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Is this the end? Investigating firm and individual level outcomes post-failure

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ABSTRACT

Research into entrepreneurial failure is increasing in prevalence. However, treatment of failure has tended to be at one level of analysis (firm or individual) and generally assumed a level of finality, marking the end of the firm, an opportunity, or, in some cases, entrepreneurial careers. In this paper, we interview 257 failed entrepreneurs and examine individual and firm level outcomes of entrepreneurial failure. Our results show that there are substantial levels of variance in regards to what happens to the firm and the entrepreneur post-bankruptcy. We discuss implications for future theorizing and research questions about entrepreneurial failure.

1. Introduction

Research on firm failure is a developing and increasingly important topic within the entrepreneurship literature. Most of this research, however, has focused on the well-being of the entrepreneur after failure through the study of emotional responses (Byrne and Shepherd, 2013; Jenkins et al., 2014; Shepherd, 2003) coping (Singh et al., 2007) and learning (Cope, 2011; Ucbasaran et al., 2013) overlooking what happens to the firm's assets and the employment status of the entrepreneur. The dominant focus on well-being after failure has assumed entrepreneurs need to recover from failure prior to continuing with a career in self-employment, neglecting entrepreneurs may be running more than one firm at the time of the bankruptcy, re-enter self-employment shortly after the failure, or seek alternative forms of employment. Focusing on what happens to the firm and individual after failure allows scholars to address a broader set of potential individual and firm level outcomes without being held to the dominant assumption that entrepreneurs need to recover from the failure prior to starting a new firm post failure. In turn, this allows us to extend research on firm failure to include additional firm and individual level outcomes that have yet to be fully addressed, such as the extent to which an entrepreneur views the failure as "the end" of their entrepreneurial careers and the extent to which the failure is part of an ongoing entrepreneurial journey (Sarasvathy et al., 2013).

Entrepreneurs who re-start directly after a bankruptcy, for example, may not view the failure as an end to their entrepreneurial careers but rather in the context of their entrepreneurial careers and the potential benefits and consequences of the failure for how they approach their next venture (Simmons et al., 2013; Ucbasaran et al., 2010). As a consequence, we argue that there is the potential for a processual view of failure, whereby firm failure is not treated as "the end" in and of itself but rather having a role in the further career of an entrepreneur. Additionally, entrepreneurs who run multiple ventures – portfolio entrepreneurs – who experience firm failure do not experience a break in the entrepreneurial careers. For them, they need to balance managing the failure with also running other businesses; however the extent of this phenomenon is unknown along with how the failure impacts the portfolio of

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firms they run.

At the firm level, it is implicitly assumed that as the firm has failed, it exits the market. This neglects that the firm may be continued – albeit in a different legal entity or form. This creates opportunities to explore the extent to which the same opportunity is continued under new management and the performance of the firm under this new management, providing a lens through which the role of individual opportunity fit (Shane, 2003). This particular instance extends the view of entrepreneurial failure as one being defined as when a firm exits the market to one whereby failure is one step to understanding how opportunities unfold over time and the role through which entrepreneurs can continue to pursue an opportunity despite failure.

To extend the focus of failure research beyond the individual level of analysis and its implications for well-being, we investigate what happens to the operations of the firm and the employment status of the entrepreneur after firm failure. We take a strict and objective definition of firm failure - bankruptcy - and illustrate that there is complexity in outcomes at the individual and firm level of analysis. The findings challenge the prevailing assumption that entrepreneurs need to recover from firm failure prior to continuing with self-employment after failure, while also establishing the avenues through which entrepreneurs do this. The findings also uncover that in approximately a third of the firms sampled, the operations of the firm continued either under old management or under new management despite the bankruptcy, suggesting that bankruptcy does not always imply the discontinuance of the firm's operations. This underlines the potential for entrepreneurial failure to be conceived of as a process that unfolds over time and ventures, as opposed to a static “event”.

2. Individual and firm level failure outcomes

The literature on entrepreneurial failure frequently assumes that failure encompasses the failure of the firm along with the failure of the individual (Cardon et al., 2011; Sarasvathy et al., 2013). While this is the case when taking a “snap shot” of the window under which a failing firm formally exits the market, a longer temporal approach to failure opens up for a more nuanced understanding of the outcomes of entrepreneurial failure (Sarasvathy et al., 2013). For example, the failed firm can be taken over by new management or the entrepreneur is able to start afresh after exiting the failing firm.

At the individual level, extant research has predominately focused on the well-being implications of failure. This subsumes that failure is conceptualized as a stressful event whereby entrepreneurs need to cope with the failure prior to being able to move onto new forms of employment (Shepherd, 2003; Shepherd et al., 2009). This overlooks that not all entrepreneurs experience a uniquely negative emotional response to failure (Byrne and Shepherd, 2014; Jenkins et al., 2014) and that entrepreneurs may seek alternative forms of employment to help address the immediate financial strain failure can pose. For example, entrepreneurs are more likely to transition in and out of hybrid status than from full immersion in self-employment to paid employment and vice versa (Folta et al., 2010).

In the literature on habitual entrepreneurship, failure experience has been incorporated to understand how it influences learning and performance (Eggers & Song, 2015; Rerup, 2005; Ucbasaran et al., 2010; Yamakawa et al., 2015). It has also shown that among individuals who re-enter self-employment after failure, they are likely to do so shortly after it (Yamakawa and Cardon, 2017). While research is beginning to understand the role of failure for habitual entrepreneurship, less is known about the nature of the firms entrepreneurs re-start or impact a single failure has for portfolio entrepreneurs.

At the firm level, extant research has focused on distinguishing between exit routes of distressed firms differentiating between bankruptcy, voluntary liquidation and restructuring through a merger or acquisition (Balcaen et al., 2011; Wennberg et al., 2010). In voluntary liquidation, the firm is dissolved and creditors repaid. In the case of bankruptcy, the firm's creditors are only partially paid and the firm's operations permanently closed (Balcaen et al., 2009). Frequently there are unpaid tax obligations which become the responsibility of the owner (Balcaen et al., 2009). Despite bankruptcy often being designed for a fresh start, research has neglected to focus on what happens to the firm's assets after small firm bankruptcy as it is assumed that the firm is permanently closed. This overlooks what happens to the liquidated assets and the extent they are redeployed to continue the business, albeit under new management.

Well-functioning bankruptcy laws enable entrepreneurs to obtain a second chance by providing a means in which they can exit their underperforming firms or re-structure them to continue their operations (Ayotte, 2007). Without such an option the entrepreneurs would take fewer risks and be more reluctant to introduce highly innovative products and services to market (White, 2001). Most research on bankruptcy and restructuring, however, has focused on relatively large (Thorburn, 2000) and/or publicly traded firms (Hotchkiss, 1995; Hotchkiss et al., 2008) where restructuring is a frequent outcome. Larger firms are more likely to file for bankruptcy under Chapter 11 which is designed to facilitate restructuring. This may not be as feasible or potentially economically useful among newer and/or smaller ventures, and is not an option in all countries. As a result there is limited knowledge about the outcomes of small bankrupt firms, which are more likely to file under Chapter 7 where the firm's assets are liquidated.

3. Method

In our empirical analysis we focus on bankruptcy, an objective firm-level conceptualization of firm failure (Jenkins and McKelvie, 2016), where the firm's assets are liquidated as part of the bankruptcy proceedings. We include in our sample frame all limited liability incorporated firms that filed for bankruptcy in Sweden during the four-month period of March 2010 to June 2010. This resulted in an initial sample frame of 1328 firms. Bankruptcy signals the formal exit of the firm as a legal entity under current management, while enabling a focus on what happens to the operations of the business and the entrepreneur post-bankruptcy.

We adopted a key informant approach and conducted telephone interviews with owner-managers of the bankrupt firms

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