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TO WHOM IT MAY CONCERN

Herewith to testify that each paper accepted for the 19th Annual Conference of the Southern African Institute for Management Scientists, 19-21 September 2007, Johannesburg has been peer-reviewed by two independent peer-reviewers.

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Critical variables of venture turnarounds: A liabilities approach

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ABSTRACT

Potential failure is a threat that businesses face during any stage of their life cycle while turnaround from decline is essential to protect from failure. The scientific literature on turnaround is however focused on strategy and process. This study’s line of enquiry firstly reviews the documented research (both theoretical and empirical) encompassing the phenomenon “turnaround”. The methodology applied is fundamentally based on an in depth literature review and grounded theory with a focus on classifying the identified relevant liabilities. Despite every situation’s uniqueness, the results suggest firstly that successful turnarounds are dependent on overcoming some universal liabilities. A conceptual framework is then proposed for liabilities associated with the turnaround situation. Secondly the results suggest that the odds against a successful turnaround are stacked against the turnaround manager. Successful turnaround depends on an integrated approach overcoming these liabilities. Finally the skills of the turnaround manager depend heavily on leadership and strategic management abilities, less on accounting and legal skills that rather suggest the investigation of a team approach to support the turnaround manager for future research.

(Key words: Recovery, Turnaround, Liability)

INTRODUCTION

Turnaround situations have become a potential threat for most business ventures somewhere in it its life cycle. Some ventures experience traumatic processes while others change direction successfully with less pain depending on where they hover between the extremes of the success-failure continuum. When closer to failure (distress, crisis or dissolution) the turnaround interventions differ in severity compared to when closer to the successful end state (under performance or decline). Each turnaround situation therefore has a unique set of preconditions that serve as barrier to overcome (Pretorius, 2006). The decisions that ventures are faced with and the potential consequences of failure have significant and interesting impacts on business decisions (Cybinski, 2001:31). In South Africa we have also now entered Chapter 6 of the proposed Companies act with its complicating effects. The appointment of a turnaround manager (supervisor) forms part of the newly proposed legislation.

While the literature is full of strategies during a turnaround, it is silent on turnaround situation liabilities that describe preconditions to overcome during turnaround. If reported, it is done sporadically and in isolation. If not reported, entrepreneurs embark on a process without grasping the realities of the situation. What exactly is a turnaround situation liability? What conditions are responsible for it? What key variables should be considered to overcome them? Finally, what are the general key knowledge and skills of the turnaround manager to overcome these liabilities? Should corporate and entrepreneurial ventures consider turnaround liabilities in the same way?
More so, is it important to know the answer to these questions? We need to clarify these liabilities to understand what faces the newly appointed turnaround manager.

Our approach was to identify critical variables from the scientific literature. Using the grounded theory approach to identify the variables, we then categorised them and finally identified the key liabilities of turnaround situations. We then propose a conceptual framework of the liabilities and propose the knowledge and skills associated with successful overcoming of the liabilities of the turnaround situation.

Both researchers and practitioners need to understand the liabilities for of the turnaround situation. Doing so, guide decision-making and judgment during the strategising process for successful turnarounds. Grasping how key liabilities of the turnaround situation impede decision-making and strategy choice better prepare the turnaround manager. Knowing the liabilities will give guidance about the skills requirements for a turnaround manager. These knowledge and skill elements are valuable to direct the selection criteria of such a person when necessary.

BACKGROUND TO THE STUDY

South African business is supportive of the long awaited business rescue legislation, which, in appropriate cases, should provide the best possible outcome for all stakeholders in distressed businesses. Chapter 6 of the proposed Companies Bill, 2007 introduce, for the first time in the South African context, business rescue and the appointment of a “supervisor” or as used in this text the “turnaround manager”. The broad intention of this chapter of the Act was to create a more conducive (debtor friendly) environment to successfully achieve business rescues. Chapter 6 does have apparent shortcomings which will open opportunities to capitalise on “loopholes” as case law will not be in evidence for a couple of years at least. It is therefore prudent that a prospective turnaround manager is cognisant of these “opportunities” and to accept the liability of these legal “loopholes”.

At the same time a debtor can in terms of section 132 can initiate a business rescue. This section requires, as a prerequisite for business rescue, the occurrence of an insolvency event or a belief that the company is or may imminently become insolvent. Initiation by a creditor in terms of section 134 merely sets out that an affected person may apply to Court to place the company under supervision if there is the occurrence of an insolvency event or a belief that the company is or may imminently become insolvent. An area that needs to be clarified is section 132(1)(b) which requires, as a prerequisite for business rescue, an apparent “reasonable prospect of rescuing the company”. Responsibility for determining the viability with regards the “reasonable prospect” will most probably fall within the ambit of the supervisor.

Regardless whether business rescue is instituted by way of resolution or by way of court order, the turnaround manager is appointed by the company (board). This aspect superimposes the critical liabilities faced by the turnaround manager. The company may make an inappropriate appointment due to lack of knowledge of business rescue and available business turnaround skills or purely due to a miscalculation of the real time business problem.

In a variety of case studies, the very reason that the company is in need of business rescue is mismanagement. It is therefore questionable if management is really equipped to assume responsibility for the appointment of the supervisor.

There is no indication in the Chapter what the prescribed or minimum qualifications of a turnaround manager referred to in clause 141(a) will be. As the company appoints the
turnaround manager, with no need to disclose the reasons for the appointment there is no way for affected parties to ensure that the turnaround manager has the necessary qualifications and meets the other requirements for appointment until after he is appointed. The extent of the turnaround manager’s duties is not sufficiently described; it is not clear whether the position of turnaround manager is a part- or full-time position. Section 143(1)(b) of the Chapter provides that the turnaround manager may approve or veto a “significant management decision” taken by the board.” In clause 130 (1) (f) a definition of “supervision” is given but it merely adds to the ambiguity surrounding the role of the turnaround manager. The turnaround manager is tasked with all the critical decision-making.

METHOD OF REVIEW

The specific research need identified in this study is one of better understanding and sense making rather than prescribing strategy although the two focuses are related and a large number of recent published works were in the field of turnaround strategy. The methodology adopted in this study was selected because primary data of turnarounds is limited (especially in developing countries) as failed firms disappear and successes are ascribed to the entrepreneur/manager or leadership. Even when the failed attempts do speak out, such explanations are likely to contain self-reporting and retrospective reporting biases (Shepherd, 2005:126). Reports on successful turnarounds are often quiet too, as the detail mostly involves elements of competitive advantage.

Scientific resources from the ABI-Inform, Ebsco-host, Proquest, Blackwell and other databases were searched for titles published since 1985. The date was somewhat arbitrarily determined (but not necessarily adhered to) based on convenience as this was the earliest date for which most databases had downloadable electronic titles, abstracts and full texts readily available. For apparent major works, the date was not a limitation especially when an article was referenced widely. Age of publication was not considered important but relevance and contribution to the body of knowledge of failure were paramount.

At first a search for “turnaround” combined with business, venture, firm or organization was conducted. All searches were keyword-based and narrowed down by using the different keyword variants identified during the process. As the articles (data) were obtained, searches were extended to include terms such as rescue, reversal, recovery and more. All articles were scanned based on titles and abstracts that led to a first complete reading of each article that were deemed to cover failure related issues similar to the method described by Forbes (1999:417).

Second and third round searches were conducted using author names in addition to keywords for cross-referencing. Thereafter specific journals were searched. Key journals included Journal of Business Venturing, Entrepreneurship Theory and Practice, Academy of Management Review, Sloan’s Management, Academy of Management Executive, British Journal of Management, Administrative Science Quarterly, Long Range Planning, Strategic Management Review, The British Accounting Review, Organisational Science, Journal of Small Business Management but were not limited to these. References of important articles were then searched and accessed to build up an extensive list of articles. Articles covering all turnaround related terms were investigated to identify more references. These articles were then obtained and the process repeated to identify the key works referenced by the different authors.

After reading (analysing) the abstracts of the articles, those papers that in fact represented turnaround related issues, as we understood it, were selected. Thereafter each article was assessed and key concepts were identified and reported. Concepts were categorised into sub-domains (categories) of turnaround related issues and reported individually with their specific
contributions based on Corbin and Strauss’s (1990:7). As the categories became clearer, each individual article was further explored for its key contributions. Initially rejected articles were then re-evaluated for potential contributions to the sub-domains and based on the new insights gathered through the process.

Eventually a list of key references was assembled. The process of adding articles was never officially stopped but drifted towards closure as no more “useful new information” came forth in accordance to the principles suggested by the grounded theory research process. This meant that the real number of articles screened became less important than initially anticipated when embarking on the study.

Finally a conceptual framework to classify the liabilities identified is proposed. Each article was scrutinized for confirmation of concepts, additional concepts and variances under different conditions and contexts. One of the principles of grounded theory research states the requirement for concepts to be repeatedly being present in the new data (Corbin and Strauss, 1990:7).

FINDINGS

An agency relationship exists whenever one party (the principal) delegates authority to another (the agent) (Combs, Michael & Castrogiovanni (2004:910). Agency theory suggests that because agents are assumed to be self-interested and possess goals that diverge from the principal’ goals, the principal must expend resources (agency costs) to ensure the agent act in their interests. In turnarounds the board or shareholders normally appoint a turnaround manager as agent to introduce a turnaround in the ailing business venture. This study argues that the turnaround manager faces several key liabilities associated with the turnaround situation that should be overcome if he/she wants to be successful in rescuing the venture from further decline. The liabilities have direct bearing on the decision-making of the turnaround manager and therefore the perceived results in comparison to the agency costs that are perceived by the board as principal.

Turnaround is defined for use in this study as: A venture has been turned around when it has recovered from a “decline that threatened its existence” to resume normal operations and achieve performance acceptable to its stakeholders (constituents) through reorientation of strategy, structure, control systems and power distribution. The turnaround definition implies that a declining firm can be rescued, while a firm that has failed cannot. Judicial actions are often associated with failed firms but less often with those in decline and very small ventures which enter and exit informally. The turnaround situation is the point in time that a turnaround is required and the appointment of a turnaround manager or alternative leadership is considered.

Liability is defined for use in this study as: A venture experiences a liability when it has to overcome some set of preconditions that limits its capacity to operate normally. Liabilities are situational deficiencies inherited from previous decision-making in the venture and are often referred to as “past decision baggage” that the venture is committed to at the turnaround situation. Liabilities originate from the resource-based view (Thornhill & Amit, 2003:500) and stems from previously identified liabilities such as liabilities of “newness, smallness, adolescence, obsolescence and senescence ” as described in the literature (Zacharakis, Meyer & De Castro, 1999:2; Shepherd, 2005:124; Kale & Arditi, 1998:459; Stanworth, Purdy, Price & Zafaris, 1998:56).
Facing the turnaround there are six liabilities that will be discussed in more detail. Figure 1 shows a conceptual framework of the key liabilities that face the turnaround manager. While the framework is the result of the research process, it is reported at this early junction to assist the discussion of the different liabilities.

Figure 1 Conceptual model of liabilities of a turnaround situation as faced by the turnaround manager (Own compilation)

Liability of Legitimacy

While boards normally appoint the turnaround manager as their agent it must be acknowledged that it could also be the result of the judicial process within the legal framework of the Company Act. Nevertheless, the turnaround manager faces legitimacy issues with other stakeholders such as creditors, staff, labour, unions, suppliers etc.

Legitimacy is derived from the Latin word *legitimare* which is clarified by Lewis and Short (1975:1047) as; “right, just, proper, appropriate, suitable, duly”. Legitimacy asks whether the turnaround manager is of the perceived capacity to successfully affect the turnaround given his/her credibility, reputation, knowledge, skills, track record, ability to muster resources, acceptability as a representative to all stakeholders and more. Barker, Patterson & Mueller (2001:239) use the term “reputational slack” which explains this legitimacy as part of the resources available to the turnaround management of a venture. A condition of turnaround manager legitimacy points to an element of “exchange power” where all affected parties (stakeholders) will support the appointee in exchange for economic prosperity and security. A further element required is “integrative power” which is derived from loyalty. The locus of
turnaround activity is spread through all affected parties. Employees stay in work, creditors paid and business contributes economically to the fiscal and society.

Much of what legitimacy is about refers to the so-called “soft issues” of a personal nature where someone could be knowledgeable and skilful and at the same time exhibit offensive behaviour and views that would make him/her an undesirable candidate to some stakeholders. Different stakeholders would support different attributes for example creditors would value someone with business and financial know-how who they think can protect their interests, revenue services would value auditing qualifications, the board would value a success turnaround track record and labour would probably value someone with a pro-labour reputation.

If the turnaround manager is appointed from “outside” it might aggravate the difficulty to achieve legitimacy especially during early stages. The way the turnaround manager is compensated may be perceived by some stakeholders as more than opportunity cost (quasi-rents) which may influence legitimacy perceptions negatively, making it harder to overcome another liability: leadership.

The liability of legitimacy is complex but crucial to overcome by whoever is appointed to lead the turnaround. It influences and is influenced by both liabilities of leadership and strategic options. This liability is created by the turnaround situation and affects the appointed of either a turnaround manager or new leadership (CEO) assigned to face it. It is therefore a universal liability inherent to the turnaround situation. While the focus of this study is on the turnaround manager, it is also stated that the venture itself may face the liability of legitimacy. The perceptions of creditors, suppliers, industry competitors and customers may challenge the legitimacy of a venture to engage in normal operations in the future.

**Liability of resource munificence**

Resource munificence refers to scarcity or abundance of critical resources needed when operating the venture (Castrogiovanni, 1991:542). Turnarounds are mostly attempted during advanced stages of the decline such as distress, crisis or dissolution and ventures typically experience tremendous resource scarcity. Resource slack is arguably the key determinant of both decline severity and the options for turnaround strategies chosen in response. Also referred to as “organisation capital” (Levinthal, 1991:418), munificence varies depending on previous decisions, organisational learning and history and is central to severity of the preconditions governing the turnaround situation. Alternatively referred to as “level of free assets”, Smith & Graves (2005:307) identify it as crucial in determining the success of turnaround interventions. Unabsorbed resource slack suggests increased ability to borrow funds and the ability to generate cash (liquidity) from the firm’s assets (Barker & Moné, 1998:1231), which give firms the ability and time to respond through recovery strategies.

Levinthal (1991) refers to negative changing organisational capital as the important determinant of firm mortality. Failure will happen if the minimum threshold for organisation capital is not met. The level of firm resources at the time of the turnaround attempt affects the declining firm’s capacity to implement strategic change. Maintaining adequate resources while responding to decline is often problematic because the decline process destroys firm resources over time (Barker & Duhaime, 1997:20). Cressy (2006:104) further measures the role of “management human capital” as part of the resource capital suggesting several aspects to the construct of resource munificence.
Environmental munificence (capacity to accommodate firms) has particular relevance for decline (Francis & Desai, 2005:1202; Castrogiovanni, 1991:543), as it determines the strategic options to choose from. Environmental munificence plays an important role in the description of preconditions and the ability of a firm to recover from decline. The matching of resource and environmental munificence is part of the turnaround process.

Resource munificence, although often incorrectly thought of as financial only in origin, is influenced by the other core principles. Pretorius (2006) argues that the leadership and origin of the distress (strategic vs operational) determine the resource slack. Resource munificence appears at the heart of the liabilities faced by a venture in decline.

While no one liability is more important than any other, all liabilities link through resource munificence whether directly or indirectly making resource munificence the main liability to overcome. The one liability that the turnaround manager must therefore overcome is the liability of resource munificence. The turnaround situation implies limited slack, which restricts the strategic options available to choose from. By default, the turnaround manager must therefore, gather information on the resources, analyse, evaluate and judge the resource situation. He has little control over it but if capable would be able to observe potential opportunities to improve slack and create manoeuvring space to strategise. The liability of strategy option is explored next.

**Liability of strategy options**

The origin of the causes of decline and failure is often categorised as either strategic or operational in nature (Robbins & Pearce, 1993:626). The literature reasons that it is easier for the business to respond to operational problems such as inefficiencies, cost relationships, incorrect resource applications and managerial deficiencies as there is room to manoeuvre and visibility of the contributing factors are better. In contrast, strategic causes have to do with weak or wrong positioning in the market, technological changes that govern demand determinants and loss of competitive advantage by the venture – all highly susceptible to external influences not clearly visible to the decision makers. Strategic factors have a close relationship with the external environment and the firm’s response to changes in that environment.

For a turnaround strategy to be effective in reversing decline, it has to address the declining firm’s core problem (Barker & Duhaime, 1997:14). A broad generalisation is therefore that if preconditions are strategically driven, it is more severe while it is less severe if coming from operational weaknesses. The rationale is that operational preconditions can be corrected with relatively ease and expectation of success while strategic preconditions requires directional change and high-risk expectations typically associated with new venture creation. Wrong choice of new strategy by the turnaround manager will therefore have a severe impact on potential recovery compared to wrong operational decisions.

Environmental munificence will also determine if certain strategies are viable, as “unforgiving environments” such as economic downturns make it harder to achieve successful turnaround than beneficial environments such as growing economies or when operating in growth industries.

It therefore stands to reason that ineffective turnarounds often occur when management fails to successfully diagnose causes of their firm’s decline and respond inappropriately (e.g. trying to increase efficiency when the firm’s weak strategic position is the cause of the problem (Barker & Duhaime, 1997:14) or vice versa. This then points to the leadership, which is discussed in the next liability.
Liability of leadership

Even the best strategy can fail if a corporation doesn't have a cadre of leaders with the right capabilities at the right levels of the organisations (Hsieh et al. 2005).

Although in this text the focus is on the turnaround manager, the liability of leadership is also relevant for alternative leadership bodies such as the “top management team”, the “new CEO” or “leadership team”. Probst and Raisch (2005) identify four elements associated with venture failure of which one is leadership and closely associated with leadership are the ability to change and organisation culture. While all three are “soft” issues it seems that the origin of decline (strategic vs operational) joint with the leadership’s inability to adapt to change on the one hand combine with its inability to create the needed culture to support the strategy on the other. Cannon & Edmondson (2005:302) suggest that managers have an added incentive to dissociate themselves from the causes of decline because most organisations reward success and penalise failure. Thus, holding an executive or leadership position in an organisation does not imply an ability to acknowledge one’s own failure.

It is almost always management problems that lead to business failure (Chowdhury & Lang 1993:15 citing Boyle & Desai 1991, Dunn & Bradsteet 1984, Edmunds 1979, McGuire 1976; Longenecker et al, 1999:503) and this has not changed since. Collard (2002:27) asks the question: If the leaders who were in power while the company’s position was allowed to deteriorate are still there, why should the lender believe that they would now be instrumental in correcting the situation? Indeed, a question that brings perspective to the leadership role of turnaround manager. The literature on turnaround from decline is lined with the appointment of new leadership when a firm has been in decline. Barker, Patterson & Mueller (2001:237) report that replacement of the top management team is a core element in the turnaround process and coins it “top management team sweepout” while Castrogiovanni, Baligwa & Kidwell (1992) reason that CEO replacement must be used only in severe turnaround situations such as crisis or dissolution.

At the same time Barker & Duhaime (1997:13) report that turnarounds stem from top management implementing cutback or retrenchment strategies that increase efficiency and retrenchment rather than from top management substantially reorienting the declining firm’s strategy and thereby confirming that the choice is solely dependent on leadership decision-making.

Chowdhury & Lang (1993:9) further suggest through threat-rigidity theory that when management faces a palpable threat (sudden crisis) they often freeze into inaction (experience cognitive rigidity) resulting in impaired decision-making that propels failure. This threat-rigidity theory is confirmed by Mellahi (2005:264) while Barker & Moné (1998:1228) postulate that leadership will tend to pursue more mechanistic strategies under pressure. Alternatively they suggest that when faced by gradual decline management fail to detect or could even ignore and deny the signs and causes responsible for it. This leads to forestalling actions to counter such decline. It seems that both cases contain an element of managerial thinking at the origin of the action process required to turn around from decline.

It therefore appears that leadership is at the core of all declines and failure causes and preconditions whether it is through their ability or inability to respond to environmental change, chosen strategies and implementation actions or any decisions (non actions and non-decisions) in response to the decline. Longenecker, Simonetti & Sharkey (1999:503) confirm the leadership liability when they identify “failure at the top” as the main cause of failure in business.
The turnaround manager is often not the official leader but must act many of the roles associated with the leader and influence the management team. The turnaround manager must therefore be able to influence leadership and management thinking within the company. Retrenchment is a crucial strategy but in a world with high unemployment staff retrenchment is seen as the last alternative available. The turnaround situation thus places additional pressure on the leadership ability of the turnaround manager.

**Liability of data integrity**

Decision-making depends on quality of information. Data integrity refers to correctness, completeness, wholeness, reliability and truthfulness of the data available for decision-making. In the turnaround situation data for decision-making is subject to misrepresentation, obscuring and suppressing for several reasons. Examples include inflated debtors to improve balance sheets, overestimated sales projections that inflate demand figures, manipulated inventory projections, overvalued assets, incorrect attributions of causes to protect positions and withholding of certain information to protect vulnerable projects and more. While some of these cases may be intentional, there are also those that are unintentional such as biases, heuristics of perceptive shortcuts.

Only a very small portion of all data requirements for determining the turnaround situation is financial in nature and available through the standard statements. A large amount of data is also subjective and opinion based confirming its susceptibility to errors of human nature. The turnaround manager depends to a large extent on the management to supply reports and data interpretations that are subject to biases and other limitations.

Verification and authentication of data is a time consuming process – time which is not abundantly available at the turnaround situation. The liability of data integrity depends on the turnaround manager’s ability to verify and authenticate data for decision-making. The complexity of data integrity is explored shortly. Not verifying data regularly lead to assumptions and contribute to poor strategy choices.

Barker & Barr (2002:963) report on the impact of the top management team as the key contributor to decline and failure if they fail to change strategies. The influences of the top management team cognitions are important influences on the decisions that influence the organisations performance. They suggest that how the top management team perceives the causes of failure determines the extent of their recovery actions. The turnaround manager is subject to these cognitions as the top management team is a key source of information. They may frame the requested information according to self-serving benefits and based on their specific knowledge structures influencing the data integrity.

Leadership is further subject to heuristics and biases of management through overconfidence (Shepherd 2005:125), escalation of commitment (Shepherd, 2005:129), risk perception and misconceptions (Le Roux, Pretorius & Millard, 2006). These biases influence leadership to be termed boiled, drowned or bullfrogs by researchers (Bollen et al. (2005). The turnaround manager must therefore overcome these elements by first identifying them and thereafter acting accordingly. In each case data integrity is undermined through escalation of commitment bias, overconfidence, misconceptions and filtered data.
Table 1 describes how data integrity is subject to some human errors, biases and heuristics. It is self explanatory about how it influences the decision-making of the turnaround manager and confirms the ease of communication breakdowns.

Table 1  Heuristics, biases and thinking shortcuts associated with the liability of data integrity of the turnaround situation

<table>
<thead>
<tr>
<th>Bias / heuristic / human error</th>
<th>How it impacts on data integrity</th>
<th>Author</th>
</tr>
</thead>
<tbody>
<tr>
<td>Misconceptions</td>
<td>Tendency to overestimate demand, underestimate competitive response and underestimate resource requirements.</td>
<td>Le Roux et al. (2006)</td>
</tr>
<tr>
<td>Escalation of commitment bias</td>
<td>Tendency to support previous decisions made even if they contributed to decline.</td>
<td>Shepherd (2005:129)</td>
</tr>
<tr>
<td>Self-serving bias</td>
<td>Take credit for success and blame other for failure that influences how one identifies the problem and how information is framed.</td>
<td>Barker &amp; Barr (2002)</td>
</tr>
<tr>
<td>Selective perception</td>
<td>Depending on previous experience of what works and ignoring signals that is “off the radar”.</td>
<td>Barker (2005)</td>
</tr>
<tr>
<td>Illusion of control bias</td>
<td>The belief of management that they can control certain elements that is actually beyond their control.</td>
<td>Le Roux et al (2006)</td>
</tr>
<tr>
<td>Overconfidence</td>
<td>The belief of management that they can achieve results despite the viability showing otherwise.</td>
<td>Shepherd (2005:129)</td>
</tr>
<tr>
<td>Paying too much attention to salient data</td>
<td>Related to selective perception, focus is now only on salient and obvious and “reliable” sources</td>
<td>Barker (2005)</td>
</tr>
<tr>
<td>Problem framing</td>
<td>If preconditions are perceived as serious the problem will be perceived differently leading to selecting more aggressive strategies for turnaround. For example if a less hostile environment is perceived then the problem is framed with more slack on decision and conservative actions are proposed.</td>
<td>Barker (2005)</td>
</tr>
<tr>
<td>Relying on filtered data</td>
<td>In trying to reduce information overload - focus is more on reports and statements which only confirm the failure but do not show causes – especially financial statements</td>
<td>Barker (2005)</td>
</tr>
</tbody>
</table>

**Liability of integration**

Integration is best explained metaphorically. Like an orchestra with different instruments the piano cannot take the role of the flute or guitar and individually they have limitations. However, when they are tuned in on each other they can create beautiful music. The conductor, who makes sense of the different elements and their roles, is able to direct them playing together successfully.
Overcoming the liabilities described so far requires an integrated approach to assimilate different strategies, activities and people in a holistic way as to create “critical mass” for the successful implementation of the turnaround plan. Integration requires a concerted effort to implement strategy through cost cutting in operations and divisions, increasing sales, influencing and motivating staff to achieve goals, improve efficiencies, creating working capital, restructure finance and more. Integration requires the ability to see the big picture and affect the detail actions of the process at the same time.

A simplistic presentation of integration and overcoming the liabilities during the turnaround may look as follows. Integration of the turnaround actions needs support from all stakeholders - thus overcoming liability of legitimacy. To assemble slack to free-up working capital to fund the turnaround suggest partial achieving resource munificence that requires knowledge of cash generating strategies (strategy options). Leading staff to implement plans on a wide front suggest overcoming the liability of leadership. Decisions of this nature depend on verification and authentication of data used in the decision-making process suggesting overcoming the liability of data integrity.

**DISCUSSION OF THE FINDINGS**

Regardless whether business rescue is instituted by way of resolution or by way of court order, the turnaround manager (supervisor) is appointed by the company. This aspect superimposes the critical liabilities of the turnaround manager. The company may make an inappropriate appointment due to lack of knowledge of business rescue and available business turnaround skills or purely due to a miscalculation of the real time business problem.

The liabilities identified confirm that the turnaround manager faces a task of immense proportions. The knowledge and skills required to overcome the identified liabilities suggest that there would be very few individuals that have what is required for a successful turnaround. There is no indication in Chapter 6 what the prescribed or minimum qualifications of a supervisor referred to in clause 141(a) will be. As the company appoints the supervisor, with no need to disclose the reasons for the appointment there is no way for affected parties to ensure that the supervisor has the necessary qualifications and meets the other requirements for appointment until after he is appointed.

The extent of the Supervisor’s duties is also not sufficiently described; it is not clear whether the position of supervisor is a part- or full-time position. Section 143(1)(b) of the Chapter provides that the supervisor may approve or veto a “significant management decision” taken by the board. ” In clause 130 (1) (f) a definition of “supervision” is given but it merely adds to the ambiguity surrounding the role of the supervisor.

Table 2 proposes some of the generic knowledge and skills associated with successful overcoming of the liabilities. To find these knowledge elements and skills in one person is no easy feat and could be described as the first prize. Naturally a team approach (second prize) would alleviate the burden of one person overcoming all the liabilities. Teams however command higher rents (transaction cost) which inherently aggravates the resource munificence liability and simultaneously the principal-agent problem.
Table 2  Knowledge and skills required to overcome the liabilities faced by the turnaround manager

<table>
<thead>
<tr>
<th>Liability</th>
<th>Knowledge requirements</th>
<th>Skills requirements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legitimacy</td>
<td>Legal framework of relevant acts</td>
<td>Personal credibility</td>
</tr>
<tr>
<td></td>
<td>Financial</td>
<td>Interpersonal skills</td>
</tr>
<tr>
<td></td>
<td>Personal credibility</td>
<td>Reputational slack</td>
</tr>
<tr>
<td></td>
<td>Interpersonal skills</td>
<td>Musterling support</td>
</tr>
<tr>
<td>Resource munificence</td>
<td>Sales and markets</td>
<td>Diagnostic skills</td>
</tr>
<tr>
<td></td>
<td>Operations / Logistics</td>
<td>Analysing skills</td>
</tr>
<tr>
<td></td>
<td>Human resources</td>
<td>Conceptualising preconditions</td>
</tr>
<tr>
<td></td>
<td>Management, Efficiencies / effectiveness</td>
<td>Learning from experience</td>
</tr>
<tr>
<td></td>
<td>Environmental munificence</td>
<td>Ability to read preconditions</td>
</tr>
<tr>
<td></td>
<td>Diagnostic skills</td>
<td>Strategic formulation</td>
</tr>
<tr>
<td>Leadership capacity</td>
<td>Situational leadership</td>
<td>Influencing capability</td>
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<tr>
<td></td>
<td>Experience of leading people</td>
<td>Vision / Direction</td>
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<tr>
<td></td>
<td></td>
<td>See the big picture</td>
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<td>Problem solving skills</td>
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<td></td>
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<td>Style (severity dependent)</td>
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<td></td>
<td></td>
<td>Create a new culture</td>
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<tr>
<td>Strategy options</td>
<td>Strategic management</td>
<td>Innovative thinking</td>
</tr>
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<td></td>
<td>Industry knowledge</td>
<td>Advanced strategic Management skills</td>
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<td></td>
<td>Environmental interactivity</td>
<td>Entrepreneurial thinking</td>
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<td></td>
<td>Cause-effect relationships</td>
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<tr>
<td>Data integrity</td>
<td>Basic financial knowledge</td>
<td>Basic financial skills</td>
</tr>
<tr>
<td></td>
<td>Taxation implications</td>
<td>Use of financial information</td>
</tr>
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<td></td>
<td>Financial ratios</td>
<td></td>
</tr>
<tr>
<td>Integration</td>
<td>Wide understanding of general business principles</td>
<td>Ability to integrate</td>
</tr>
<tr>
<td></td>
<td>Sales, marketing, operations and strategy interactions</td>
<td>Ability to implement</td>
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</table>

The complexity of the turnaround situation and the liabilities to overcome by the turnaround manager opens a can of worms for different stakeholders. Banks, for example, may lose their power as primary creditor over decision-making in the venture within the new rescue legislation. New and innovate strategies are required to find flags that would warn earlier than traditional “early warning signals” to enable management to act pro-actively and eliminate turnaround situations completely. The liabilities suggest alternative roles above that of a creditor for banks to play such as influencing the appointment of turnaround managers or radical strategies such as setting up units to fulfil these roles at low agency cost but benefiting through protecting their “assets”.

**MANAGEMENT IMPLICATIONS**

This study has specific implications for five groups: practitioners, boards, government, financial institutions and academics. Firstly practitioners can use the liabilities to improve their checklists and procedures to ensure that additional issues illuminated by this study are incorporated in their processes. Doing so would guard against oversight and protect them against personal liability
and the argument of quasi rents (too high agency costs). At the same time and secondly boards who need to appoint turnaround managers obtain directions for the selection of such individuals.

Thirdly government, as the law makers can use the guidelines for knowledge and skills required for a turnaround manager to guide compilation of minimum requirements. At this junction there is a high level of speculation and jockeying by different organisations to influence minimum requirements for the appointment of turnaround managers as to ensure exclusivity to certain groups such as chartered accountants only. This study has emphatically shown that financial skills are but a small segment of the knowledge and skills required for successful turnaround. This study challenges some elements of the appointment of a supervisor as proposed in Chapter 6 rescue legislation.

Fourthly financial institutions as the primary credit providers benefit from this study as it exposes several weaknesses of the proposed legislation with potential to expose creditor’s future actions. As a key role player (stakeholder) they could use the liability of legitimacy to protect their “stake” in turnaround ventures.

Finally academics can use the liabilities to teach the complexity of turnarounds so it supplies research data in an area which is generally under researched in South Africa. It is hoped that this study will stimulate further research in this field as to build a body of knowledge for turnaround and strategic studies. Table 2 has already contributed to the framework of turnaround training courses and should guide development of the same.

STUDY LIMITATIONS AND FUTURE RESEARCH

Limitations of one study should serve as challenges for future research. Firstly the grounded theory approach depends to some extent on the interpretation by the researchers and is therefore subject to their own biases and mental structures as determined by background and experiences. While every attempt was made to not fall into these traps, the researchers are still subject to this natural phenomena.

Secondly, no empirical data is presented though some of the articles used to support the concepts have statistical support. The limited nature of data in South Africa eliminates this option to some extent and in-depth research of case studies is proposed to find support for the different concepts.

Finally, this study ventures to the frontier of conceptual research in this field. It thereby challenges other researchers to find support for the liabilities or challenge their existence with primary data.

REFERENCES


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Hiesl, 2005


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