

Examining the Relationship Between Succession Planning and Small Business Failure

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ABSTRACT:

Data has demonstrated the critical significance of succession planning in the context of small businesses. Small enterprises, constituting a substantial portion of the U.S. economy, face unique challenges ensuring seamless transitions from one leadership generation to the next. The study emphasizes the pivotal role of succession planning in mitigating disruptions, enhancing organizational resilience, and preserving long-term viability.

Examining the complexities inherent in small business succession, the study delves into the multifaceted reasons behind the lack of formal succession plans, including emotional attachments, fear of retirement, and reluctance to confront uncomfortable decisions. Despite the crucial role played by small businesses in the nation's economic landscape, a substantial majority lacks preparedness for succession, leading to potential repercussions for local economies and employment.

Acknowledging the legislative efforts to address this gap, the study discusses the introduction of the Small Business Succession Planning Act. This bipartisan initiative aims to empower small business owners by providing resources, tax incentives, and educational support to facilitate the creation of formal succession plans. By dissecting the challenges faced by small businesses and presenting legislative interventions, this abstract underscores the urgency of prioritizing succession planning for the sustained growth and resilience of small enterprises.

Keywords: Succession planning, Small business, Minority business, Key roles

I. INTRODUCTION

Small businesses constitute the majority of privately held companies in the U.S. The Small Business Administration (SBA) notes small businesses constitute a vital component of the U.S. economic landscape, contributing significantly to job creation, innovation, and the nation's competitive edgeⁱ. A recent report underscores their substantial impact, revealing that these entities represent forty-four percent of the total U.S. economic landscape. Within this study, minority businesses comprise more than 1.1 million businesses in the United Statesⁱⁱ. The Small Business Administration notes that minority businesses encompass fifteen percent of all U.S. small businesses.

Another study notes that among small businesses, over seventy-five percent of small business owners consider the transfer of management or ownership at some pointⁱⁱⁱ. This underscores the necessity for formal succession planning. However, research indicates that only thirty percent of these businesses will successfully navigate a transition, primarily due to the absence of formal succession plans or other external factors. The impending challenge for small businesses in the U.S. lies in the fact that, as they approach retirement, nearly seventy percent of owners lack prepared plans to facilitate a seamless transition of ownership and management. The limited success in succession or transition within small businesses can be attributed partly to small business owners' absence of formal succession planning, as noted by Kislik (2018). A study conducted by Rashid, N. A., & Puttri, D. (2018) in Padang City suggests that most small business owners react to succession issues without having a business continuity strategy. The study also notes that the complexities of succession planning are further exacerbated when owners pass the business to their children, with parents often hesitant to initiate planning due to the discomfort associated with making critical decisions. The research adds that even if owners formulate a succession strategy, external factors such as economic downturns, market declines, competition, and limited access to financial capital can threaten their planning efforts. Both anticipated and unforeseen challenges may emerge during the transaction and post-deal transition phases, potentially impacting the small business's performance. In the absence of a well-defined formal succession plan, these challenges can become overwhelming and have detrimental effects on the long-term success of the small business and potential successors. These problems are even more prevalent in minority-owned businesses.

II. THE PROBLEM OF SUCCESSION PLANNING AND SMALL BUSINESSES

Research has noted that while sixty percent of small businesses don't have a succession plan, this number is over seventy percent for minority businesses^{iv}. The study adds that minority business owners lack a succession plan for several reasons, including lack of succession planning instruction, family members not being interested in taking over the business, and the business still being small and struggling. This lack of a succession plan eventually leads to business failure and closure. One of the most notable minority business failures was the closure of Wall Street, Daniels & Bell Inc.

In the unfortunate demise of Travers J. Bell Jr., co-founder of Daniels & Bell Inc. (D&B), the first black investment firm to have a seat on the New York Stock Exchange, the absence of a succession plan proved to be critically detrimental^v. Following Bell's untimely death in 1988, leadership transitioned to his offspring, Rhonda and Darrell, lacking any prior experience in the securities industry. This lack of preparedness resulted in a series of management decisions that stirred discontent among company principals, prompting some to depart for other firms. Simultaneously, the inexperienced successors accumulated debt on the corporate credit card and committed several payroll errors, ultimately leading to the closure of the business within five years. This poignant case underscores the vital importance of effective succession planning in sustaining organizational continuity.

The failure of small businesses, particularly those owned by minorities, is a multifaceted issue, with minority-owned businesses experiencing higher failure rates^{vi}. The impact of small business closures extends beyond individual enterprises, posing a broader challenge for any state's economy. Small businesses play a crucial role in job creation and employment, and their failure contributes to increased unemployment, creating an additional burden for local communities and the country at large. Each time a small business shuts down, it not only represents the loss of an individual enterprise but also has cascading effects on overall economic vitality and community well-being. Studies have indicated that small businesses face failure due to diverse factors, including insufficient management skills and inadequate capital. However, an often overlooked factor contributing to business failure and closure is the absence of a succession plan.

Succession Planning and its Importance to Business Survival

Succession planning is a comprehensive process designed to identify, develop, and retain individuals within an organization who have the potential to fill key leadership or critical roles in the future^{vii}. It is a strategic approach to ensure the continuity of leadership, maintain institutional knowledge, and prepare for the departure or retirement of key personnel. Below are the key components of succession planning explained in detail:

1. **Identification of Key Positions:**

- Organizations begin by identifying positions crucial for the success and sustainability of the business. These are typically leadership roles or positions with specialized skills and knowledge.

2. **Talent Assessment and Identification:**

- Once key positions are identified, organizations assess current employees' skills, competencies, and potential. This involves identifying high-potential individuals who exhibit qualities necessary for future leadership roles.

3. **Development Planning:**

- High-potential employees are provided with targeted development plans to enhance their skills and prepare them for future responsibilities. This may include training programs, workshops, mentorship, and exposure to different aspects of the organization through job rotations.

4. **Succession Candidate Pool:**

- A succession candidate pool is created, consisting of individuals who have been groomed and identified as potential successors for critical roles. This pool ensures that multiple qualified candidates are available for each critical position.

5. **Leadership Training and Education:**

- Organizations invest in the continuous training and education of potential successors, ensuring they are well-equipped to handle the challenges and responsibilities of leadership roles. This may involve leadership development programs and executive education.

6. **Performance Monitoring and Feedback:**

- The progress of individuals in the succession pipeline is regularly monitored. Feedback is provided to help them understand their strengths and areas for improvement. This feedback loop is essential for continuous improvement.

7. **Knowledge Transfer:**

- Employees in key positions often possess valuable institutional knowledge. Succession planning includes strategies for capturing and transferring this knowledge to potential successors. This may involve mentorship, documentation, or knowledge-sharing initiatives.

8. **Contingency Planning:**

- Succession plans should include contingency measures in case of unforeseen events, such as sudden departures or emergencies. Having backup candidates or interim solutions ensures business continuity.

9. **Regular Review and Revision:**

- Succession plans are not static; they require regular review and adjustment. Changes in organizational strategy, shifts in talent dynamics, or evolving business needs may necessitate updates to the succession plan.

10. **Integration with Organizational Strategy:**

- Succession planning aligns with the overall strategic goals of the organization. It ensures leadership development aligns with the company's long-term vision and objectives.

Research notes that forty-five percent of organizations do not have a contingency plan for the chief executive officer's (CEO) succession. The research also stated that forty-six percent of U.S. organizations do not have a CEO succession planning process. The succession planning process involves systematically identifying pivotal roles within an organization and formulating strategic initiatives to prepare and empower individuals to assume these key positions. Research notes that statistics are more staggering for small and minority-owned businesses, which lack the financial and physical resources for succession planning.

Succession in small businesses raises concerns due to the challenge of finding capable successors to replace small business owners effectively^{viii}. Small businesses typically lack established processes for a systematic transition of leadership. In these enterprises, control and ownership are commonly concentrated in a single individual—the business owner. Unlike large corporations, the identity of the business is closely tied to the owner. Consequently, any unplanned departure of small business owners often results in the downfall of the business.

The majority of small business owners fail to engage in future planning, opting to leave everything to chance. Many of these owners procrastinate or avoid succession planning due to emotional attachments to their businesses, fear, or hesitancy to retire^{ix}. However, the crucial role of small businesses in a nation's economy underscores the necessity of prioritizing succession planning in this sector.

III. SUCCESSION PROBLEM STATEMENT

Succession planning poses a significant challenge for contemporary small businesses. This critical process, which involves identifying and nurturing potential successors for key roles within an organization, stands out as a significant contributor to the global failure of small businesses^x. The fate of a business is inevitably tied to its succession planning—either it will thrive through successful succession or face failure. Despite ongoing research aimed at comprehending the factors associated with successful business transition and succession, it remains complex to unravel why small business owners adopt various succession strategies and the underlying motivations for their choices.

In the period of transition from one owner to the next, a majority of small businesses face failure, with only thirty percent enduring into a second generation and a mere twelve percent remaining viable into a third generation^{xi}. The research adds a mere three percent manage to operate into the fourth generation and beyond, experiencing a significant decline in value during succession. While existing research has explored succession planning strategies for identifying and selecting capable successors, there is a notable gap in studies examining the integration of racial diversity into succession planning. This study delves into the specific research elucidating the rationales behind small business owners' reluctance to perceive succession planning as imperative, offering potential solutions for exploration by small business owners.

The transfer of ownership and leadership from existing proprietors to successors in small enterprises within the United States is a pivotal predicament affecting these entities' continued viability and prosperity, exerting a substantial influence on their operational efficacy and valuation^{xii}. The study adds that the absence of a structured succession plan is posited as the ultimate factor, culminating in the cessation of organizational existence. However, the scholarly landscape exhibits a notable absence of empirical investigations scrutinizing the perspectives and methodologies employed by minority and non-minority small business proprietors in the United States regarding the intricate domain of succession planning.

Current research literature on succession planning in small businesses delves into various aspects, including organizational control, leadership, management, and ownership transfer^{xiii}. Researchers have explored the impacts of succession planning, its essential nature, and the associated challenges. Despite these investigations, there is a notable gap in empirical research that scrutinizes the influence of factors such as the level of succession preparedness, the existence of a formally developed succession plan, and specific business characteristics on how U.S. small business owners navigate the landscape of succession planning.

IV. WHAT SUCCESSION PLANNING IS NOT – CHANGING PERSPECTIVES THROUGH VIABLE SOLUTIONS

Certain leaders perceive succession planning as a process of selecting an individual, publicly introducing them to the organization, and subsequently entrusting them to manage the ensuing consequences. Successful succession planning requires the current leader to manage the process of creating a smooth transition of power^{xiv}. There are a few things that we recommend the predecessor can do to assist in this process:

- Current leaders have the gift and ability to inspire and mobilize others to think and function differently. These same skills need to be applied in helping the new leader gain support from leadership and followers. The predecessor can reduce resistance by creating an atmosphere of confidence and assurance among leaders and followers.
- To ensure a smooth transition, the predecessor should transfer control gradually, allowing the successor to learn each area and their leaders while gaining the knowledge needed to function in those areas.
- The predecessor needs to stay aware and manage their emotions and feelings. Relinquishing authority can be challenging personally, so the predecessor must watch their emotions because it will impact the team and possibly unintentionally split loyalties.

We also recommend that small business owners utilize the Key Position Approach.

The key position approach in succession planning involves identifying and focusing on critical roles within an organization. Instead of planning for all positions, it prioritizes key positions crucial for the business’s success^{xv}. This approach ensures that the organization has a targeted and effective plan for filling critical roles in the event of succession needs.

In determining the categorization of a position as “key,” an evaluative criterion lies in assessing the consequential impact associated with that specific role within the organizational structure. The classification of a position as “key” can be ascertained by evaluating the ramifications of the incumbent’s absence, particularly instances where the non-presence leads to deferred decision-making, interruption of vital activities, or disruption and turmoil within the organizational framework.

The identification of key positions involves thoughtful consideration of specific inquiries:

- Which roles, if unoccupied, would significantly impede the achievement of present and future objectives?
- Which positions, if left vacant, would jeopardize the business’s well-being, safety, or security?
- Which roles pose challenges in terms of recruitment due to the specialized expertise and knowledge essential for task accomplishment?

Below is a form utilized to identify critical roles.

SIGMASuccession identify critical roles								i
Critical Role Identification Questionnaire								
	1 Not descriptive of this role	2 Slightly descriptive of this role	3 Moderately descriptive of this role	4 Strongly descriptive of this role	5 Very descriptive of this role			
Critical Role	Urgent Need	Lack of External Candidate Availability	Poor Internal Bench Strength	Strong Impact on Business	Unique Skill Set or Knowledge Base	TOTAL	*	
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			
	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5	1 2 3 4 5			

Figure 1. Identify critical roles

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Once key roles are pinpointed, it is imperative for small business leaders to meticulously compile a roster for each prospective candidate earmarked for occupying a critical position. Business proprietors should elucidate the criteria pertinent to the position and articulate the competencies anticipated from the candidates. Below is an example of a questionnaire to assist business owners in identifying key candidates.

The form is titled "SIGMA Succession Succession Profile". It includes a header with fields for Date, Succession Position, Current Incumbent, Exit Year, and Urgency (indicated by five stars). The main body is divided into several sections: a silhouette placeholder for a candidate, a "Succession Candidate" section with fields for Name, Position, Location, Service, Age, and Readiness (with radio buttons for Now, 1 to 2 Years, 3 to 4 Years, and 5 Years or More), an "Education and Experience" table with columns for Education and Experience, a "Position Criteria" section with a list of criteria and corresponding radio buttons, and a "Leadership Profile Assessment Gaps" table. The bottom of the form features the SIGMA logo and the text "Your Future. Down to A Science. www.SIGMASuccession.com" and "© 2017 SIGMA Assessment Systems Inc. All rights reserved."

Figure 2. Succession profile

Succession planning facilitates the proactive identification of potential candidates well in advance of actual organizational needs. This discovery process empowers the organization to scrutinize potential candidates, formulate a transition plan, and enhance preparedness for abrupt changes arising from environmental or personal factors. The key position approach not only provides the opportunity to minimize suboptimal leadership choices resulting from unforeseen vacancies but also generates potential candidates and fosters their development before the occurrence of a vacancy. Addressing unanticipated vacancies becomes more streamlined, preventing disruption to ministry operations and alleviating pressure on other leaders tasked with absorbing additional workload. Moreover, succession planning serves as a strategic tool for identifying ministry areas that may require restructuring, particularly those vulnerable to risk, such as an aging leader with no immediate successor. This restructuring may involve redistributing responsibilities to specific individuals or implementing cross-training initiatives to enhance proficiency in various areas.

Amidst the solutions proposed for small business owners in readiness for succession planning, it is noteworthy that government officials recognize the significance of this process. In acknowledgment of its importance, legislative measures have been considered to aid small business owners in their succession planning endeavors.

V. THE GOVERNMENT AND SUCCESSION PLANNING IN SMALL BUSINESSES

The cessation of small businesses exerts pronounced repercussions on local economies, influencing factors such as employment, services, and overall economic prosperity. In the United States, a considerable number of business proprietors operate without established succession plans, thereby exposing economies to heightened vulnerability. Contemporary legislative initiatives strive to furnish small businesses with the

essential resources requisite for retaining a workforce, extending services to other enterprises, and sustaining investments within communities.

Representatives Jason Crow (D-CO-06) and Andrew Garbarino (R-NY-02) have reintroduced the bipartisan Small Business Succession Planning Act^{xvi}. This legislation, which enjoys support from members of both parties, aims to aid small business proprietors in formulating comprehensive business succession plans. These plans are designed to establish structured processes for the seamless continuation of leadership and operational activities in scenarios involving an owner's retirement, demise, or other significant personnel changes.

The proposed Small Business Succession Planning Act entails several key provisions:

1. Directing the Small Business Administration (SBA) to develop an online business succession planning toolkit, offering guidance for small businesses to create effective succession plans in collaboration with the SBA or its resource partners. The SBA would be mandated to furnish trained staff or partners to assist small businesses in formulating their plans.
2. Encouraging the SBA to organize business succession planning workshops or events nationwide to enhance awareness and understanding of the importance of succession planning among small businesses.
3. Formulating a strategy to augment the prevalence of business succession plans, particularly among minority-owned businesses, through the SBA's outreach initiatives.
4. Offering financial incentives for small business owners to establish their succession plans, including a one-time \$250 tax break for initiating the planning process and an additional one-time \$250 tax break upon execution of the succession plan.

VI. CONCLUSION

An organization devoid of a succession plan exposes itself to potential disruption, ambiguity, and internal discord, thereby jeopardizing its future competitiveness. Particularly for small or minority-owned businesses, the matter of succession introduces profound emotional complexities, extending the sphere of stakeholders to encompass family members. The absence of a structured succession plan heightens the vulnerability of such businesses to multifaceted challenges, necessitating a strategic and emotionally intelligent approach to ensure organizational resilience and sustained success. Entrepreneurs are cognizant that triumph hinges on sustained continuity, encompassing established product or service creation procedures, fostering client relationships, and retaining key personnel. The essence of succession planning lies in securing enduring continuity, guaranteeing the business's resilience and expansion even after the departure of its progenitor. This strategic approach acknowledges the integral role of structured planning in preserving the business legacy and fostering sustained growth.

In delineating the obstacles confronted by small business proprietors in formulating and executing a succession plan, we have concurrently delineated various methodologies to facilitate the accomplishment of this undertaking. This acknowledgment underscores the multifaceted nature of the challenge and offers pragmatic strategies to navigate and surmount the complexities associated with succession planning in small business contexts.

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Conflict of Interest

There is no conflict of interest

Social media profiles

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