconception that only major corporations define regional markets, when it is entrepreneurship that provides potential for job and wealth creation. This is especially true for the Greater Philadelphia Area where there is a “Brain drain” of young professionals leaving the area for cities they perceive to be more economically viable and trendy.³ As the 5th largest city among the top 100 U.S. regional areas, Philadelphia is ranked only 68th in entrepreneurship activity.⁴ This is a dilemma for Philadelphia and an indirect problem for the nation.

Philadelphia must create incentives for local entrepreneurship by appealing to and protecting the minority business community. There is a need for improvement in the numbers and fiscal health of minority-owned businesses. The correct implementation of incentives must be applied to deliver productive results. However, this is a two-fold recommendation, which requires *supporting incentives for new minority entrepreneurship ventures and providing succession planning strategies* for mature Philadelphia-based minority businesses.

A “mature” minority-owned business is a venture that has operated long enough (five years or beyond) to survive the substantial obstacles that cause approximately 56% of business start-ups to fail.

The findings and recommendations of this report may be used to help enhance the regional economy by advancing the city’s minority business community, curtailing the current “Brain drain,” and serving as a national model for mature minority businesses in other cities that are confronted with similar challenges.



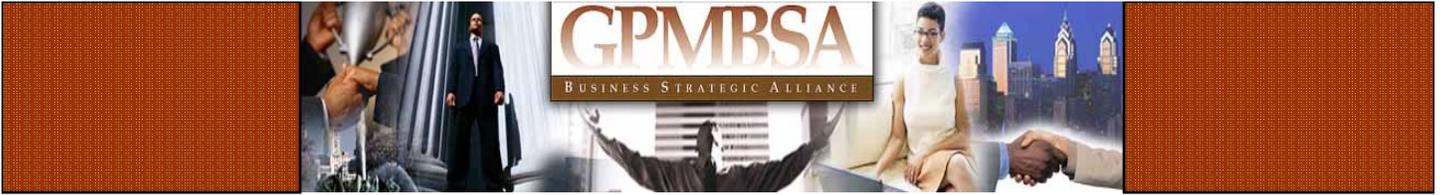
THE SCOPE OF THIS REPORT

For over 20 years, the managers of the GPMBSA have been assisting Greater Philadelphia Region minority entrepreneurs, many of whom started businesses in the post Civil Rights era. During that period, many of the area's largest and most successful minority-owned businesses ceased doing business because they failed to develop an adequate succession plan. Recently, GPMBSA managers have seen many minority entrepreneurs who built successful businesses face the same challenge. Many of these companies are now maturing, and the founders who built the companies are facing retirement without a plan for sustaining the business and protecting the equity in the business.

The challenge is that many of these minority entrepreneurs do not have a plan for passing on the business to a successor. Often their children and family members are not interested in or prepared to continue the business. They do not have a direct means to find younger, minority entrepreneurs who are qualified and interested in acquiring and managing their business. Additionally, there is no readily available market of minority buyers who have either the resources to seek traditional financing, or who are interested in purchasing the mature firm at fair market value. Many of the existing contracts and relationships of minority-owned businesses were built upon their "minority enterprise" status; and if these businesses are not passed on to other minority owners, most of the social and economic benefits of minority ownership will be lost.

This report examines the socio-economic impact that minority-owned businesses have on the Greater Philadelphia region. It cites examples of successful minority-owned businesses that are thriving. It also cites examples of sizable minority-owned businesses in need of succession planning. The "Findings" section of this report presents the results of surveying 350 minority-owned businesses about their succession plan, and provides additional insights from survey participants. Finally, this report proposes "Next Steps" for this dilemma.

Many of the existing contracts and relationships of minority-owned businesses were built upon their 'minority enterprise' status.



THE OVERALL IMPACT

Why is inadequate succession planning a problem?

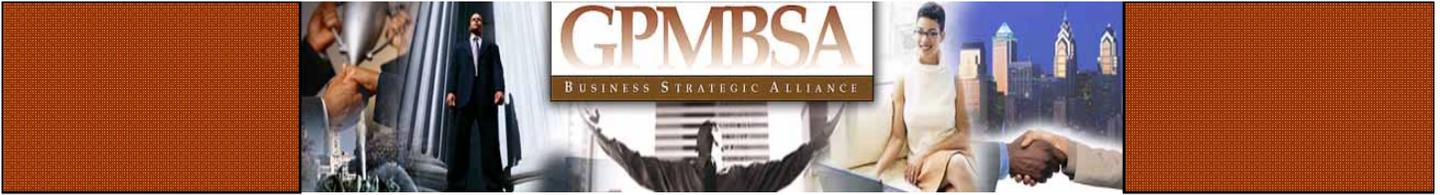
Every year various economic development agencies in the area spend millions of dollars and countless hours assisting start-up or growing minority-owned businesses. Only a select few of these businesses are fortunate enough to survive past the first four years. These are the businesses that develop into job producers, corporate suppliers, and social anchors. They are the businesses that provide most of the social benefit of minority business ownership. These businesses are typically founded and managed by entrepreneurs who are critical to the organization's growth and survival. As these businesses mature and the entrepreneurs age, succession planning becomes critical.

If these entrepreneurs do not plan sufficiently for business succession to new minority owners, the establishments will most likely go out of business or be sold at below-market prices to non-minorities. As a result, local and national tax revenues will decline, jobs that are available to minorities will disappear, and the many other social and economic benefits of sustained minority-owned businesses will be lost. The social fabric of the community will be impaired because of the loss of minority-owned businesses and the products and services they provide.

Healthy minority-owned businesses create pride and a sense of ownership and aspiration within the minority community. Furthermore, minority business owners inspire young people and help to deter street gangs, drugs and vandalism in the community.

The GPMBSA decided to compile this report to bring this business continuity problem to the forefront, in hope that government, private corporations, and the minority entrepreneurial community will be informed of the issue and its impact. This research project was also conducted to determine the socio-economic benefits of successful minority-owned business continuity in the minority community and incite area leadership to develop solutions for the challenge.

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CONTRIBUTION OF MINORITY-OWNED BUSINESSES

Economic Impact

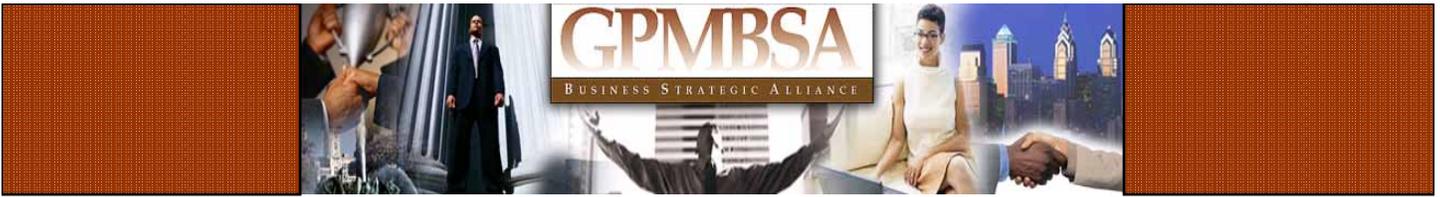
The importance of minority firms to local business and communities across the nation is obvious, especially in the Philadelphia area. There was a 110% increase in the number of minority firms with paid employees in the Philadelphia area from 1992 to 1997.⁵ This equates to the creation of 8,000 additional businesses with paid employees in Philadelphia during this period. Clearly, the impact of these businesses on the Philadelphia community is profound. For example, Philadelphia-area minority businesses sustained over 46,000 jobs during this period, which accounts for greater than \$1 billion in annual payroll.⁶

Minority Owned Businesses and Major Corporations

Many mature minority businesses offer expertise and quality products and services in their area of trade. Large corporations currently have many long-standing relationships with minority businesses. Large corporations desire goods and services from businesses that are well established in their industry. With the demise of these businesses, corporations would have to take risks contracting with other companies that have little or no track record. The alternative for these larger corporations would be to conduct business in the traditional manner with non-minority alliances. Allowing mature minority businesses to die would not only affect its owners, but also will be a drain on reliable resources for other corporations that require quality goods and services in compliance with their diversity/vendor programs.

Social Impact

The health of communities depends on economic stability and growth. Minority businesses provide more than just jobs and contribute to the Gross Domestic Product. They create pride and a sense of ownership within the communities they inhabit. Additionally, the business owners and managers serve as role models, mentors and community activists. Mature minority businesses also create an anchor within the community and provide diverse opportunities, including career internships, for high school and college students.



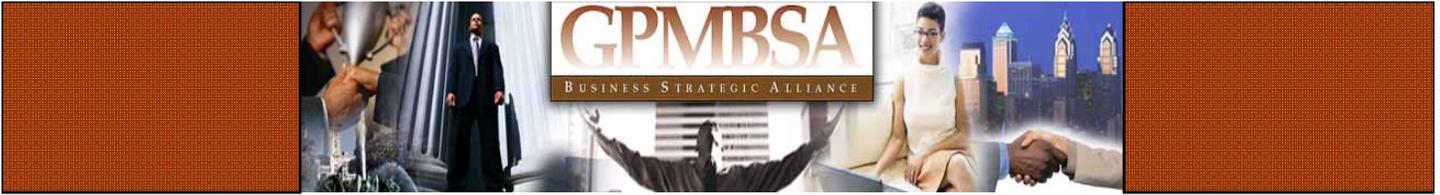
EXAMPLES OF MINORITY BUSINESS CONTRIBUTIONS

KENNETH GAMBLE

To highlight the benefits of minority-owned firms in the community, we can evaluate the investments of Mr. Kenneth Gamble, renowned musical writer, composer, producer, founder and CEO of Philadelphia International Records. Since the 1960's, Mr. Gamble and his company have written, produced and recorded more than 3,000 songs performed by numerous artists. Mr. Gamble is credited as the creator of The Sound of Philadelphia (TSOP), which has placed Philadelphia on the international map as a mecca for the music industry and promoted Philadelphia worldwide. In addition to his musical talent and entrepreneurship, Mr. Gamble began investing in blighted residential communities in Philadelphia in 1970. In 1993 he founded Universal Companies, a community development corporation which confronts the challenge and alleviates the effects of urban decline in the Philadelphia community. Universal has developed a wealth of skilled staff support in the areas of real estate, education, workforce and economic development. Universal has grown to exceed 130 professionals with a wide range of skills and professional expertise, which are vital to rebuilding and improving the socio-economic health of the community.

WILLIE F. JOHNSON

Another visible example of community advancement is seen through an entrepreneur by the name of Willie F. Johnson, Chairman and Chief Executive Officer of PRWT Services, Inc. Founded in 1988 and headquartered in Philadelphia, PA, with six additional offices around the country, PRWT is one of the fastest growing minority-owned and operated companies in the nation and one of the Philadelphia region's top six minority-owned firms, as reported by Black Enterprise magazine (June 2004). PRWT contracts with governments for tasks such as cleaning, phone services, toll taking, and building management. The company provides jobs to 1,180 people and generates annual revenues in excess of \$33 million.



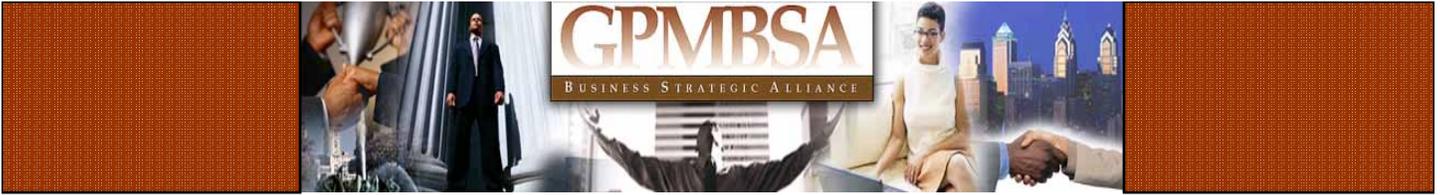
EXAMPLES OF MINORITY BUSINESSES FACING THE CHALLENGE

SIDNEY JOHNSON

Sidney Johnson, President and Founder of Supreme Janitorial & Maintenance Co., is a prime example of an established, mature, minority-owned company confronted with the challenge of passing on his business to a minority entrepreneur. Mr. Johnson founded Supreme Janitorial in 1985 as a mom-and-pop operation. This government-certified, minority-owned company is currently one of the finest building maintenance service establishments for janitorial and window cleaning services in the Delaware Valley Region. The profitable company, which also provides on-site training, was listed as # 1 in the Philadelphia Business Journal's (2004) "Top Ten" Minority-Owned Businesses. Over the past 20 years, this company has grown to a multi-million dollar establishment with more than 140 employees. The founder is approaching retirement and is facing the succession planning dilemma discussed in this report.

LANXTON WASHINGTON

L. Washington & Associates, Inc., a licensed, minority-owned, private detective and armed security agency, was started in 1987 by its Founder and President, Lanxton Washington. Mr. Washington is a former United States Army commissioned officer and a Vietnam Veteran. He was called, once again, to serve his country in the aftermath of the September 11th tragedy. His company was awarded substantial contracts from the Federal Emergency Management Agency (FEMA) to provide round-the-clock security at Ground Zero in New York City. Twenty-three new jobs were created as a result of this contract. In addition to the increased contract work with FEMA, the company provided additional security personnel at the US Postal Service Office and the Federal Courthouse in Brooklyn, NY and provided security service to the Federal Aviation Administration Control Towers. L. Washington & Associates, Inc. has been assigned responsibilities at the Philadelphia International Airport, Northeast Philadelphia Airport, Wilkes-Barre-Scranton International Airport, Reading Airport and the Harrisburg Airport. Together, these contracts created 69 additional jobs. The company is poised to receive future government contracts in the wake of heightened security needs in the United States. Like Sidney Johnson and numerous other area entrepreneurs, Mr. Washington must focus on developing an adequate succession plan.

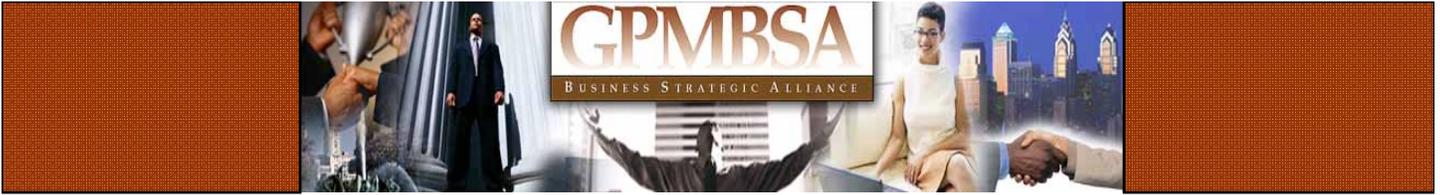


THE FINDINGS

The GPMBSA, in conjunction with graduate and undergraduate business students at Drexel University LeBow College of Business and the University of Pennsylvania's Wharton African American MBA Association, surveyed 350 minority entrepreneurs in the Greater Philadelphia Region during the last six months. The list of companies surveyed came from many minority-owned (MBE) and women-owned (WBE) Business Enterprise Directories, including: the Minority Supplier Development Council of PA-NJ-DE, the African American Chamber of Commerce of PA-NJ-DE, the SBA Philadelphia Regional Office, SBA 8(a) listing of certified minority companies, the U.S. Department of Commerce-MBDA's Philadelphia Minority Business Development Center (2003), the Philadelphia Business Journal Annual List of the Top 25 minority firms in the region for 2004, and Black Enterprise List of the Top 100 Companies in 2004.

From the 350 minority entrepreneurs surveyed, the study identified 100 mature minority-owned businesses that had reached the phase of their life cycle where succession planning has become critical.

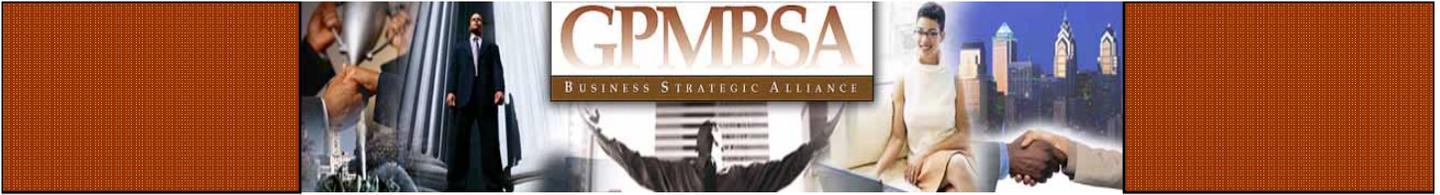
- Of these businesses, 62% do not have a formal succession plan.
- Several of those who said they have a succession plan qualified that statement with: "My spouse will run the business if something happens to me." "I hope my children will pitch in." "I would ask my father." "My supervisor will have to be in charge." "I hope my brother or sister will continue the business."
- 85% of these mature companies are interested in passing on their business to another minority entrepreneur, since a large percentage of their business is based on their "minority enterprise" status.
- Many said they have not given serious thought to this matter.
- 90% of these mature business owners have not directly sought out a qualified minority successor.
- 75% of these mature companies have some form of "minority-based" contracts.



ADDITIONAL INSIGHTS

Questionnaire responses and subjective narrative obtained from business owners provided invaluable information for this report. Insights obtained from participant interviews and feedback included the following points:

- Many of the most successful of these business owners want to feel comfortable with the entrepreneur who will succeed them and want to be convinced that their businesses will continue (live on through the next generation) and be managed consistently with their values.
- Several participants would be willing to take back a promissory note from a qualified minority entrepreneur who would responsibly take over their business, if that entrepreneur is able to offer a down-payment of at least 15% or 20% of the business selling price.
- Several participating business owners also said they would be willing to work (remain) with the company for as long as it takes to support the younger, minority entrepreneur as he/she learns the operations and takes over the business.
- Many business owners indicated they are willing to help the qualified minority entrepreneur on a consulting basis.



NEXT STEPS...

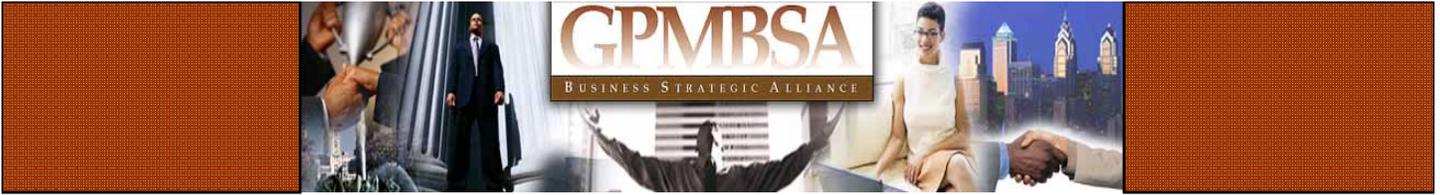
There is an opportunity to develop initiatives to help sustain minority-owned firms through succession planning.

Based on the findings in this report, the GPMBSA sees the need for dialog that would lead to solutions for succession planning for minority-owned enterprises in the Greater Philadelphia Region. Although this report does provide general recommendations for protecting the minority business community, it does not offer specific solutions for addressing the minority business succession dilemma. A deliberate and integrated coalition should be formed to develop a model that produces well-planned and executed results.

The GPMBSA hopes to stimulate dialog within the community with the release of this report and to help the community develop an understanding of the scope of the problem.

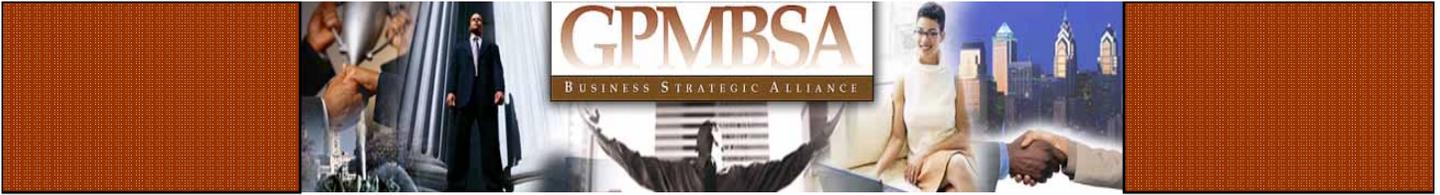
As a next step, government, corporations, and the minority business community need to work together to develop a solution for minority succession planning. The business leadership in the area also has an opportunity to foster on-going forums to connect, educate, and inform the mature minority business owner and the younger minority entrepreneur of business-ownership opportunities within the Philadelphia Region.

For additional information please contact the Greater Philadelphia Minority Business Strategic Alliance at phone# 215 399-0062. Or visit our website at www.gpmbsa.com



INFORMATION SOURCES

- African American Chamber of Commerce of PA-NJ-DE
- African American MBA Association, University of Pennsylvania
- Black Enterprise Magazine—June 2004
- Drexel University-LeBow College of Business
- The Enterprise Center/Advanced Research Technologies, LLC
(October 2003 Report) on Accelerating Minority Entrepreneurship
- The Milken Institute/MBDA (September 2000 Research Report) on
The Minority Business Challenge
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- Philadelphia Inquirer, 4-6-03
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- U.S. Small Business Administration



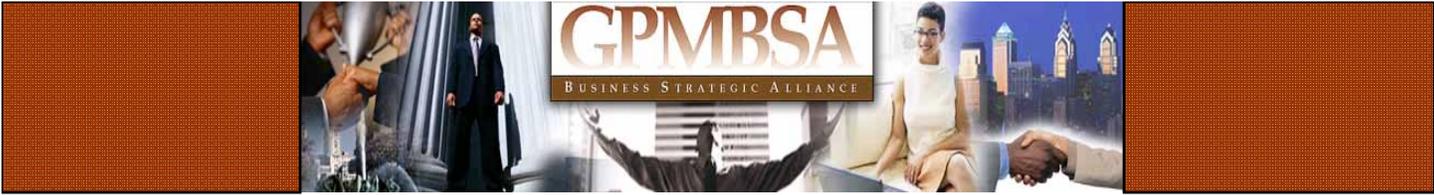
FOOTNOTES

- 1.) U.S. Small Business Administration
Frequently Asked Questions
Advocacy Small Business Statistics and Research
<http://www.sba.gov/>

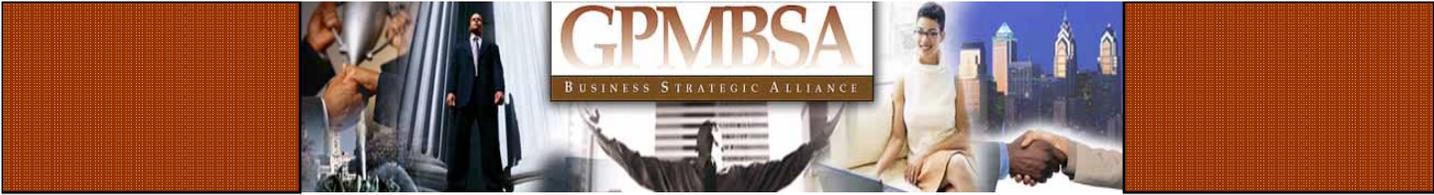
According to the “Frequently Asked Questions” section of the U.S. Small Business Administration’s website (<http://www.sba.gov/>):

44% of new business establishments survive at least four years. This means that 56% of these same businesses fail or close within the first four years. Sources: “Survival and Longevity in the Business Employment Dynamics Database” by Amy E. Knaup, Monthly Labor Review, Volume 128, Number 5 (May 2005), pp.50-56;
“Redefining Business Success: Distinguishing Between Closure and Failure” by Brian Headd, Small Business Economics, Volume 21, Number 1 (August 2003), pp. 51-61.

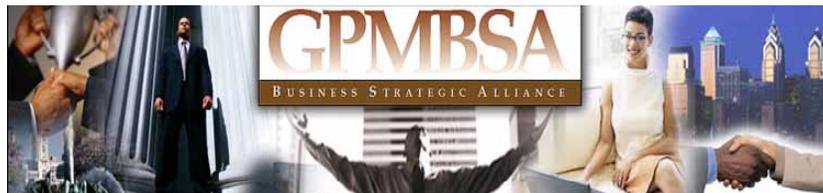
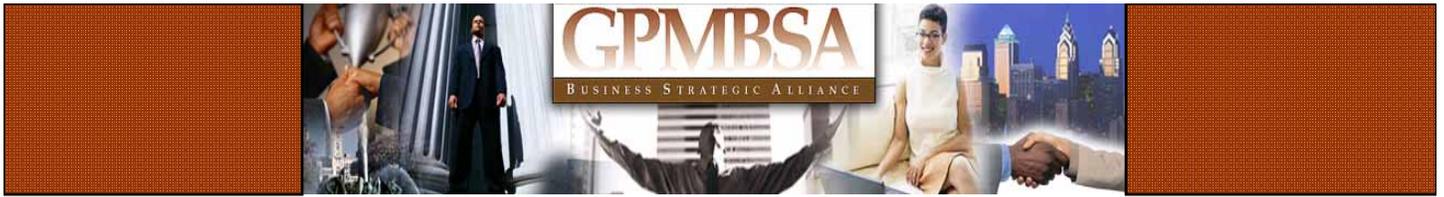
- 2.) The Milken Institute Report (September 25, 2000); “The Minority Business Challenge.”
- 3.) Brain drain references:
 - a. Philadelphia Metro 2-27-06
 - b. Philadelphia Inquirer 4-6-03
 - c. Philadelphia Business Journal 11-22-02
 - d. Philadelphia City Paper 1.31-2.7-2002
- 4.) “Accelerating Minority Entrepreneurship in Greater Philadelphia,” The Enterprise Center/Advanced Research Technologies, LLC, p.3, October 2003.
- 5.) 1997 U.S. Census Data.
- 6.) 1997 U.S. Census Data.



NOTES



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Greater Philadelphia Minority
Business Strategic Alliance
105 N. 22nd Street
Philadelphia, PA 19103
215-399-0062
www.GPMBSA.com