Title: A Taxonomy of Distinctive Explanatory Business Failure Patterns amongst Small Firms: A Qualitative Approach

Abstract: Whereas it is obvious that the failure process can vary from one firm to another (Argenti, 1976; D'Aveni, 1989; Laitinen, 1991), to date, few researchers have worked on the detection of several (explanatory or subsequent) failure patterns. In addition, none of the reviewed research really focuses on small firms while their failure is important and particular (Haswell and Holmes, 1989). Considering these observation and on the basis of an abductive and qualitative analysis (Thiétart, 2003), this paper identifies, among a sample of 208 small distressed firms, a taxonomy of five explanatory business failure patterns, i.e. five homogenous groups of small firms on the basis of the reasons for their failure. As the detection of the fundamental explanatory failure factors is the basis of failure prevention (Argenti, 1976), the identification of these patterns is of crucial importance for a better understanding and for a better prevention of this phenomenon amongst small businesses.
Introduction

Small firms are crucial actors in the world economy (Keasey and Watson, 1991). Small and medium-sized businesses compose more than 99% of the total population of firms in the U.S. (Birch, 1987) and in Europe (OECD, 2005). More locally, in 2007, small firms composed 91% of the total population of firms in Belgium (Graydon, 2009). These firms generate job creation and they largely contribute to the economic development of these areas (Keasey and Watson, 1987; Keats and Bracker, 1988; OECD, 2005).

Nevertheless, as numerous studies have demonstrated it in various countries, it is now an evidence that the small business sector has at its base a great volatility, i.e. “a foundation of massive, continual failure” (Birch, 1987; Bates and Nucci, 1989). Whatever the country in which it is analyzed (USA, UK, France, Finland, Belgium, etc.), the failure rate of small firms is high (Keasey and Watson, 1987; Haswell and Holmes, 1989; Unizo, 2007) and it is much more important than the failure rate of large firms.

The failure of small firms is not only considerable, it is also particular compared to the failure of larger firms. Indeed, small firms are not simply smaller versions of large ones (Keats and Bracker, 1988; Hall and Young, 1991) : they have particular characteristics such as a small resource base or a strong dependence towards one individual (Robinson and Pearce, 1984; Keasey and Watson, 1987; Julien, 2005). Considering these specificities, it is thus reasonable to assume that they are confronted to different problems than larger entities are and that they respond differently to them. In other words, small firms do not necessarily enter a failure process for the same reasons as large firms do and they do not evolve similarly in a failure process.

In this context, it would be judicious to identify the (specific) causes of small business failure and, then, to propose a series of explanatory failure patterns dedicated to small business in order to better prevent this phenomenon. Nevertheless, an extensive review of the literature on business failure prevention (Auteure and Auteur, 2008; Auteure, 2009) leads to the conclusion that, up to now, there is no published scientific research that presents a typology (or a taxonomy) of explanatory business failure patterns (EBFPs) dedicated to small firms. Actually, the previous studies which propose several EBFPs are either general (Malecot, 1981; Masuch, 1985) or they focus on large firms (D'Aveni, 1989; Miller, 1992; Moulton et al., 1996).

Based on these observations and on a conceptual model proposed by Auteure and Auteur (2008), the present study gathers empirical evidence on distinctive explanatory business failure patterns amongst small firms. As briefly mentioned above, as the detection of the fundamental explanatory failure factors is the basis of failure prevention (Argenti, 1976), the identification of distinctive explanatory business failure patterns, which would differentiate small firms according to the reasons why they fail, is of crucial importance for a better understanding and for a better prevention of this phenomenon.

1. Organization for Economic Co-operation and Development
2. Firms with 50 workers or less (European Commission, 2003)
3. For example, in Belgium, more than 99.5% of the firms that went bankrupt between 1996 and 2008 were small firms (Unizo, 2007; Graydon, 2009).
4. Nevertheless, even if very small firms generally represent the bulk of failure, it is worth mentioning that a study carried out by the European Observatory for SMEs in 1997 shows that, in 1993, very small firms (with less than 9 workers) seem to be more resistant to insolvency than small enterprises (between 10 and 49 workers). Indeed, their proportion among insolvent and liquidated firms is consistently lower than their share in total firm population.
Concretely, on the basis of an abductive and qualitative analysis (Thiétart, 2003), this paper identifies, among a sample of 208 small distressed firms, a taxonomy of five EBFPs, i.e. five homogeneous groups of small firms on the basis of the reasons for their failure. These five main EBFPs are themselves detailed into several sub-patterns.

Concretely, the present paper is organized into five main sections. The first section is dedicated to a clarification of the key concepts that are used in the present research whereas the second section briefly summarizes the results of previous research on explanatory business failure patterns. Then, the third section describes the methodology used to induce the taxonomy: the sample of distressed firms, the data collection and the data analysis methods used in the present research are presented. The fourth section is dedicated to the presentation of the results of the qualitative analysis: the five distinctive EBFPs are exposed into details. Finally, the last section proposes a discussion of the results on the basis of previous literature.

1. Clarification of key concepts

1.1. The concept of small firm

The definition of small firm on which the present study is based is the one adopted by the European Commission in 2003, which is effective since January 1, 2005 (see Table 1).

<table>
<thead>
<tr>
<th>Firm category</th>
<th>Personnel</th>
<th>Turnover</th>
<th>OR</th>
<th>Balance Sheet total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medium-sized</td>
<td>&lt; 250</td>
<td>&lt;= € 50 million</td>
<td>&lt;= € 43 million</td>
<td></td>
</tr>
<tr>
<td>Small</td>
<td>&lt; 50</td>
<td>&lt;= € 10 million</td>
<td>&lt;= € 10 million</td>
<td></td>
</tr>
<tr>
<td>Micro</td>
<td>&lt; 10</td>
<td>&lt;= € 2 million</td>
<td>&lt;= € 2 million</td>
<td></td>
</tr>
</tbody>
</table>

Table 1: Definition of SMEs (European Commission, 2003)

Previous literature shows that small firms have specific characteristics (Keats and Bracker, 1988; Julien, 2005), which make them particularly vulnerable and which have an impact on why they do fail (Birch, 1987).

Mintzberg (1979) and Julien (2005) summarize the most common characteristics of small firms as follows:

- These firms are organizations of “small size”. Referring to the resource-based theory of the firm (Wernerfelt, 1980; Barney, 1991), the quantity of available resources (immaterial, human, technical and financial resources) in these firms is thus small compared to larger firms.
- In most of the cases, the power is centralized in the hands of ONE entrepreneur: the chief executive or the owner himself (Mintzberg, 1979). Small businesses are thus generally under the preponderant influence of one individual who is at the center of the firm (Mintzberg, 1979; Keats and Bracker, 1988; Julien, 2005): organizational activities largely depend on the personal tastes, experiences and competences of this individual who is able to control other agents within the firm by direct supervision and who is generally responsible for

5 or one small circle of people such as couples, families or partners (Chowdhury and Lang, 1993; Lambrecht and Pirnay, 2008)
the various aspects of the management of the firm (strategic, commercial, operational, financial aspects, etc.).

- Due to their small size, these organizations are 'structurally simple' in Mintzberg (1979) sense:
  - There is at most a loose division of labor, a small managerial hierarchy and hardly any formalization of behaviors and activities (Preisendörfer and Voss, 1990).
  - The strategy is intuitive and/or little formalized.
  - The internal and external information-systems are relatively simple. There is no formal and written mechanism to transfer internal or external information: the entrepreneur directly discusses with workers, customers, bankers, etc.
- The firm has less power vis-a-vis customers and competitors compared to larger counterparts (Keats and Bracker, 1988). It is thus particularly dependent on its external and evolving environment.

1.2. The concept of business failure

As recognized by many authors, a clear and generally-accepted definition of the concept of business failure does not exist in the literature (Sharma and Mahajan, 1980; Koenig, 1985; Guilhot, 2000).

Most commonly, a narrow and financial definition of this concept is used as well by researchers as by practitioners. Business failure is then strongly related to financial distress and a failing firm is often defined as a firm that can not meet its financial obligations (Malecot, 1981; Morris, 1997). However, this definition only concentrates on the financial consequences of more fundamental problems and it does not integrate the early stages of failure (Weitzel and Jonsson, 1989). Therefore, in a preventive perspective, a broader definition of failure is necessary in order to understand and explain why (causes) and how (process) firms do fail.

In the present research, business failure is then defined as follows (see Auteure and Auteur, 2009):

Failure occurs when, because of some fundamental problems (such as a lack of managerial competences or a technological change), there is a misalignment of the firm to the environment's realities and when, under these circumstances, the firm can not create or sustain a viable strategic position on its market (Greenhalgh, 1983; Weitzel and Jonsson, 1989).

Once entered in a failure process, if no corrective actions are taken, the failing firm evolves in a downward spiral (Hambrick and D'Aveni, 1988): its organizational, and later its financial, situation deteriorates more and more.

This failure process eventually ends up with the bankruptcy of the firm if the solvency and liquidity ratios are critically affected. Other (negative or positive) issues are also possible: companies involved in an economic failure process may disappear through different ways (such as a bankruptcy, a liquidation or a merger (Balcaen and Ooghe, 2007)) but they may also recover if the adequate corrective actions are taken within the firm.

1.3. The concept of (explanatory) failure patterns

Even if common stages can be identified in the failure process of each firm, some researchers as Argenti (1976), D'Aveni (1989) and Laitinen (1991) argue that all firms do not enter a failure process for the same fundamental reasons and that they do not behave the same way when they are engaged in a failure process. Considering this scientific observation, different failure patterns can thus be distinguished amongst failing firms, notably according to some of their inherent characteristics, such as their age (Thornhill and Amit, 2003) or their size (Hambrick and D'Aveni, 1988).
Nevertheless, even if the term “failure patterns” has already been used by several researchers such as Moulton and Thomas (1996) or Thornill and Amit (2003), they have not clearly defined this concept in their research. In addition, various terms such as failure syndromes (Miller, 1977) or failure scenario’s (Malecot, 1981) are used in previous literature as synonyms of patterns. As this concept is not commonly defined in previous studies, it is therefore necessary to clarify how it is perceived in the current research. With reference to the definition proposed in the “Merriam-Webster” dictionary, the term “business failure patterns” refers to homogeneous sets of traits, acts, tendencies or characteristics which significantly portray firms along the failure process.

As the present research concentrates on the causes of small business failure, it proposes thus to identify several typical explanatory business failure patterns (dedicated to small firms): homogeneous sets of traits, acts, tendencies or characteristics which fundamentally explain small business failure.

2. Literature Review

An extensive review of the literature on business failure prevention (Crutzen, 2009) points out eight studies that propose a series of distinctive explanatory business failure patterns. As mentioned in the Introduction, none of them concentrates on small firms, as the present study does. They are either general or they focus on large business failures (Miller, 1992; Moulton et al., 1996).

Table 2 summarizes the findings of these previous studies that appear to be transferable to small firms by considering their intrinsic characteristics (such as described by Julien et al. (2005)). On the basis of these studies, this table highlights the five typical patterns which could explain small business failures.

<table>
<thead>
<tr>
<th>Poor performing firms that never succeed</th>
<th>Rapid expansion</th>
<th>Late(r) expansion</th>
<th>External events</th>
<th>Lack of progressive adaptation or missed adaptation to the environment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argenti (1976)</td>
<td>Young firms that never get off the ground (Type 1)</td>
<td>Firms that fail after a rapid over-expansion or precipitous growth (Type 2)</td>
<td></td>
<td>Mature firms which become progressively misaligned with their environment (Type 3)</td>
</tr>
<tr>
<td>Miller (1977)</td>
<td>Impulsive syndrome (1)</td>
<td></td>
<td></td>
<td>Stagnant bureaucracy (2)</td>
</tr>
<tr>
<td>Malecot (1981)</td>
<td>Poor performing firms that are outdated (1)</td>
<td>Firms that fail because of the unbalanced growth of their financial structure (4)</td>
<td>Firms which are too dependent on a client, a supplier, etc. (2)</td>
<td>Poor performing firms that are outdated (1) AND Firms which have adapted too late or inadequately to their environment (3)</td>
</tr>
</tbody>
</table>

6 With reference to the “Merriam-Webster” dictionary, a pattern is “a reliable set of traits, acts, tendencies or other observable characteristics which significantly portray a person, group or institution”.

7 As they are dedicated to large firms or to the consequences of failure, the other two patterns presented by Miller (1977) cannot be used to explain small firms’ failure.
To conclude this first section, on the basis of previous literature, we have identified five patterns which could explain small business failures. These are:

1. Poor performing firms that never succeed
2. (Young) firms that fail after a rapid expansion
3. (Older) firms that fail after expansion
4. Firms that fail after an external event
5. Firms that have not adapted (adequately) to their (changing) environment

With reference to the principles of the abductive reasoning (Thiéart, 2003), we are now going to induce EBFPs from the ground and we will then compare our empirical results with this five typical patterns, which emerge from previous literature. We will then have the opportunity to determine if our empirical findings are consistent with previous research and if they provide some new interesting insights regarding EBFPs amongst small firms.

3. Methodology

3.1. Sample of distressed firms

The selection of a (large) sample of distressed firms and the gathering of information about the reasons for their failure are real challenges. On the one hand, it is difficult to isolate a population (and then a sample) of distressed firms that are different from bankrupt or death firms (Haswell and Holmes, 1989). Indeed, it is possible to observe legal bankruptcies from Court records with reasonable accuracy but it is much more difficult to isolate distressed firms on the basis of less precise criteria such as the default payment criterion (Hambrick and D'Aveni, 1988; Haswell and Holmes, 1989). On the other hand, once a population of distressed firms has been identified and delimited, it is difficult to contact their owners.

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8 As they are dedicated to large firms or to the consequences of failure, the other two patterns presented by Masuch (1985) can not be used to explain small firms' failure.
leaders and to get information about the fundamental causes of their failure. Indeed, failure is a very sensitive topic (Ooghe and De Prijcker, 2008) and individuals have a natural reticence to discuss failure and its causes (Bruno et al., 1987).

Under these conditions, the partnership between the University and the Court of Commerce of Liège (Belgium) on which the present study is based has two main advantages. On the one hand, the distressed firms are identified beforehand by the Court: a population of distressed firms is thus clearly delimited, i.e. distressed firms placed under investigation by the Court. On the other hand, the leaders of the distressed firms are invited by a legal authority to speak about their failure. It is therefore much easier to obtain information about explanatory failure factors than to try to collect these data without any official legitimacy.

In order to ensure the diversity of the data, three types of files from the Court (Commercial Inquiries, Legal Reorganizations and Bankruptcies) are analyzed in the present research.

A) **106 distressed firms convoked to a Commercial Inquiry by the Commercial Inquiry Department** are considered in the sample. These firms were convoked to a Commercial Inquiry, and were thus included in the sample, on the basis of the following criteria (Bayard and Lonhienne, 2003):

- Firstly, they were detected and then considered as distressed firms by the Commercial Inquiry Department on the basis of predetermined failure signals. These are protests, judgments against the debtor, payment defaults to the social security administration or to the tax administration (VAT, Income tax) for at least 2 trimesters, any decisions of suspension or withdrawal of a procurement contractor’s certification and any pertinent information from the annual accounts or from a report filled by the controller of the firm's accounts. The combination of criteria retained to consider a firm as a distressed firm varies from one Court to another. Generally, a newly founded firm is considered as distressed as soon as ONE negative signal is collected. Otherwise, it is the combination of several negative signals that leads to the opening of a specific file.

- Secondly, after the collection of additional information about this firm and after a first analysis realized by the administrative department, it comes out that the signals are relevant and significant, so that the Chamber of Commercial Inquiry can analyze it.

- Finally, the judges from the Chamber of Commercial Inquiry estimate it is necessary to convocate the leader(s) of the distressed firm to a Commercial Inquiry, i.e. a meeting between a (consular) judge and the leader(s) of the detected distressed firms, in order to investigate the problems of the firm further. During this meeting, questions about the “perceived” causes of the distress of the firm, the current situation of the firm and the measures intended to remedy the situation are asked.

In order to limit the bias linked to the selection procedure explained just before and, thus, in order to make sure that the present research does not focus on particular distressed firms, the sample includes two other kinds of distressed firms:

9 This official meeting between judges from the Court of Commerce is presided by a professional judge who is assisted by 2 consular judges. They analyze the situation of the detected distressed firms and they can make three distinctive decisions: to close the file if they consider that the firm's continuity is not in peril, to organize a Commercial Inquiry if further investigation is necessary or to engaged into a bankruptcy procedure if the conditions for it are fulfilled.

10 For example, a selection bias could derive from the fact that the (consular) judges may have a natural tendency to
B) **51 bankrupt firms** are included in the sample

C) **51 firms that entered a legal reorganization procedure** are considered in the present sample.

Concretely, the sample of firms on which this research is based is then composed of 208 incorporated small Belgian distressed firms investigated by the Court of Commerce of Liège for a Commercial Inquiry, a Legal Reorganization or a Bankruptcy.

Tables 3 and 4 describe globally the sample on the basis of some objective characteristics (age, size\(^\text{11}\), capital and industry).

Table 3 presents descriptive statistics about the sampled firms by type of file (Commercial Inquiry, Legal Reorganization and Bankruptcy), in function of their age and size.

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Commercial Inquiry</th>
<th>Legal Reorganization</th>
<th>Bankruptcy</th>
</tr>
</thead>
<tbody>
<tr>
<td>AGE</td>
<td>Mean</td>
<td>10.7</td>
<td>8.1</td>
</tr>
<tr>
<td></td>
<td>Median</td>
<td>7.00</td>
<td>5.00</td>
</tr>
<tr>
<td></td>
<td>Minimum</td>
<td>0.0000</td>
<td>0.0000</td>
</tr>
<tr>
<td></td>
<td>Maximum</td>
<td>44</td>
<td>32</td>
</tr>
<tr>
<td></td>
<td>Standard Deviation</td>
<td>9.6</td>
<td>7.8</td>
</tr>
<tr>
<td></td>
<td>Skewness</td>
<td>1.036342</td>
<td>1.521007</td>
</tr>
<tr>
<td>SIZE (Personnel)</td>
<td>Mean</td>
<td>6.4</td>
<td>8.4</td>
</tr>
<tr>
<td></td>
<td>Median</td>
<td>4.00</td>
<td>4.00</td>
</tr>
<tr>
<td></td>
<td>Minimum</td>
<td>0.0000</td>
<td>0.0000</td>
</tr>
<tr>
<td></td>
<td>Maximum</td>
<td>50</td>
<td>48</td>
</tr>
<tr>
<td></td>
<td>Standard Deviation</td>
<td>7.7</td>
<td>11.0</td>
</tr>
<tr>
<td></td>
<td>Skewness</td>
<td>3.130028</td>
<td>2.236837</td>
</tr>
<tr>
<td>EQUITY (in euros)</td>
<td>Mean</td>
<td>119606.7</td>
<td>140986.0</td>
</tr>
<tr>
<td></td>
<td>Median</td>
<td>20000.00</td>
<td>25000.00</td>
</tr>
<tr>
<td></td>
<td>Minimum</td>
<td>250.0000</td>
<td>250.0000</td>
</tr>
<tr>
<td></td>
<td>Maximum</td>
<td>4713835</td>
<td>1240000</td>
</tr>
<tr>
<td></td>
<td>Standard Deviation</td>
<td>488428.7</td>
<td>263005.8</td>
</tr>
<tr>
<td></td>
<td>Skewness</td>
<td>8,712899</td>
<td>2,689161</td>
</tr>
</tbody>
</table>

**Table 3**: Characteristics of the sample by type of file

In addition, Table 4 shows the distribution of the Sample by Type of files and by Industry\(^\text{12}\).

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11 The size of the firms is determined by the number of workers. Regarding the European Commission Definition (2003), small firms are organizations that have less than 50 workers.
12 HORECA is the French abbreviation for the Industry grouping **Hotels, Restaurants and Cafés**
3.2. Data collection

For each of the three types of distressed firms mentioned above, a series of data were collected. More precisely, information about the evolution of the file at the Court (date of the first detection, exit of the process, etc.), about the intrinsic characteristics of these firms (age, size, life cycle) and of their leaders as well as about the fundamental reasons for their failure were gathered. In order to ensure the reliability and the homogeneity of the data collection, systematic collection grids were elaborated for each kind of files (Commercial Inquiry, Bankruptcy and Legal Reorganization), on the basis of an adaptation to small firms of the model presented by Auteure and Auteur (2009) (see Appendix 1). Different data collection methods were used in function of the type of distressed firms.

Concerning the firms convoked to a Commercial Inquiry, the data collection process consists in the observation of the meeting between the judge and the leader(s) of the distressed firms. Concretely, before each meeting, the file was analyzed by the scientific researcher and by the consular judge: pertinent information was already drawn from the diverse documents which the Department disposed of (financial annual accounts, possible answer of the entrepreneur to a questionnaire, failure symptoms identified, etc.). Then, the meeting took place and the judge asked questions to the entrepreneur regarding the failure of his firm and the reasons for this situation. Sometimes, depending on the personality of the judge, the researcher had the opportunity to ask some questions. Finally, after the meeting, the information collected was discussed with the judge (feedback).

Concerning the other two kinds of distressed firms, the data collection process consists in a document analysis: the analysis of bankruptcy and legal reorganization records. These documents have to be written by the (bankruptcy or legal reorganization) administrators and they contain crucial information about the firm's characteristics and about the fundamental factors that explain its failure.

In order to make sure that the failure of the studied firms is not related to particular environmental conditions, the data include distressed firms investigated by the Court at different periods of time.

Firstly, data about distressed firms convoked to a Commercial Inquiry were collected during two distinctive time periods:

Table 4: Distribution of the Sample by Type of files and by Industry

<table>
<thead>
<tr>
<th></th>
<th>Commercial Inquiry</th>
<th>Legal Reorganization</th>
<th>Bankruptcy</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacture</td>
<td>16</td>
<td>8</td>
<td>3</td>
<td>27</td>
</tr>
<tr>
<td></td>
<td>7,69%</td>
<td>3,85%</td>
<td>1,44%</td>
<td>12,98%</td>
</tr>
<tr>
<td>Construction</td>
<td>17</td>
<td>11</td>
<td>10</td>
<td>38</td>
</tr>
<tr>
<td></td>
<td>8,17%</td>
<td>5,29%</td>
<td>4,81%</td>
<td>18,27%</td>
</tr>
<tr>
<td>Services</td>
<td>24</td>
<td>11</td>
<td>10</td>
<td>45</td>
</tr>
<tr>
<td></td>
<td>11,54%</td>
<td>5,29%</td>
<td>4,81%</td>
<td>21,63%</td>
</tr>
<tr>
<td>Commerce</td>
<td>33</td>
<td>15</td>
<td>17</td>
<td>65</td>
</tr>
<tr>
<td></td>
<td>15,87%</td>
<td>7,21%</td>
<td>8,17%</td>
<td>31,25%</td>
</tr>
<tr>
<td>HORECA</td>
<td>16</td>
<td>6</td>
<td>11</td>
<td>33</td>
</tr>
<tr>
<td></td>
<td>7,69%</td>
<td>2,88%</td>
<td>5,29%</td>
<td>15,87%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>106</td>
<td>51</td>
<td>51</td>
<td>208</td>
</tr>
<tr>
<td></td>
<td>50,96%</td>
<td>24,52%</td>
<td>24,52%</td>
<td></td>
</tr>
</tbody>
</table>
periods:

- Data about the first 50 cases were collected between September and December 2006. An exploratory analysis of this first 50 firms was then rapidly carried out in order to obtain some exploratory results.
- Information about the remaining 56 cases were collected between January and June 2008.

Secondly, data about bankrupt firms refer to firms that were declared bankrupt between September 2007 and January 2008\(^{13}\). More precisely, the first ten\(^{14}\) incorporated firms that were declared bankrupt in September, October, November, December 2007 and January 2008 are included in the sample.

Finally, information is gathered about firms that entered a legal reorganization procedure between 1998 and 2004.

### 3.3. Data analysis

The data are analyzed according to the principles of the qualitative content analysis (Glaser and Strauss, 1967; Mayer and Ouellet, 1991; Hlady Rispal, 2002).

In a first time, the data collected are organized and classified into several predetermined categories in a systematic analysis grid. The categorization of the data is a crucial step in the data analysis process because it allows the comparison of the data (Hlady Rispal, 2002). For the present analysis, the categories are determined in advance on the basis of the integrative model proposed by Auteure and Auteur (2009) and they mainly portray the fundamental reasons for a small business failure. Appendix 2 describes these different categories.

In a second time, a content analysis of the data is carried out: in-depth horizontal and vertical analyses are successively undertaken. More precisely, the horizontal analysis consists in a detailed analysis of each case in order to understand it completely while the vertical analysis focuses on the identification of the similarities and of the differences between the cases. The cases were read and re-read (Deslauriers, 1991) in order to precisely identify homogeneous groups of distressed firms in function of the fundamental reasons for their failure. Each atypical case was taken into account in order to enrich the results.

As briefly mentioned above, two main chronological steps have to be distinguished in the data analysis process.

Firstly, data concerning 50 distressed firms convoked to a Commercial Inquiry between September and December 2006 were analyzed. This first analysis gives rise to exploratory results and, in particular, to an exploratory taxonomy of seven failure patterns which are published in Auteure and Auteur (2009).

Secondly, the exploratory results were refined on the basis of two types of complementary analyses which were conducted in parallel over a two-year period:

1. A questionnaire was sent to 21 “experts”\(^{15}\), i.e. scientific researchers or practitioners from different countries who are

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\(^{13}\) The juridical year is similar to the academic year in Belgium (from September until June)

\(^{14}\) The President of the Court confirms us that the first ten bankruptcies of each month are not selected according a procedure which differ from the one used to select the other bankruptcies of the month.

\(^{15}\) These “experts” come from the social network of the Court of Commerce of Liège and from the social network of
familiar with small businesses and/or with their failure. This questionnaire summarizes the initial exploratory results and complements them by asking a series of open questions whose answers bring additional information in order to refine the results.

Table 5 summarizes the main characteristics of the experts included in this analysis.

<table>
<thead>
<tr>
<th>Main criteria</th>
<th>BACKGROUND</th>
<th>BUSINESS FIELD</th>
<th>COUNTRY</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Scientific</td>
<td>Non Scientific</td>
<td>Finance</td>
</tr>
<tr>
<td>Number of experts</td>
<td>7</td>
<td>14</td>
<td>9</td>
</tr>
<tr>
<td>TOTAL</td>
<td>21</td>
<td>21</td>
<td></td>
</tr>
</tbody>
</table>

Table 5: Main characteristics of experts

Globally, all experts agree with the exploratory taxonomy and their supplementary comments were taken into account in order to refine the exploratory results.

2. Data collected about the other 158 distressed firms were analyzed according to the principles of the qualitative content analysis presented above.

So, the final taxonomy was constructed thanks to a process of continuous improvement of the initial exploratory results, progressively enriched with the comments of the panel of experts and with information about 158 additional cases. In fine, these additional analyses conducted to the refinement as well as to a saturation of the results (Mayer and Ouellet, 1991).

3.4. Reliability and validity

"Reliability and validity remain appropriate concepts for attaining rigor in qualitative research." "Qualitative researchers should reclaim responsibility for reliability and validity by implementing verification strategies integral and self-correcting during the conduct of inquiry itself" (Morse et al., 2002).

In order to ensure the reliability and the validity of our qualitative study, several "strategies" were implemented (Morse et al., 2002):

- The global methodological coherence of the research is ensured by the fact that there is a congruence between the research question and the components of the methodology. Indeed, the sample of small distressed firms investigated by the Court of Commerce of Liège, the data collection process (interviews and document analysis in order to understand the fundamental reasons for their failure) and the data analysis method (a qualitative content analysis) are appropriate to respond to the current research question, which is "Which distinctive explanatory failure patterns can we identify amongst a sample of small distressed firms?"

the CEPE-ULg (Research Center of Business Performance – HEC-University of Liège). This is why most of the interviewed people are Belgian (see Table 5).
This qualitative analysis is based on a *systematic and beforehand categorization* of the data (Glaser and Strauss, 1967; Mayer and Ouellet, 1991), on the basis of the conceptual model proposed by Auteure and Auteur (2009) This objective predetermined categorization of the data limits the risk that another researcher would have had very different results (Hlady Rispal, 2002).

A *saturation* of the results is observable at the end of the data analysis process (Glaser and Strauss, 1967; Mayer and Ouellet, 1991).

According to Morse et al. (2002), “the notions of categorization and saturation ensure replication and confirmation”.

Data were collected and analyzed concurrently (see section 2.3.), so that there were a mutual interaction between what is known and what one needs to know. This pacing and the iterative interaction between data and analysis is the essence of attaining reliability and validity (Morse et al., 2002).

*Triangulation methods* (Yin, 1988) were used in order to ensure the trustworthiness of the data collection and of the data analysis. For example, each firm's financial statements were collected and analyzed in order to confront and confirm the data collected at the Court and the data collected about distressed firms convoked to a commercial inquiry were discussed with the judge responsible for them (see section 2.2.).

The exploratory results were confirmed (Morse et al., 2002) and refined by 21 experts from several countries in order to ensure their (external) validity.

The results were finally *compared to previous literature* in order to make sure they were not too specific regarding our methodological choices (external validity).

### 4. Results

After a qualitative content analysis, a taxonomy of five major EBFPs comes out: (1) badly-created firms, (2) firms with growth-related problems, (3) nonreactive (old) firms, (4) firms that serve other interests and (5) shocked firms. These failure patterns are themselves detailed into several sub-patterns.

#### 4.1. Badly-created firms (106 firms)

This first EBFP is, by far, the most common one. Indeed, more than half of the sampled firms are included in it. These firms have been engaged in a failure process since their creation because they have never succeeded in creating a viable strategic position on their market. More precisely, the entrepreneur(s) has never succeeded in developing strategic assets and strategic asset deployment, because of diverse fundamental failure factors (such as a lack of managerial competences or a lack of experience). Unsurprisingly, firms that are included in this failure pattern are globally young when they are detected by the Court of Commerce of Liège (for a Commercial Inquiry, a Legal Reorganization or a Bankruptcy). Indeed, 59 firms out of the 106 are younger than 3 years and 76 are younger than 5 years at that time.

Five sub-patterns may be discerned among badly-created firms: (1) firms that are based on poor foundations, (2) firms that are lead by entrepreneurs with insufficient managerial competences, (3) firms that cumulate the preceding two fundamental problems, i.e. they are based on poor foundations and they are lead by entrepreneurs with insufficient managerial competences, (4) innovative firms that are highly product-oriented and (5) firms that suffer from youthful indiscretion(s).
4.1.1. Firms that are based on poor foundations (51 firms)

This failure pattern gathers together firms whose foundations are problematic: already before the official launch of the firm, important (pre-startup) deficiencies may be observed in these firms. Three categories of firms belonging to this sub-pattern may be distinguished.

Firstly, there are firms (three sampled firms) that are created by entrepreneurs who are not really motivated by the launch, the conduct and the development of the firm. For example, some entrepreneurs create a firm in order to help a family member or a friend who could go into a personal bankruptcy, who has been unemployed for a long time or who did not have the necessary diploma's to create this kind of firm. That is, the official founders of these firms do not believe profoundly in the firm's project and they are thus not deeply committed to it. Under these circumstances, the initial available resources are often not sufficient to permit an adequate start.

Secondly, some firms (nineteen sampled firms) consist in the revival of a failed business on the same wrong basis by the same or by new entrepreneurs. This sub-category relates to individuals who launch a (new) firm that is based on the same inadequate business model as a previously liquidated or bankrupt firm. Under these conditions, these new firms never succeed in obtaining a viable strategic position. In addition, the negative image of the preceding failure has a negative impact on the new firm's failure. Indeed, commercial partners, such as clients or suppliers, mistrust the firm.

Thirdly, there are firms (twenty-nine sampled firms), which are created by (motivated) entrepreneurs who are not able to analyze and to anticipate, prior to startup, their environment and their market. This leads to an inadequate pre-startup diagnosis and, more concretely, to an inadequate business model (or business plan). Diverse inadequacies may be observed: a non-viable business concept, insufficient or inadequate initial resources (under-capitalization, insufficient technical resources, etc.), an inappropriate location of the firm, an overestimation of the potential revenues of the firm, etc. More globally, the inadequate pre-startup diagnosis leads to the overestimation of the future sales of the firm compared to its real potential on its market.

4.1.2. Firms that are lead by entrepreneurs with insufficient managerial competences (23 firms)

This sub-pattern refers to young firms that are conducted by entrepreneur(s) with insufficient managerial competences. Generally, these individuals are good technicians, i.e. they are technically competent in their industry, but they lack the skills needed to successfully run and develop a business. Whereas their commercial skills are generally sufficient, some of the following deficiencies may be detected. The entrepreneurs are unable to control the firm and its costs. They lack skills in finance, in accounting or in business administration. For example, they are unable to calculate the cost price of their product and they determine the sale price on the basis of the price of their competitors or they are unable to anticipate their working capital requirements.

4.1.3. Firms that are based on poor foundations and lead by entrepreneur with insufficient managerial competences (24 firms)

Firms that belong to this third sub-pattern combine the fundamental failure problems shown by the patterns 3.1.1. and 3.1.2. They are based on inadequate foundations and they are lead by entrepreneur(s) with insufficient managerial competences. More concretely, the leaders of these firms lack commercial skills as well as the ability to analyze their environment adequately and to anticipate events but also, the ability to control their firms as well as skills in finance, in
accounting and in business administration.

4.1.4. **Innovative firms that are highly product-oriented (5 firms)**

This fourth sub-pattern concerns innovative firms that are generally operating in a niche market. These firms are lead by entrepreneurs who are passionate by their technology and/or by their product but who are incompetent or uninterested by the conduct of a business. Two main characteristics of firms belonging to this pattern have to be underlined. On the one hand, once the firm is created, it sometimes takes years before the commercial activities start. Indeed, the research and development phase is continued during the first years of the firm's existence. This situation conducts to important (financial) difficulties before the beginning of the sales. On the other hand, the entrepreneurs of these firms concentrate on the development of their technology and of their product rather than on its commercialization and, more globally, on the management of the business. More precisely, as they are less interested in the commercial aspects of business, they have it difficult to find customers and to sell their product. Furthermore, they lack skills in finance, in accounting and in business administration. In other words, they are technology- or product-oriented rather than business-oriented.

4.1.5. **Firms that suffer from youthful indiscretion(s) (3 firms)**

Even if they are not confronted to the problems presented in the sub-patterns 4.1.1. to 4.1.4., young firms may enter a failure process because of youthful indiscretions. Actually, in firms which have just been created, the leaders sometimes lack experience in their industry or in business management. In some cases, this inexperience leads them to commit youthful errors such as an error in the cash flow management of the firm, a mistake in the choice of partners (customers, suppliers, accountants, etc.) or an enormous marketing budget which does not bring the expected sales.

4.2. **Firms with growth-related problems (20 firms)**

The second EBFP relates to firms in which the growth issue has been inadequately managed. Two main sub-patterns can be differentiated : firms in which the future growth has been overestimated and growing firms faced with problems of control, organization and planning.

4.2.1. **Firms in which future growth has been overestimated (6 firms)**

This sub-pattern refers to firms in which the future potential sales have been overestimated (compared to the actual evolution of the environment) and in which a too heavy structure has be implemented compared to the actual level of activity of the firm. The fundamental problem at the origins of this failure sub-patterns is the inadequate market analysis made by the entrepreneurs. On the one hand, the environment may change and become less benevolent : they may not have anticipated changes in the market, such as the arrival of new competitors on a (growing) market. The pace of expansion is then too fast under the new conditions. On the other hand, they may have lost their sense of realities and/or they may have become too optimistic after a previous (punctual) growing period. These two situations may, for example, lead to the following problems. Firstly, the structure of the firm is finally too heavy compared to its real level of activity. Secondly, the diversification strategy implemented by the entrepreneur is inadequate. Thirdly, the planned geographical expansion is unappropriated. Etc.
In summary, in any case, due to an inadequate market analysis, the amount of charges necessary to cover the activities of the firms is too high compared to the actual revenues.

4.2.2. Uncontrolled growing firms (14 firms)

This second sub-pattern gathers together growing firms faced to problems of control, organization and planning. Three situations may be discerned.

Firstly, the entrepreneur is unable to manage a bigger and more complex structure. He is competent to run a very small business with one or two workers but he is unable to control and to manage a higher and more formalized entity. For example, in a bigger firm, the human resource management, the accounting management and the administrative management are much more complex. The entrepreneur is not always able to adequately deal with all the aspects of the management of his firm. In this case, if he does not delegate some part of his preceding work to collaborators, the firm will probably enter a failure process.

Secondly, the entrepreneur has not modified the structure and the organization of his firm after its growth: it is still operating as a very small entity (intuitive strategy, no formalization, few planning, etc.). Nevertheless, as the volume of sales/activities is higher, new methods of organization, planning, administration, etc. are necessary. Indeed, the growth of the firm usually induces a need for a more formalized structure. This lack of adaptation of the firm's structure leads to internal crises, i.e. internal organization problems, such as an insufficient amount of workers, late delivery delays or a deteriorating human climate due to stress.

Thirdly, if the growth is very (too) rapid, the firm generally does not have the needed cash to finance it and it has to use external financing. This is why rapidly growing firms often fail due to the financial stress of the growth. Furthermore, similarly with the preceding point, if the firm's growth is very rapid, the entrepreneur lacks time to adapt its structure to its new level of activities. In other words, the pace of growth overtaxes the firm's financial and managerial resources. As mentioned in the previous point, this leads to problems of control, organization, etc. Under these circumstances, rapidly growing firms have increasing sales concurrent with higher costs of goods sold, greater debt and, finally, smaller profit margins.

4.3. Nonreactive (old) firms (15 firms)

The main fundamental problem that explains the failure of the firms that belong to this third EBFP is their progressive misalignment with their environment, i.e. their progressive loss of connection with the external world, because their leaders lack the ability to anticipate events and to adapt to (progressive) changes.

All the firms that are attached to this failure pattern are older than 12 years and the main fundamental reasons for their progressive misalignment with their external environment is the lack of dynamism and the loss of motivation of their leaders. Actually, as the firm has been operating without any particular failure for years, they continue to stick to past (successful) courses of actions. As they progressively loose their ability to anticipate and to adapt the firm to its environment, the firm becomes nonreactive. As the environment is continuously evolving, there is then a progressive mismatch between the firm and the requirements of its environment: it is thus progressively misaligned with the external world. Under these circumstances, the firm can no longer sustain a viable strategic position. For example, some nonreactive firms continue operating for years in a declining market without any project of diversification. As a result,
the sales of these firms progressively decline. In some other firms, while the sales are still satisfactory thanks to their good reputation or to an efficient marketing, the management methods used for years are no more adapted to the current economic environment (old-fashioned cost accounting methods or information channels, for example).

As mentioned above, the fundamental reason for the failure of these firms is the following one. As they have been operating for years without any particular problem, their leaders have progressively lost their dynamism and, in particular, their ability to anticipate and to adapt to changes. In fact they become overly dependent on their mental models.

Two categories of nonreactive entrepreneurs have to be distinguished:

- There are aging entrepreneurs who are no more able to run a business in the current and rapidly-changing world. Here are some examples. Their management methods are old-fashioned. As they become older, they progressively loose their dynamism and their flexibility. Their intellectual capabilities decrease. Etc. In other words, they have more and more difficulties to stay in touch with the current environment.

- There are younger entrepreneurs who are listless, bored or unmotivated leaders. They do not involve themselves completely in the firm and they are not enough dynamic, flexible to make the firm reactive to (progressive) external changes.

4.4. Firms serving other interests (25 firms)

The fourth EBFP relates to firms whose operations mainly serve other interests than its own ones. In these firms, the (personal or professional) objectives of the entrepreneurs are, consciously or unconsciously, not aligned with the corporate goals, which would normally lead to an efficient development of the firm. This EBFP can be detailed into three sub-patterns: (1) firms that serve the enrichment of the entrepreneurs, (2) firms that serve the interests of another organization, (3) firms with fraudulent activities.

4.4.1. Firms that serve the enrichment of the entrepreneurs (12 firms)

This sub-pattern concerns firms that are run by one or several entrepreneurs whose main objective is their own enrichment and not the good development of the firm and of its activities. For example, they withdraw a large part of the cash flows necessary to the financing of the firm's operations for personal use. They buy an expensive professional car while the firm's activities are insufficient to afford its financing.

4.4.2. Firms that serve the interests of another organization (2 firms)

This failure pattern refers to firms whose activities and, in particular, cash flows, are only used to finance or enrich another organization. For example, some entrepreneurs use the cash generated by the activities of a firm to finance a parent company in distress.

4.4.3. Firms with fraudulent activities (11 firms)
This third sub-pattern regroups firms involved in one or several frauds such as tax, VAT frauds or even penal or criminal frauds.

**4.5. Shocked firms (42 firms)**

The last EBFP refers to firms that fail after one or several shocks\(^{16}\). The impact of a shock on a firm's failure mainly depends on two related elements: the magnitude of the shock and the (resource) buffer of the firm. The higher the magnitude of the shock and the smaller the set of available resources, the more likely this shock will cause the firm's failure. As, by definition, small firms have a smaller set of resources than larger ones do, they are thus much more vulnerable to shocks. Theoretically, this failure patterns should thus be much more common in small business failures.

From the present qualitative analysis, it comes out that several categories of shocks can explain the failure of a small firm. Four main sub-patterns are distinguished: (1) firms that fail because of a managerial decision which does not have the predicted consequences, (2) firms that fail because of an external shock, (3) firms that fail because of individual problems linked with the firm's life, (4) firms that fail after an individual problems, without any relationship with the firm's life.

4.5.1. Firms that fail because of a managerial decision with an unexpected outcome (7 firms)

A punctual managerial decision, which generates important investments, such as an important strategic reorientation or a big risky investment, explains the failure of seven firms of the sample. Actually, these managerial decisions are damageable for the firms because they do not have the expected consequences: the investments related to these managerial decisions are not profitable. The reasons for these unpredicted consequences are either a wrong market analysis or an unpredictable change in the environment.

4.5.2. Firms that fail because of an external shock (13 firms)

This sub-pattern gathers together firms whose failure can be explained by one or several external shocks. Three kinds of external shocks may be discerned. Firstly, macroeconomic shocks, such as a big technological change or an economic downturn, are external factors which can explain a small firm failure. Secondly, shocks coming from the competitive environment of the firm such as the loss or the bankruptcy of an important customer, are the reasons for the failure of nine firms of the sample. Thirdly, accidents such as a fire or a bribery can also explain the failure of small firms.

4.5.3. Firms that fail because of individual problems, linked to the firm's life (18 firms)

Two major categories of individual problems linked to the firm's life have been identified: problems related to the transmission of the firm and a dispute or a disagreement between key actors.

Firstly, the transmission of a firm can be at the origins of its failure. Even if, in some circumstances, the takeover of the firm may have a favorable impact on its performance (Haveman and Khaire, 2004), it can also harm a small firm.

\(^{16}\) Punctual events in the firm's life, unrelated with its evolution along its life cycle.
Indeed, the takeover of the firm by a family member or by external actors is presented as a challenge (Norton, 2005), or even as crisis period (Gouldner, 1954; Grusky, 1963; Allen et al., 1979; Carroll, 1984; Churchill and Hatten, 1987; Haveman, 1993), in the literature. If this challenging period is inadequately managed by the predecessor (vendor) as well as by the successor (purchaser), it can be at the origins of its failure.

The qualitative analysis points out different kinds of problems related to the takeover of firms. They may be attributable to the predecessor(s) or to the successor(s).

On the one hand, in some firms, the predecessor is dishonest and he does provide the successor with unfair information. For example, the financial statements do not reflect the true situation of the firm. In some other firms, the predecessor has it difficult to leave the firm because he regards it almost as his child. Under these circumstances, the successor has no real chance to take the control of the firm and to really implement the required changes.

On the other hand, the successor may also be at the origins of the failure. Here are some example of errors made by successors. Firstly, some purchasers make a wrong diagnosis and are convinced that the firm has much more potential than it really has. Under these circumstances, they invest too much in it compared to its potentialities and their investments are thus unprofitable. Secondly, some successors are unable to take the firm over because they are not prepared to manage the crisis period related to the takeover and/or because they are simply unable to run a business (see point 3.1.2.). Thirdly, some successors who are insufficiently experimented with the firm industry or with business management make youthful indiscretions (see point 3.1.5.).

It is worth mentioning that it is difficult to clearly identify who is really guilty in takeover conflicts. Indeed the interests of both parties (predecessor versus successor) are often opposed and they have the tendency to externalize the problems. As an example, if the successor is not able to surpass the natural challenging period related to the takeover, he will often blame the predecessor and he will accuse him of unethical behaviors.

Secondly, a dispute or a disagreement between key firm's actors, such as shareholders or directors, is presented by four interviewed entrepreneurs as the main reason for the failure of their firm.

4.5.4. Firms that fail after a private problem (4 firms)

In four sampled firms, the entrepreneur or key actors within the firm are confronted to private problems, such as an illness, a divorce or a death. These private problems may paralyze the firm for a long time or they may completely destroy it.

Nevertheless, the fifth EBFP, which refers to shocked firms, has to be relativized. Indeed, the entrepreneurs have it difficult to objectively detect the causes of the failure (Bruno et al., 1987). As mentioned above, they have a natural tendency to externalize the reasons for their business failure and they sometimes hide their own mistakes. Under these circumstances, as Ooghe and Waeyaert (2004) argue, the failure of “shocked firms” can often be attributed to other more fundamental explanatory factors such as an inadequate anticipation of the evolution of the environment, an inappropriate commercial strategy that leads to a (too) high dependence towards one or a few customers, an insufficient preparation of the founder's succession, etc. In other words, in some cases, some unfavorable conditions are already developing within the firm before the occurrence of the shock.
Despite this relevant comment, the present study considers that the fifth EBFP has anyway to be presented as a specific failure pattern for two main reasons. Firstly, in practice, some shocks are very difficult to forecast or are even unpredictable. A sudden financial crisis or an illness are examples of shocks that are difficult to be anticipated by the entrepreneur. Secondly, the present research concentrates on small firms. As, by definition, these firms have a small set of resources, a shock can be much more damageable for them than for larger firms and it can thus much more likely explain their failure.

In order to conclude this third section, Table 6 summarizes the taxonomy induced by this qualitative analysis and it presents the key characteristics (used in categorization) of each (sub)pattern.
<table>
<thead>
<tr>
<th>Major EBFPs</th>
<th>Sub-EBFPs</th>
<th>Key characteristics</th>
</tr>
</thead>
</table>
| 1 BADLY-CREATED FIRMS | 11 Poor foundations | Lifecycle : Creation  
Poor ability to analyze the environment and to anticipate its evolution  
Inadequate business plan (Lack of motivation and commitment) |
| | Insufficient managerial competences | Lifecycle : Creation  
Good technical competences  
Motivated entrepreneurs  
Poor managerial competences (Finance, Accounting, Administration, Lack of control) |
| | Poor foundations + Insufficient managerial competences | Lifecycle : Creation  
Innovative firms  
Motivated entrepreneurs (Passion)  
Lots of Research and Development  
Poor managerial competences (Marketing, Sales, Finance, Accounting) |
| 2 FIRMS WITH GROWTH-RELATED PROBLEMS | Overestimation of the future level of activity | Lifecycle : Growth  
Poor ability to anticipate the evolution of the environment |
| | Lack of control | Lifecycle : Growth  
Ability to adapt the firm’s structure and to control it  
Poor managerial competences (operational management, finance, accounting, administration, control) |
| 3 NON-REACTIVE FIRMS | Progressive misalignment | Lifecycle : Maturity-Decline  
Lack of analysis of the environment and of anticipation of its changes  
Inadaptation of the firm to the changing environment  
Poor motivation/dynamism/commitment (Aging entrepreneur) |
| 4 FIRMS SERVING OTHER INTERESTS | Enrichment of the owner/manager | Lack of commitment  
Other interests : Entrepreneur  
Unethical management of “Shareholders’ amounts receivables” |
| | Interests of an other organization | Lack of commitment  
Other interests : another organization |
| | Fraud | Lack of commitment  
Fraudulent activities |
5. Discussion

5.1. Strong relationship with the Life Cycle Theory

A strong relationship can be traced between the EBFPs induced by the present qualitative analysis and the Life Cycle Theory (Penrose, 1952; Lippit and Schmidt, 1967; Greiner, 1972; Adizes, 1979, Robbins, 1990; Dodge and Robbins, 1992).

Researchers who support this theory compare firms with biological organisms: “Like people and plants, organizations have a life cycle. They have a green and supple youth, a time of flourishing strength, and a gnarled old age...” (Lippit and Schmidt, 1967). They consider that firms develop a life cycle, which is characterized by several chronological or development phases. The phases that are the most commonly evoked in the literature are the introduction/creation, growth, maturity and decline phases. According to the principles of the Life Cycle Theory, the entrepreneur is confronted to different challenges or crises at each stage of the life cycle of his (small) firm (Van Caillie, 2001). A large part of the business failures are related to an inadequate management of the different development crises because the firm does not possess the required resources and the adequate resource deployment to face them (Lippit and Schmidt, 1967). Similarly, Hall and Young (1989) argue that “an intuitively plausible proposition is that small firms experience a life cycle, at each stage of which they are confronted by a different set of problems. Though the nature of the problems will differ, the results of a failure to solve them can remain equally potentially catastrophic”. Each stage is regarded as a crisis period with its own challenges (Van Caillie, 2001).

Table 6: A taxonomy of explanatory failure (sub)patterns and their key characteristics

<table>
<thead>
<tr>
<th>Pattern</th>
<th>Key Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Punctual managerial error</td>
<td>Ability to analyze the environment and to anticipate its evolution, Poor managerial decision, Inadequate investment</td>
</tr>
<tr>
<td>External shock(s)</td>
<td>Shock(s) from the macroeconomic environment, Shock(s) from the competitive environment (customers, suppliers, competitors, business partners)</td>
</tr>
<tr>
<td>Individual problems (in relationship with the firm's life)</td>
<td>Takeover of the firm, Problems related to the predecessor OR to the successor, Interests: unethical own enrichment, Personality, Lack of motivation/commitment, Poor managerial competences</td>
</tr>
<tr>
<td>Private problem</td>
<td>Private problem (disease, death, divorce, etc.)</td>
</tr>
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</table>
Under these conditions, the first three EBFP have voluntarily been presented successively because they are strongly linked with the evolution of the small firm on its life cycle and, particularly, with an inappropriate management of the various life cycle crises.

The first EBFP, i.e. badly created firms, refers to firms in which the first stage of development has been badly managed. The entrepreneurs of these firms have not succeeded in overcoming the challenges of this first stage: they have not succeeded in creating a viable strategic position. As mentioned previously, this situation can be fundamentally explained by various factors such as a lack of commitment or insufficient managerial competences.

The second EBFP, i.e. firms with growth-related problems, concerns firms in which the entrepreneurs have inadequately dealt with the growth issue.

The third EBFP, i.e. nonreactive (old) firms, relates to mature, or even declining, firms that have progressively lost touch with their environment.

In contrast, the last two EBFP are not related to particular stage(s) of the firm's life cycle. Conflicting interests or shocks can explain the failure of firms situated at any stage of their life.

5.2. Consistency with previous literature

Even if none of the previous studies focuses on small businesses, Table 7 shows that the results of the present analysis are consistent with the explanatory failure patterns emerging from previous literature (see Section 2).

<table>
<thead>
<tr>
<th>Patterns emerging from previous literature</th>
<th>Poor performing firms that never succeed</th>
<th>Rapid over-expansion</th>
<th>Late(r) over-expansion</th>
<th>Lack of progressive adaptation</th>
<th>External events</th>
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<tbody>
<tr>
<td>Patterns induced from the ground</td>
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<td></td>
</tr>
<tr>
<td>1. Badly created firms</td>
<td>X</td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>2. Firms with growth related problems</td>
<td></td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
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<tr>
<td>3. Non reactive firms</td>
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<td></td>
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<td>X</td>
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<td>4. Firms serving other interest</td>
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<td>5. Shocked firms</td>
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</table>

Table 7: Relationship between patterns emerging from previous literature and patterns induced from the ground

Indeed, the EBFPs 1, 2, 3 and 5 have been discussed by previous researchers. Globally, these patterns do not seem to be specific to small business failures.

Nevertheless, the present research provides some interesting new insights.

Firstly, an original EBFP dedicated to firms that serve other interests is proposed whereas none of the previous nine studies on EBFPs deals with this frequent business problem (Newton, 1985).

Secondly, the five EBFPs are detailed into sub-patterns: a lot of details are exposed and numerous subcategories are
presented compared to preceding research. 
Thirdly, the taxonomy induced by the present analysis focuses on small firms and on their specific characteristics. As a consequence, some failure (sub)patterns are particularly related to small business failures. For example, shocked firms are much more common among a sample of small distressed firms than among a sample of larger ones. Indeed, their resource set is smaller and it should thus much more rapidly be affected by a shock. In this sense, a private disorder or problems related to founder's succession can explain the failure of a small firm but they will rarely cause the failure of a large firm.

In addition, the results that come out from this analysis are, more generally, coherent with the literature on business failure. Indeed, even if they were not presented as specific EBFPs, the basic ideas underlying each (sub)pattern were already tackled in previous research.
Refering to the EBFP 1, Stinchcombe (1965) or Thornhill and Amit (2003) discuss the problems of badly-created firms. More precisely, Smallbone (1990) states that non-motivated entrepreneurs may be at the origins of a business failure. Castrogiovanni (1996) and Perry (2001) demonstrate the importance of written business plan and of pre-startup planning. Larson and Clute (1979) and Haswel and Holmes (1989) confirm that managerial incompetence or insufficient managerial competences are common failure factors. Bruno et al. (1987) analyze the failure of innovative firms and precise they are rather technology-oriented than business-oriented.
Concerning the EBFP 2, Boardman et al. (1981) and Gaskill et al. (1993) underline the danger of rapid expansion. Moreover, a lot of previous researchers stress the problems faced by nonreactive old firms (EBFP 3). O'Connor (1994), Ranger-Moore (1997), Henderson (1999), Sull (1999) or Kisfalvi (2000) are examples of researchers who underline the importance to remain flexible and responsive to changes.
Referring to the EBFP 4, Hall and Young (1991), Newton (1985) or Jaminon (1986) remind conflicting interests may explain a business failure. In addition, Kellens (1993) and Ooghe and Waeyaert (2004) underline that entrepreneurs who only serve their personal enrichment or who have fraudulent activities inevitably provoke the failure of their firm.

Conclusion

Based on a qualitative content analysis of the reasons for the failure of 208 Belgian distressed firms, the present paper proposes an original taxonomy of five major EBFPs for small firms, which are themselves detailed into several sub-patterns (Table 8).
The present research has the following interests. On the one hand, it reinforces previous literature in inducing an original taxonomy of five EBPFs which are focused on small businesses. The induced results are consistent with previous literature. In particular, they are coherent with previous research on explanatory business failure patterns and they can be related to the principles of the Life Cycle Theory (Penrose, 1952; Greiner, 1972; Adizes, 1979). Additionally, it brings new insights regarding the reasons for small business failures and it proposes several EBFPs that are related to the particular characteristics of small firms.

On the other hand, as the detection of the fundamental explanatory failure factors is the basis of failure prevention (Argenti, 1976), it is obvious that the identification of distinctive explanatory business failure patterns is of crucial importance for a better understanding and for a better prevention of small business failure. More concretely, it provides entrepreneurs, managers or external advisers with crucial information about the reasons for the failure of small firms. With reference to this information, they have thus it easier to detect the fundamental causes of failure and, then, to find adequate corrective strategies that would lead to a durable recovery (Argenti, 1976).

Nevertheless, even if it brings new insights about the reasons for the failure of small firms, the present study has currently some limitations and it provides suggestions for future studies about this phenomenon.

Firstly, even if “strategies” were implemented in order to ensure the validity and the reliability of this study (Morse et al., 2002), a qualitative research is usually presented as more subjective than quantitative research (Cooper and

<table>
<thead>
<tr>
<th>Table 8: Five main explanatory failure patterns amongst small firms</th>
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<tbody>
<tr>
<td><strong>Five main EBFPs</strong></td>
</tr>
<tr>
<td>1 BADLY-CREATED FIRMS</td>
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<td></td>
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<tr>
<td>2 FIRMS WITH GROWTH-RELATED PROBLEMS</td>
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<tr>
<td></td>
</tr>
<tr>
<td>3 NON-REACTIVE FIRMS</td>
</tr>
<tr>
<td>4 FIRMS SERVING OTHER INTERESTS</td>
</tr>
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<td></td>
</tr>
<tr>
<td></td>
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<tr>
<td>5 SHOCKED FIRMS</td>
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17 See section 2.4.
Schindler, 2000; Thiétart, 2003). Under these conditions, it would then be interesting to complete this study by a quantitative analysis of the available data.

Secondly, the present study concentrates on the identification of several explanatory failure patterns while, after an analysis of 208 small distressed firms, it is obvious out that, as already mentioned in the literature (Argenti, 1976; Newton, 1985), the business failure process is generally characterized by a sequence of unfavorable factors over time and that the same firm can share characteristics of several patterns, at least in successive stages of the failure process. In a future research, it would then be interesting to concentrate on the identification of various failure paths (or failure trajectories), which would describe the sequence of events from the origins of the failure of the firm until it is investigated by the Court of Commerce for a Commercial Inquiry, a Legal Reorganization or a Bankruptcy.

Thirdly, the present paper does not integrate the organizational and financial approaches of business failure. Actually it would be interesting to determine if, in the years or months preceding their detection by the Court, firms that exhibit a particular EBFP show similar financial symptoms. In other words, it would be interesting to determine if firms belonging to the same EBFP can be identified beforehand on the basis of publicly available data, i.e. financial information published in the annual accounts. If each EBFP leads to specific financial symptoms, it would thus be possible to have an idea about the fundamental problems of failure without having any access to internal information. In a preventive perspective to failure, this would be very useful because it would notably facilitate the work of the Court as well as the identification of key problems before the elaboration of a recovery plan.

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APPENDIX 1: The entry of small firms in a failure process (Crutzen and Van Caillie, 2009)

- **ENTREPRENEUR** (+ personal environment)
- **MACRO and COMPETITIVE ENVIRONMENT**

**RESOURCES**

**RESOURCE DEPLOYMENT**

- Learning and Innovation
- Operations
- Clients

Non-viable STRATEGIC POSITION

- Age
- LC
- Size
- Industry
### APPENDIX 2: Systematic analysis grid (based on the integrative model proposed in Appendix 1)

<table>
<thead>
<tr>
<th>General characteristics</th>
<th>External environment</th>
<th>Entrepreneurial environment</th>
<th>Resources</th>
<th>Resource deployment</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Case information</strong></td>
<td><strong>PESTEL environment</strong>: Political, Economic, Social, Technological, Ecological, Legal</td>
<td>Technical competences</td>
<td>Personality - Style of leadership (autocratic, etc.) - Charism</td>
<td>Immaterial resources</td>
</tr>
<tr>
<td><strong>Firm characteristics</strong></td>
<td><strong>Competitive environment</strong> - Customers - Suppliers - Competitors</td>
<td>Breath of managerial knowledge (across finance, marketing, operations, etc)</td>
<td>Interests researched in the firm</td>
<td>Human resources - Quality - Quantity</td>
</tr>
<tr>
<td><strong>Leaders’ characteristics</strong></td>
<td><strong>Ability to anticipate events</strong></td>
<td><strong>Ability to control the firm</strong></td>
<td><strong>Climate among leaders and/or shareholders</strong></td>
<td><strong>Financial resources</strong>: Capital/Financial structure, Cash flows, Profitability, Liquidity, Solvency</td>
</tr>
<tr>
<td><strong>Failure information</strong></td>
<td><strong>Accidental factors</strong> - Fire - Bribery - Etc</td>
<td><strong>Ability to control the firm</strong></td>
<td><strong>Climate among leaders and/or shareholders</strong></td>
<td><strong>Financial resources</strong>: Capital/Financial structure, Cash flows, Profitability, Liquidity, Solvency</td>
</tr>
</tbody>
</table>
- Output of the file (bankruptcy, recovery, reorganization, etc.)