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Abstract

The UK Company Voluntary Arrangement (CVA) is an early example of a bankruptcy regime designed to aid the rescue of financially distressed SMEs. Its efficacy hinges on its application to aid only *viable* companies with liquidation as the preferred option for companies that are not viable. This article proposes the resource-based view as a theoretical means to assess the viability of bankrupt SMEs. Seven hypotheses are tested and provide support for the central proposition, that a company which has resource strength, but is pushed into bankruptcy by temporary factors, is more likely to succeed in a CVA. The article concludes that the resource-based view is useful for analysing the viability of bankrupt companies and that well-designed bankruptcy law can promote SMEs and entrepreneurship.

Keywords

bankruptcy law, entrepreneurship, insolvency law, rehabilitation, SMEs, turnaround

Introduction

One of the principal findings of research on small and medium-sized enterprises (SMEs) is that the financial performance of SMEs is inherently more volatile than large firms, and that a significant number will naturally experience periodic financial difficulty (Dannreuther and Kessler, 2010). Governments in many countries have focused on improving their bankruptcy regimes so that they

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are more SME-friendly. Collective frameworks have been proposed by the International Monetary Fund (IMF, 1999), the Organisation for Economic Co-operation and Development (OECD, 1998) and the European Union (European Commission, 2007). There is much to improve. The European Commission (2007) concludes that many countries had introduced appropriate measures only recently or not at all, and the academic literature concurs. In their review of the literature on SMEs and entrepreneurship, Blackburn and Kovalainen (2009) classify general public policy research as 'enduring', as it is in need of continuous theoretical and empirical development. More specifically, in a recent overview of bankruptcy law design, Lee et al. concluded that the topic is 'an important but understudied area' (2007: 268).

What should an SME-friendly and efficient bankruptcy regime look like? Franks and Torous (1992) suggest that bankrupt SMEs fall into two categories: those that are not viable (*economically* distressed), and those that are viable but are experiencing temporary financial difficulty (*financially* distressed). Lower levels of entrepreneurship and economic growth will occur if a bankruptcy regime allows the former to limp on and/or allows the latter to fail. Therefore, a bankruptcy regime should facilitate the speedy reallocation of resources tied up in SMEs that are not viable, while at the same time facilitate the rehabilitation and recovery of SMEs that are viable (Finch, 2009). Particular bankruptcy regimes may be biased one way or the other. Getting the balance right hinges on the ability to discriminate between firms that ought to be liquidated and firms that can be rehabilitated: that is, deciding on viability. The literature provides little practical guidance on how such a choice should be made (Mokal, 2004).

This article aims to address this lacuna by suggesting that the resource-based view of the firm which is rooted in economic theory (Penrose, 1959) provides an appropriate framework for considering the economic viability of bankrupt SMEs. It does so by analysing data on the UK Company Voluntary Arrangement (CVA) procedure, which was designed to encourage the directors of viable companies to instigate change before bankruptcy and, failing this, to promote the rehabilitation of viable SMEs once bankruptcy had occurred.

Specifically, the article addresses two questions. First, what factors discriminate between those bankrupt SMEs that should be saved and those that should not? Second, can the resource-based view be used to explain the factors that discriminate between bankrupt SMEs that should be saved and those that should not?

The article is structured as follows. The next section provides an overview of bankruptcy law and the CVA in the UK. This is followed by a literature review which leads to the generation of seven hypotheses. Next, the study's research design is elucidated and this is followed by a presentation of its results. A final section discusses these results and concludes the article.

Bankruptcy law and SMEs in the UK

The serious promotion of viable SME rescue through bankruptcy law in the UK dates back to 1982, when the Cork Report (Cork Committee, 1982) was produced. Legislation based on the recommendations of this report was enacted in 1985–1986. Practice began to change, and by 2002 administrative receivership, which favoured secured creditors and incentivized company liquidation, had lost dominance to collective procedures aimed at business rescue. In addition to schemes of reconstruction and arrangement, the legislative changes saw the advent of two customized rescue procedures for bankrupt or financially troubled companies. Of these, the administration order was the more formal, requiring petition to a court for an administration order and the potential removal of the directors from control of the company. By contrast, the second procedure, the CVA, was intentionally designed to be more informal, being both an out-of-court and a debtor-in-possession procedure:

that is, similar to the USA's Chapter 11 procedure, where the company's management remain in place during the course of the procedure (see Weisgard et al. 2010 for a comprehensive account of the CVA). Of course, debtor-in-possession will be undesirable when the firm is unviable, as existing management may block liquidation. However, it becomes desirable when the firm is viable and even more so when the firm is small and therefore unable to function without top management remaining in place (Mokal, 2004). Additionally, Lee et al. argue for debtor-in-possession thus:

Managers make firm-specific investments during their tenure with firms. This firm-specific knowledge may especially be required when a firm is in distress ... If managers are going to be driven out when a firm files for reorganization bankruptcy, not only will they be reluctant to file bankruptcy but they also may lack incentives to make firm-specific investments in the first place. (2007: 264)

The UK CVA procedure is now a mature SME rescue mechanism that is viewed to have achieved good results overall (Weisgard et al., 2010) and has become part of a general regime aimed at fostering entrepreneurship in the UK. Its success is indicated in the UK chancellor's (finance minister) Budget Report of 22 April 2009, which announced a consultation towards extending the procedure's moratorium against creditor action to large corporate entities (The Insolvency Service, 2009).² However, its take-up has been 'disappointingly low' (Department of Trade and Industry, 2001: 9), although to an extent the gradual uptake of the reforms was expected as accountants, lawyers and bankers need time to acclimatize (Mokal, 2004). To speed uptake, moratorium reforms were implemented in the Insolvency Act 2000.

Literature review and hypotheses

Resources are acknowledged increasingly within the SME and entrepreneurship fields as important influences on survival, strategy and performance (Terziovski, 2010). It is not hard to see why this is the case. The resource-based view emphasizes the heterogeneity of firms, which sits well with the idea that an entrepreneurial firm will do something innovative compared to other firms in the market. It has a natural affinity with Kirzner's (1973) view that entrepreneurs have the vision to spot unexploited opportunities, and hence can acquire resources for less than they are worth. The resource-based view has been used to illuminate many issues in entrepreneurship, but what is missing from this growing literature is anything on resources and the prospect of failure and bankruptcy. This article addresses this gap.

As stated previously, the first research question of this study is how to tell which among bankrupt firms are viable, and so warrant an attempt at rehabilitation, and which are not viable and so warrant liquidation. There is a consensus in the literature that it is very difficult to predict success and failure, whichever way these terms are defined (Gartner et al., 1999). The current study attempts to improve on this state of affairs by framing the analysis of SME viability within the resource-based view (Barney, 1991), which has rapidly become influential in the strategy, international business and entrepreneurship literatures (Barney et al., 2001).

The essential argument of Barney (1991) is that in order to provide a basis for viability, resources must be valuable, rare, imperfectly imitable by rivals and not subject to strategic substitution by alternative resources. Barney's definition of resources is broad and inclusive:

firm resources include all assets, capabilities, organizational processes, firm attributes, information, knowledge etc. controlled by a firm that enable a firm to conceive of and implement strategies that improve its efficiency and effectiveness. (Barney 1991: 101; emphasis in original)

Despite some progress in operationalizing resources for the purpose of empirical investigation, Wernerfelt laments the fact that the definition of resources leaves them resembling ‘an amorphous heap’ (1995: 172).

Bearing this shortcoming in mind, what can be said about resources, failure and rehabilitation? Here, we recall Franks and Torous’ (1992) suggestion that bankrupt SMEs fall into two categories: those that are not viable (economically distressed) and those that are viable but are experiencing temporary financial difficulty (financially distressed). This thinking draws from conventional microeconomics, arguing that failing firms which do not have the resource base necessary to earn a ‘normal’ (in the sense used by economists) return on capital should be liquidated, and their resources reallocated elsewhere. However, those firms which do have the necessary resource base to earn at least a normal return, but are pushed into bankruptcy by one or more adverse temporary factors – that is, are experiencing financial difficulty in the short run (in the sense used by economists) – should be subject to a rehabilitation attempt. On this basis, we have the study’s central proposition which informs seven hypotheses that are subsequently developed:

A firm which has resource strength or lacks resource weakness, that is pushed into bankruptcy by one or more adverse temporary factors, will be more likely to succeed in a CVA.

A number of resources have been identified as being important to SMEs, although there is little detail on the precise type of firm or context in which each type of resource will be more or less critical: a weakness also of the more general strategy-related resource-based view literature (Barney et al., 2001). Brumagim (1994) argues that the most important resources are *strategic vision* resources. In SMEs, these will reside in the entrepreneur (Barney, 1995). In line with this, much of the literature on the resource-based view and entrepreneurship places high importance on the quality of top management as a resource (Brush and Chaganti, 1999). The entrepreneur has a vital role in seeing opportunities, and assembling and coordinating resources to bring to bear capabilities within the market (Barney et al., 2001; Brush et al., 2001; Chandler and Hanks, 1994). This also fits with Bozner et al.’s (1998) emphasis on the importance of mental models and cognitive capacities as inimitable resources. Moreover, they argue that tacit, socially complex resources of the firm are often unique to and inseparable from the founder, cognate with Peteraf’s (1993) observation that imperfect mobility can arise where the firm and the factor are in essence a team. This is particularly salient, given the distinctive nature of the CVA as a debtor-in-possession regime which is, at least implicitly, predicated on the assumption that incumbent management is an important resource of the firm. This leads to our first hypothesis:

H1: CVA success will be less likely when poor management is the primary resource weakness.

No matter what resources the firm possesses, unless they are effectively marshalled, it will be to little avail (Thomas and Pollock, 1999). Hence Barney’s (1995) suggestion that to create competitive advantage, resources must be well organized, implying a premium on effective management in general – but which management functions might be most important?

Hunt and Morgan (1995) and Hunt (1997) make a strong case for *marketing* management. In essence, this approach fuses the resource-based view and marketing by stressing

the importance of market segments and resources. Market segments are identifiable groups of consumers whose tastes and preferences with regard to an industry’s output are relatively homogeneous *within* each group but significantly heterogeneous *across* the groups. Resources are tangible and intangible entities

available to the firm that enable it to produce efficiently and/or effectively a market offering that has value for some market segment(s). *Competition* among firms is an ongoing process and consists of the struggle among them for a comparative advantage in resources that will yield a marketplace position of competitive advantage and, thereby, superior financial performance. (Hunt, 1997: 60; emphasis in original)

Accordingly, this approach places the marketing function at the core of the firm: it is marketing management that marshals resources, such that a particular marketplace position is achieved with associated competitive advantage and financial performance. Deshpande and Webster concur: 'the marketing concept defines a distinct organizational culture ... that put[s] the customer in the centre of the firm's thinking about strategy and operations' (1989: 3). This leads us to our second hypothesis:

H2: CVA success will be less likely when poor marketing management is an important resource weakness.

Building on this line of thinking, Brush and Chaganti (1999) argue that an SME's ability to serve a market segment successfully will be positively correlated to the *human* resources that it possesses. Indeed, they maintain that the quantity and quality of human resources will be more important than the pursuit of a generic strategy (Porter, 1985) in determining financial performance. Ceding control of family firm to external professional managers can be critical to SME survival (Ng and Keasey, 2010). Chandler and Hanks (1994) also link market orientation and human resources when explaining SME financial performance:

[F]irms seeking to provide high quality products require a strong commitment to customer service which they show by training and empowering employees, delegating to lower ranks the authority to solve customer problems, and by rewarding employee efforts. (1994: 335).

They conclude:

The ability to organise and harness the creative and productive capacity of human resources appears to be of key importance. (1994: 343).

This leads to our third hypothesis:

H3: CVA success will be less likely when poor human resource management is an important resource weakness.

Brush et al. (2001) categorize resources on a scale from utilitarian to instrumental. Resources classified as utilitarian are applied directly in the productive process. At the opposite extreme, although instrumental resources are applied indirectly, they are fundamental as they allow access to other resources. The best example of an instrumental resource is finance: it is via financial resources that other resources (e.g. human) may be accessed. If a firm's financial difficulty is caused by poor financial management which, over time, has had the effect of weakening or failing to strengthen other (utilitarian) resources, then we would expect the chances of successful recovery to be slim (Thorburn, 2000). This leads to our fourth hypothesis:

H4: CVA success will be less likely when poor financial management is an important resource weakness.

Dyer and Singh (1998) have developed our understanding of resources by extending the scope of the search from resources residing *within* the firm to resources that exist *between* firms. They argue that critical resources may span firm boundaries and may be embedded in inter-firm relationships, stating that 'the (dis)advantages of an individual firm are often linked to the (dis)advantages of the network of relationships in which the firm is embedded' (1998: 660). Moreover, they find that the importance of such relationship resources is increasing as firms have become more dependent on supplier relationships. Subsequent empirical work has supported this line of thinking by showing that network resources do have a significant influence on firm performance (Cope et al., 2007; Pittaway and Rose, 2006). Regarding the focus of this article, the extent to which creditors are supportive during CVA indicates the strength of the firm's 'relationship' resource. All classes of creditor can be important, but for different reasons. Secured creditors, generally banks, have a very strong position in the UK bankruptcy system, and can make life very difficult for a firm which does not have their favour. Similarly, preferential creditors, especially HM Revenue & Customs (which collects corporation tax and sales taxes), have a strong position.⁴ Unsecured creditors often have little choice but to go along with a CVA proposal. In other types of bankruptcy regime they will almost certainly receive nothing, whereas in a CVA they have at least some prospect of a return. Nevertheless, they can be both hostile and awkward during the course of the CVA where they judge the directors of the firm to have been either reckless or dishonest in the course of running up their debts. In summary, supportive creditor attitudes indicate the existence of relationship resource, whereas unsupportive creditor attitudes indicate the opposite. We should expect that firms with a strong relationship resource will have a better chance of recovering from financial difficulty. This leads to our fifth hypothesis:

H5: CVA success will be positively related to the strength of 'relationship' resources.

In the resource-based view, what matters is not the absolute quantity and quality of resources, but rather the quantity and quality of resources that a firm controls relative to competitors (Hunt, 1997). In addition to resource strengths relative to competitors, resource weaknesses relative to competitors are important. West and De Castro (2001) maintain that resource-based view scholars have tended to focus on resource strengths, but this is one-sided because financial outcomes for the firm will be influenced also by its resource weaknesses and distinctive inadequacies *relative* to its competitors. This leads to the conclusion that poor performance may arise either because the firm has no particular resource strengths and resource weaknesses or where the weaknesses are serious enough to offset any strengths it may possess. This perspective informs our sixth hypothesis:

H6: CVA success will be more likely when the firm has relative resource strength, and less likely when the firm has relative resource weakness.

The final hypothesis relates to a firm which does have at least an adequate resource base, but is pushed into bankruptcy by one or more adverse temporary factors that do not damage this base. The concept of core competence (Prahalad and Hamel, 1990) is pertinent here. Hunt and Morgan (1995) define core competencies as higher-order intangible resources that enable a firm to perform – perhaps better than the competition – activities within its value chain (Porter, 1985). When this ability is unaffected by the cause of bankruptcy, then the firm can be thought of as having an *adequate* resource base before, during and after bankruptcy. For adequate firms that are temporarily pushed into bankruptcy by factors that do not affect their core competence, the CVA allows part of the debt to be written off and the breathing space to recover. Examples of such temporary factors

include a single bad debt and bad luck. Indeed, Storey (2011) has challenged those attempting to explain the performance of small firms to acknowledge more honestly the large role played by chance, with bad luck in one period often being reversed in a succeeding period. This leads to our final hypothesis:

H7: CVA success will be more likely when a factor that does not affect core competence is an important reason for bankruptcy.

Method

Data collection

Data to test the seven hypotheses were collected from a postal questionnaire³ sent to all 1522 names appearing on the HMSO list of licensed insolvency practitioners.⁴ Given the legal restrictions on who can carry out a CVA, the HMSO list is in effect the only sampling frame required for the purposes of this study: 435 replies were received, a response rate of 28.6 percent. Of these, 350 indicated that they had no experience of CVAs and therefore could not complete the questionnaire, itself an interesting finding. In some cases the insolvency practitioner, having conducted more than one CVA, was able to fill in more than one questionnaire, and so our final sample consisted of questionnaires on 97 different CVAs. There is no basis on which to test formally for non-response bias by comparing the composition of the present sample with the population of all CVAs, since information beyond the simple number of CVAs per year is not compiled. However, we do not have any obvious evidence that the sample is biased. In terms of sector membership, the proportion of companies in the sample in construction, manufacturing, distribution and services is similar to the proportion of all bankrupt companies in these sectors. The insolvency practitioners who responded were spread across small, medium and large accounting firms and all areas of the country. The questionnaire was piloted with two experienced insolvency practitioners to check for clarity and relevance in terms of the possible range of causes of bankruptcy asked about, and the reasons why the CVA was attempted.

Given that the CVA was designed for SMEs, we expected that the average company would be small, and indeed this was the case. The median company within the sample had sales revenue of £1.5 million and 20 employees. Mean sales revenue was £3.8 million, and mean employment 54 employees. Of the total debt owed, 20.8 percent was owed to secured creditors, 7.8 percent to preferential creditors and 71.5 percent to unsecured creditors (figures do not sum to 100 due to rounding).

Operationalization of hypotheses

CVA success or failure, the dependent variable, was measured on the basis of the rating given by the insolvency practitioner of the extent to which the CVA plan had been realized. The categories of performance against plan were 'unsuccessful', 'satisfactory' or 'very successful'. This has potential validity problems as it could be subjective – success in the mind of the insolvency practitioner may not equate with more objective notions of success. However, two things reassure of its use. First, a statistical analysis was conducted, which found that success as rated by the insolvency practitioner was strongly correlated with more objective measures of success such as total dividends paid and the proportion of promised dividends paid to preferential and unsecured creditors (secured creditors are almost always promised and paid 100 percent of their debt). Second, a further analysis of a previous cohort of companies in CVAs (Milman and Chittenden, 1995) revealed

that the insolvency practitioner's assessment at the time of the original survey in 1995 was significantly correlated with survival, free of insolvency five years later in 2000.

In terms of variables indicating resource strength or weakness, causes of bankruptcy and reasons for attempting rehabilitation, respondents were asked to rate each possible factor on a Likert scale (ranging from 1 = 'not important' to 5 = 'very important'). Independent variables were coded 1 = 'important' where respondents ranked them as being 'important' or 'very important' in the questionnaire, and as 0 = 'not important' otherwise to economise on degrees of freedom, given the limited sample size. Robustness tests were conducted by adding 'moderately important' cases to the 'important' category and repeating all analyses. In addition, robustness was checked by using alternative groupings of outcomes in the ordered Probit analysis. These robustness tests led to no substantive differences in the results.

The most important indicators of resource weakness were when respondents judged the bankruptcy to have occurred due to poor marketing management, poor human resource management and poor financial management (H2 to H4). In addition, a new variable was constructed which indicated where the company's problems were solely attributable to poor management (H1). This was a dichotomous variable which took the value 1 when any of the specific types of poor management were rated as being either an important or very important reason for the company's bankruptcy, and no other reason was given for the bankruptcy. Also, when it was indicated that the arrival of new management was a reason for attempting the CVA, this was taken to indicate an existing resource weakness in the company.

The strength of relationship resources was measured in terms of the attitudes of each class of creditors. The respondents were asked to rate these attitudes as either positive, neutral or negative (H5). Similarly, to test H6, CVA success was related to the importance attached to increased competition as a cause of a company's bankruptcy, and insolvency practitioners were asked to assess the extent to which companies were able to compete as normal while in the CVA. The existence or otherwise of resource-based strength was inferred from the reasons for implementing the CVA by assessing: (a) shareholders' willingness to commit new capital; (b) the identification of turnaround potential by the supervising insolvency practitioner; and (c) the identification of the company's problems as being temporary.

Finally, variables which might lead to company failure that did not relate to resource weakness (H7) were: (a) the failure of one major contract; (b) one bad debt; (c) sheer bad luck; (d) a general downturn in the market; and (e) adverse macroeconomic conditions.

Control variables

There are a number of important control variables which have been suggested by the literature on small firm success and failure which were worthy of inclusion in this study. In studies examining the relationship between resources and performance, size and age are the two most common, being consistently associated positively with firm survival (Audretsch, 2002; Brush and Chaganti, 1999; Chandler and Hanks, 1994). There are many reasons why size may matter, particularly in the context of firm survival. Larger firms are simply likely to have more resources. Furthermore, they are more likely to have surplus assets that can be disposed of, generating cash. Age too may be associated with the accumulation of resources and learning (Jovanovich, 1982), overcoming the 'liability of newness' (Stinchcombe, 1965). The square and cube of age are included in the full model to allow for a non-linear effect of age on the likelihood of survival. Very young firms are particularly vulnerable, and it is well understood in the literature that chances of survival improve with age, but

do so at a diminishing rate. This may lead plausibly to an S-shaped relationship best modelled with a cubic functional form. The strong correlation between age, age-squared and age-cubed will lead to the separate effects of these three variables being confounded, but should not lead to more general problems of multicollinearity in the rest of the model (as indicated by stable coefficients between the full and restricted models).

In terms of industry membership, although SME survival, failure and turnaround rates are found to vary from one sector to another, the differences are relatively insignificant. This is in line with the resource-based view, which is predicated on the assumption that variability in performance is greater within industries than between them. Nevertheless, dummy variables are used to account for the broad type of activity in which the firm was engaged.

Three further control variables, not addressed in the literature, are whether or not the CVA is carried out in conjunction with another bankruptcy procedure, the experience of the insolvency practitioner charged with implementing the CVA and the size of the company to which the insolvency practitioner belongs. First, regarding these further control variables, one important feature of UK bankruptcy law is that it provides for a CVA to be carried out in conjunction with an administration order, as well as allowing each procedure to be carried out independently. The administration order provides far greater powers of control and investigation to the insolvency practitioner as well as providing a strong moratorium against hostile creditor actions. With an administration order, the insolvency practitioner has the important power to dismiss and appoint directors. Therefore, one would expect that CVAs conducted in conjunction with an administration order would be more likely to succeed, since the insolvency practitioner has a better chance to assess the prospects of the company and to remedy any senior management deficiencies. Second, the simple expectation is that the more experienced the insolvency practitioner, the higher the probability of a successful outcome. By the same token, one might expect the larger the accounting firm to which the insolvency practitioner belongs to be positively correlated with CVA success, as the insolvency practitioner will have a greater wealth of expertise within the firm from which to draw.

Results

The ordered Probit analysis results are presented in Table 1. Table 2 presents the correlation matrix and Table 3 provides the key to the variables in that matrix. The correlation matrix shows that, with the exception of age, age-squared and age-cubed, there are no worrying large correlations between the independent variables.

The results shed considerable light on the central proposition and hypotheses. Both the full and restricted models are highly significant. In the latter, nine independent variables are statistically significant at conventional levels. Comparison of the coefficients between the full and restricted models reveals stability in most of the coefficients. The full model was tested down to the restricted model by eliminating those variables which appeared least significant based on *t*-ratios or extant theory. These variable deletions were data admissible as evidenced by a likelihood ratio test. As a robustness check, the sequence of deletions was altered. This had no effect on the principal conclusions reported below.

Poor management as a sole cause of a company's problems took a counterintuitive positive sign. However, this was entirely due to collinearity with the three variables indicating problems with marketing, human resource management and financial management. Without these three variables, the sign switches to being negative as expected, although not significant. The difficulty experienced in CVAs of dealing with poor management is underscored by the negative coefficient on new

Table 1. Ordered Probit Analysis Results*

Variable	Full Model		Restricted Model	
	Coeff.	t-ratio	Coeff.	t-ratio
Poor management was the sole major cause of the bankruptcy	0.357	0.331		
Poor marketing management was an important cause of the bankruptcy	-2.618	-1.451	-1.960	-1.750*
Poor human resource management was an important cause of the bankruptcy	-0.962	-0.467	-0.732	-0.666
Poor financial management was an important cause of the bankruptcy	-0.560	-0.539	-0.353	-0.972
The arrival of new management was an important reason for the CVA	-0.833	-0.648	-0.767	-1.073
Secured creditors were supportive of the CVA	-0.154	-0.150		
Preferential creditors were supportive of the CVA	0.251	0.401		
Unsecured creditors were supportive of the CVA	1.541	1.277	1.391	2.440**
Increased competition was an important cause of the bankruptcy	-1.241	-1.322	-1.363	-2.186**
A general demand in decline for the company's type of product was an important cause of the bankruptcy	1.180	1.160	0.852	1.635
The company had difficulty acting as a normal competitor due to the CVA	1.723	1.543	1.086	1.926*
The company's turnaround potential was an important reason for the CVA	1.059	0.707	1.052	1.924*
The fact that the company's problems were temporary in nature was an important reason for the CVA	0.192	0.173		
Shareholders willing to invest additional funds was an important reason for the CVA	0.108	0.066		
A single bad debt was an important cause of the bankruptcy	0.317	0.154		
The failure of one big project was an important cause of the bankruptcy	0.709	0.957		
Bad luck was an important cause of the bankruptcy	0.452	0.225	1.004	0.875
Poor macroeconomic conditions were an important cause of the bankruptcy	-0.870	-0.684		
Failure of another company was an important cause of the bankruptcy	-0.280	-0.176	-1.019	-0.988
Problems with a major contract was an important cause of the bankruptcy	-0.768	-0.617		
Amount of debt owed to secured creditors	-0.0003	-0.741	-0.0001	-0.709
Amount of debt owed to preferential creditors	0.0007	0.237		
Amount of debt owed to unsecured creditors	0.0001	0.561		
Age of the company	0.182	0.872	0.026	2.238**
Age ²	-0.007	-0.868		
Age ³	0.00007	0.895		
Firm belongs to manufacturing sector	0.250	0.180		

Table I. (Continued)

Variable	Full Model		Restricted Model	
	Coeff.	t-ratio	Coeff.	t-ratio
Firm belongs to distribution sector	-0.475	-0.374		
Firm belongs to service sector	-1.117	-0.779	-0.980	-2.169**
CVA done in conjunction with administration order	-0.571	-0.775		
The IP's accounting practice has between 10 and 50 partners	2.663	1.816*	1.617	3.866***
The IP's accounting practice has more than 50 partners	3.105	2.129**	2.016	3.643***
Years of experience of the insolvency practitioner	0.016	0.465		
The IP's accounting practice has supervised between 5 and 25 CVAs	0.052	0.052		
The IP's accounting practice has supervised more than 25 CVAs	-1.132	-0.743		
The major purpose of the CVA was to rehabilitate the company	-0.302	-0.345	-0.374	-0.760
CONSTANT	-1.983	-0.968	-0.964	-1.524
Log-Likelihood	-45.036		-51.083	
χ^2	74.780***		62.685***	
% correct predictions	71		71	
LR test of restriction $\chi^2(19)$			12.095	

***indicates significant at 1% ** significant at 5% and * significant at 10%

or improved management being an important rationale for attempting the CVA. Therefore, there is support for H1. The three management failings all emerge with negative signs as expected, with poor marketing emerging as the strongest influence, significantly reducing the chances of a successful CVA. The influence of problems of financial management on the chances of success was stronger than that of problems with human resource management in all specifications. Therefore, this evidence supports H2 to H4.

Regarding creditor attitudes, the results indicate that chances of success are significantly higher where unsecured creditors are supportive of the CVA. Interestingly, support from secured and preferential creditors is not influential. A somewhat different picture emerges when the dummy indicating supportive creditor attitudes is replaced by one indicating unsupportive creditor attitudes (not reported in the table). Here, it is unsupportive secured creditors who exert the most important and significant negative influence on chances of a successful outcome. Overall, the evidence supports H5.

The importance of the relative position of the company, which is the basis of H6, is indicated by the significant influence of increased competition as a cause of the company's problems. Furthermore, the positive – and in some specifications significant – coefficient on the variable indicating that the company's problems stemmed from a general decline in demand, indicates that prospects are less impaired by general difficulties facing all companies than where difficulties stem from a disadvantage relative to rivals. The fact that poor marketing management has a consistently negative coefficient is also consistent with H6, as poor positioning in the market will place a

Table 2. Correlation Matrix

	Secure	Pref	Unsec	Age	Age ²	Age ³	Length	Rehab	Purebad	Part1050	Part50	Cva25	Difdebt	Difecon	Difprod	Difcomp	Difproj	Difpro
Secure	0.097																	
Pref	0.703 ¹	0.503 ¹																
Unsec	0.251 ²	0.061	0.160															
Age	0.217 ³	0.007	0.085	0.940 ¹														
Age ²	0.194 ³	-0.007	0.059	0.870 ¹	0.984 ¹													
Age ³	0.018	-0.047	0.090	-0.064	-0.084	-0.093												
Length	0.141	0.145	0.020	0.136	0.190 ³	-0.206 ²	-0.284 ¹											
Rehab	0.032	0.253 ²	0.075	-0.020	0.034	0.068	0.106	-0.092										
Part1050	-0.003	-0.064	-0.063	-0.128	-0.150	-0.144	0.054	-0.180	0.163									
Part50	0.207 ³	0.195 ³	0.282 ²	0.108	0.089	0.083	-0.011	-0.032	-0.071	-0.511 ¹								
Cva25	0.257 ²	0.206 ³	0.317 ¹	0.157	0.176	0.191 ³	0.100	-0.106	0.219 ³	0.151	0.399 ¹							
Difdebt	-0.000	0.028	-0.012	-0.081	-0.072	-0.066	-0.128	0.269 ²	-0.117	-0.054	0.223 ²	0.185						
Difecon	0.018	-0.009	-0.054	0.079	0.083	0.082	-0.334 ¹	0.130	-0.162	0.118	0.044	-0.003	0.233 ²					
Difprod	-0.026	-0.078	-0.072	0.072	0.025	-0.014	-0.150	-0.215 ³	-0.218 ³	-0.030	0.082	-0.179	-0.128	0.129				
Difcomp	-0.038	-0.087	-0.142	0.167	0.136	0.101	-0.238 ²	-0.229 ²	-0.200 ³	-0.138	0.000	-0.196 ³	-0.117	0.054	0.393 ¹			
Difco	-0.102	-0.045	-0.024	-0.090	-0.066	-0.062	0.102	-0.046	-0.117	-0.169	0.223 ³	0.185	0.145	0.069	-0.128	-0.117		
Difproj	0.087	-0.040	0.091	-0.097	-0.092	-0.093	-0.005	0.175	-0.218 ³	-0.030	0.015	0.018	0.005	0.027	-0.073	-0.218 ³	-0.128	
Difpro	0.081	0.149	0.056	-0.114	-0.073	-0.045	0.081	0.204 ³	0.410 ¹	0.222 ³	-0.157	0.163	0.001	-0.047	-0.197 ³	-0.082	-0.106	0.136
Difhrrm	0.078	-0.012	0.022	0.002	0.003	-0.020	0.166	-0.185	-0.000	0.235 ²	-0.030	-0.067	-0.076	0.046	-0.019	0.129	-0.076	-0.019
Difcontr	-0.104	-0.066	0.126	0.132	0.189 ³	0.216 ³	-0.092	0.252 ²	-0.200 ³	0.013	-0.071	-0.081	0.023	0.162	-0.131	-0.108	-0.117	0.131
Difluc	-0.089	-0.006	0.025	-0.118	-0.075	-0.056	-0.009	0.072	-0.089	0.017	0.116	-0.046	0.222 ³	-0.072	-0.098	-0.089	-0.052	0.241 ²
Attsec	0.249 ²	0.148	0.207 ³	0.431 ¹	0.296 ¹	0.255 ²	-0.207 ³	0.232 ²	-0.115	0.012	-0.020	-0.152	0.046	0.272 ²	0.280 ²	0.092	-0.164	-0.045
Attunsec	0.193 ³	0.122	0.186	0.374 ¹	0.303 ¹	0.254 ²	0.039	0.155	-0.195 ³	-0.287 ²	0.065	-0.072	-0.066	0.222	0.073	0.149	-0.171	0.138
Whyhrrm	0.199 ³	0.066	0.151	0.186	0.145	0.121	-0.106	0.189 ³	-0.329 ¹	-0.357 ¹	0.095	-0.317 ¹	-0.014	0.064	0.143	0.120	-0.014	0.059
Whyhrrm	-0.128	-0.056	-0.138	0.018	0.055	0.078	0.144	0.046	0.446 ¹	0.088	-0.141	0.150	-0.117	-0.054	-0.218 ³	-0.015	-0.117	-0.131
Whyhrrmp	0.054	0.244 ²	0.055	-0.014	0.013	0.024	-0.069	0.480 ¹	-0.030	-0.083	0.111	-0.019	0.150	0.249 ²	-0.143	-0.120	0.014	0.196 ³
Whyhrrm	0.111	0.034	0.075	-0.015	-0.026	-0.044	-0.100	0.262 ²	-0.038	0.059	-0.094	0.035	0.257 ²	0.407 ¹	-0.165	-0.151	0.084	0.157
Whyhrrm	0.024	0.134	-0.056	0.031	0.149	0.210 ³	-0.210 ³	0.693 ¹	-0.036	-0.057	-0.132	-0.115	0.140	0.159	-0.150	-0.036	-0.080	-0.013
Admin	0.030	0.172	0.280 ²	-0.125	-0.190 ³	-0.190 ³	0.277 ³	0.320 ¹	0.129	0.164	0.166	0.321 ¹	-0.213 ³	-0.211 ³	0.003	-0.082	0.108	0.069
Manu	-0.150	-0.034	-0.095	-0.153	-0.174	-0.120	0.045	-0.038	0.224 ²	0.117	-0.242	0.125	0.052	-0.067	-0.184	-0.149	-0.061	-0.043
Dist	-0.013	-0.084	0.056	0.046	-0.006	-0.042	0.136	-0.195 ³	-0.254 ²	0.117	0.165	-0.212 ³	-0.149	-0.111	0.254 ²	0.307 ¹	0.095	0.026
Serv	0.257 ²	-0.062	0.075	0.185	0.270 ¹	0.297 ¹	0.032	0.301 ¹	0.025	-0.093	0.149	0.236 ²	0.185	0.130	-0.089	-0.204 ³	0.069	0.056
Difop	0.038	0.145	-0.004	-0.154	-0.127	-0.120	0.035	-0.041	0.255 ²	0.095	0.090	0.236 ²	-0.048	-0.048	0.056	-0.051	0.069	0.056

Table 2. (Continued)

	Diffinma	Diffrm	Difconr	DiflucK	Attsec	Attpref	Attunsec	Whynma	Whytemp	Whyinv	Whyturn	Admin	Manu	Dist	Serv
Secure															
Pref															
Unsec															
Age															
Age ²															
Age ³															
Length															
Rehab															
Purebad															
Part1050															
Part50															
Cva25															
Difdebt															
Difecon															
Difprod															
Difcomp															
Difco															
Difproj															
Diffinma															
Diffrm	-0.038														
Difconr	-0.152	-0.129													
DiflucK	-0.162	0.192 ³	-0.089												
Attsec	-0.047	-0.007	0.023	0.062											
Attpref	-0.068	0.082	0.149	-0.077	0.410 ¹										
Attunsec	-0.235 ²	0.010	-0.060	0.094	0.279 ²	0.359 ¹									
Whynma	0.410 ¹	-0.000	-0.015	-0.089	-0.046	-0.057	-0.418 ¹								
Whytemp	0.098	-0.135	0.239 ²	0.080	0.189 ³	0.043	-0.129	0.060							
Whyinv	0.244 ²	0.220 ³	0.189 ³	-0.068	0.160	-0.017	-0.062	0.189 ³							
Whyturn	0.290 ¹	-0.210 ³	0.325 ¹	-0.146	0.170	0.098	0.059	0.108	0.172	0.109					
Admin	0.036	-0.234 ²	-0.152	-0.026	-0.204 ³	-0.120	-0.166	0.059	0.502 ¹	-0.188 ³	-0.205 ³				
Manu	0.196 ³	-0.192 ³	0.149	-0.133	-0.128	-0.034	-0.267 ²	0.373 ¹	-0.039	0.141	-0.135	0.196 ³			
Dist	-0.217 ³	-0.052	-0.254 ²	0.042	-0.044	0.001	0.188 ³	-0.174	-0.032	-0.192 ³	-0.162	0.149	-0.378 ¹		
Serv	-0.102	0.033	0.025	0.023	0.098	0.139	0.145	-0.127	0.152	0.070	0.263 ²	-0.160	-0.418 ¹	-0.356 ¹	
Difop	0.248 ²	-0.074	0.025	-0.125	-0.244 ²	-0.260 ²	-0.277 ²	0.373 ¹	0.078	0.164	0.023	0.248 ²	0.076	-0.024	-0.076

¹ indicates significant at 1%; ² indicates significant at 5%; ³ indicates significant at 10%

Table 3. Key to Variables in the Correlation Matrix

Variable	Variable description
Secure	Amount of debt owed to secured creditors
Pref	Amount of debt owed to preferential creditors
Unsec	Amount of debt owed to unsecured creditors
Age	Age of the company
Age ²	Age ²
Age ³	Age ³
Length	Years of experience of the insolvency practitioner
Rehab	The main purpose of the CVA was to rehabilitate the company
Purebad	Poor management was the sole major cause of the bankruptcy
Part1050	The IP's accounting practice has between 10 and 50 partners
Part50	The IP's accounting practice has more than 50 partners
CVA25	The IP's accounting practice has supervised more than 25 CVAs
Difdebt	A single bad debt was an important cause of the bankruptcy
Difecon	Poor macroeconomic conditions were an important cause of the bankruptcy
Difprod	A general demand in decline for the company's type of product was an important cause of the bankruptcy
Difcomp	Increased competition was an important cause of the bankruptcy
Difco	Failure of another company was an important cause of the bankruptcy
Difproj	The failure of one big project was an important cause of the bankruptcy
Diffinma	Poor financial management was an important cause of the bankruptcy
Difhrm	Poor human resource management was an important cause of the bankruptcy
Difcontr	Problems with a major contract was an important cause of the bankruptcy
Difluck	Bad luck was an important cause of the bankruptcy
Attsec	Secured creditors were supportive of the CVA
Attpref	Preferential creditors were supportive of the CVA
Attunsec	Unsecured creditors were supportive of the CVA
Whyhma	The arrival of new management was an important reason for the CVA
Whytemp	The fact that the company's problems were temporary in nature was an important reason for the CVA
Whyinv	Shareholders willing to invest additional funds was an important reason for the CVA
Whyturn	The company's turnaround potential was an important reason for the CVA
Admin	CVA done in conjunction with administration order
Manu	Firm belongs to manufacturing sector
Dist	Firm belongs to distribution sector
Serv	Firm belongs to service sector
Difop	The company had difficulty acting as a normal competitor due to the CVA

company at a competitive disadvantage. These findings make sense, as CVAs were simply not designed to deal with this kind of strategic failure. Accordingly, H6 is also supported.

Where turnaround potential was an important reason for the CVA, success is more likely, significantly so in the restricted model. The fact that the company's problems were temporary in nature and that the shareholders were prepared to invest additional funds were also positive influences, as expected. Those causes of failure which did not imply a company's resource weakness generally took positive signs, as expected. A general decline in demand for the type of product that

the company sold was positive and not far from significance in the restricted model. Overall, there is clear support for H7.

Regarding the control variables, there is little evidence that size (proxied by debt owed to creditors) is a significant influence on chances of success, yet neither does it appear to exert a counter-intuitive influence. In the full model, none of the polynomial terms for age are close to statistical significance due to a high degree of collinearity. When the squared and cubed terms are removed, age emerges as a positive and significant influence on the chance of success. The industry sector dummies for manufacturing and distribution were a long way from statistical significance, therefore there is no meaningful difference between chances of success for companies in these sectors compared to the default category of construction. Companies in the service sector emerge as having significantly lower chances of success.

The size of the accounting practice to which the insolvency practitioner belongs is a positive and significant influence on the chances of success, while the insolvency practitioner's years of experience is positive but not significant. Very interesting is the result that where a large number of CVAs had been previously managed by the insolvency practitioner's firm, the chances of success were lower. One possible interpretation of this result is gained from a discussion with a senior insolvency practitioner who complained of a small number of 'cowboy' insolvency practitioner firms that oversold the CVA as a panacea.

Discussion

It is clear that where problems are due to poor management, then the chances of successful delivery of the CVA plan are lower. This reflects the difficulties of correcting poor management within the CVA, where the debtor remains in possession and the CVA supervisor has no powers to direct management or investigate the company (Mokal, 2004). The singular importance of the quality of management within SMEs is entirely consistent with the resource-based view (Rouse and Daellenbach, 1999).

The utility of the resource-based framework is also attested to by the support for H2, H3 and H4, which indicate that companies with important resource weaknesses are unlikely to be associated with a successful CVA process. Resource weaknesses that leave the company at a competitive disadvantage relative to rivals (H6) are particularly problematic, while strong relationship resources in terms of relationships with key creditors (H5) emerge as having a fundamental bearing on chances of success within a CVA. Ultimately, we find that a successful outcome following bankruptcy is likely when a company has resource *strength* and became bankrupt for *non-resource* related reasons (H7). Accordingly, we find strong support for this study's central proposition, that a firm which has resource strength or lacks resource weakness but is pushed into bankruptcy by adverse temporary factors will be more likely to succeed in a CVA.

The findings that a resource weakness is negatively associated with the prospects of success, and resource strength positively associated, fits with the broader findings on the success and failure of entrepreneurial firms (Audretsch, 2002). Strategic posture has been found to have an influence on the likelihood of survival and success rates of small firms, typically measured either by growth or profitability (Lussier and Pfeifer, 2000). In addition to strategic posture, a range of operational factors have been proposed as bearing some relationship to chances of survival: financial management (Peterson et al., 1983), product or marketing management (Gartner et al., 1999) and human resource management (Lussier and Pfeifer, 2000). The present results are consistent with this literature. The association between age and survival is also well established in the broader literature (Everett and Watson, 1998).

Conclusion

In summary, the consistency of the present findings with the existing literature on SME success and failure provides additional validation for the utility of the resource-based view for considering these issues. The resource-based view has the advantage of providing an overarching conceptual framework within which this body of work can be interpreted, and one which can guide future research. The article has also widened both the resource-based view and the literature on entrepreneurial success and failure by addressing the under-researched question of the turnaround of bankrupt SMEs.

What does this evidence imply about the utility of the government's attempts to use bankruptcy law reform to promote entrepreneurship? First, the procedure does allow the problems of bankrupt SMEs to be addressed, resulting in good rates of business survival, and orderly liquidation in those cases where the firm cannot be saved. Thus CVAs can help to avoid failure or, if not, mitigate its effects. A series of R3/SPI surveys (formerly Society of Practitioners of Insolvency; Weisgard et al., 2010) have shown the CVA to outperform other bankruptcy regimes in terms of business survival, preservation of employment and debt recovery by creditors. To that extent, the CVA deserves to be more strongly promoted. One aspect which is particularly important is that CVAs pay better returns to trade creditors than other types of regime, thus helping to avoid a 'domino effect' where the failure of one firm can lead to the failure of its suppliers (Weisgard et al., 2010). Nevertheless, policymakers (and indeed insolvency practitioners) should be realistic. The CVA is not – and neither could it be – a panacea.

In terms of specific implications, the nature of a debtor-in-possession regime requires careful consideration. The results presented here indicate that such a regime can work well when the firm is viable, but can present problems when the firm is not viable. For an SME the main resource, and therefore the factor on which viability hinges, is the quality of its management. When management quality is good, a CVA will be appropriate and preferable to a management displacement regime, since the evidence shows that debtor-in-possession regimes involve significantly lower costs than management displacement regimes such as receivership (Thorburn, 2000). Designing a bankruptcy procedure which is capable of correcting senior management and strategic deficiencies would appear to be extremely difficult.

What are the implications for entrepreneurs or would-be entrepreneurs? This research indicates that poor management, in particular poor marketing management, failing to keep up with the competition and poor financial management are all associated with lower degrees of CVA success. These can all be influenced by the entrepreneur: for example, through appropriate training or taking professional advice and being vigilant about competitive position (Brush et al., 2001). The research also indicates the importance of managing customer and supplier relationships. The attitude of creditors can make or break an attempt at survival (Cook et al., 2001). The evidence regarding poorer chances of success where the cause of the firm's financial problems was the failure of another firm, or problems with a major contract, support the traditional advice to avoid over-reliance on a single customer. Additionally, the quality of the insolvency practitioner has been seen to influence outcomes, therefore entrepreneurs need to choose their advisers with care.

Recommendations for future research

This research was based on broad measures of resources and not on in-depth research carried out within the organization, where many complex resources reside (Rouse and Daellenbach, 1999). The article suggests from both a theoretical and empirical standpoint that the resource-based view is a useful and potentially powerful framework for explaining the success and failure of SMEs. In

so doing, it responds to the call for further theoretical development in the otherwise mature general topic of picking winners (Blackburn and Kovalainen, 2009), and builds on the small but growing body of literature that is advancing the use of the resource-based view within the field of SMEs and entrepreneurship.

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Notes

1. In the UK the correct term to apply to companies is insolvency and in this case, 'technical insolvency' – when the company is unable to pay its debts on time. Bankruptcy applies only to individuals. However, throughout this article the more usual international term 'bankruptcy' is used. Similarly, when referring to the dissolution of a company, the international term 'liquidation' is preferred.
2. Initially, larger companies were not included because, having access to greater resources, they are more able to resolve financial difficulties through non-legal informal arrangements, and so were less needy of legislative reform than SMEs.
3. The research instrument is available on request from the corresponding author.
4. Over the time period relating to the current sample these agencies were separate – the Inland Revenue and HM Customs & Excise – they are unified now as HM Revenue & Customs.
5. An insolvency practitioner is authorized to implement a bankruptcy proceeding.

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