Transeo Academic Awards 2012

# *Understanding the Continuation of Firm Activities when Entrepreneurs Exit their Firms: Using Theory of Planned Behavior*

**Hannes Leroy, Sophie Manigart, Miguel Meuleman, Veroniek Collewaert**

**Vlerick Leuven Gent Management School and Ghent University**

After having been largely neglected in the entrepreneurship literature, an emerging body of literature acknowledges entrepreneurial exit as being a vital part of the entrepreneurial process (DeTienne 2010). Initially, scholars mainly focused on exit at the firm or industry level (for example, Hannan and Carroll 1992; Sarkar, Echambadi, Agarwal, and Sen 2006). More recently studies have focused on exit at the individual level, acknowledging that entrepreneurs are driven by their own, unique intentions and motivations when making decisions (DeTienne and Cardon 2010; Wennberg, Wiklund, DeTienne, and Cardon 2010). While research is starting to shed light on some of the reasons why entrepreneurs exit their firms, little attention has been paid to what happens to the firm itself when the entrepreneur exits. This is important because entrepreneurial exit may have an important impact on the future success and strategic course of the company (Bamford, Bruton, and Hinson 2006; DeTienne 2010).

With this paper, we aim to address this gap in the literature by using the theory of planned behavior (TPB, Ajzen 1991) to explain whether an entrepreneur decides to sell rather than to liquidate his or her firm when leaving and hence whether the firm will continue its activities or will cease to exist. We argue that an entrepreneur's personal attitude, subjective norms towards and perceived behavioral control over firm sale influence an entrepreneur's intention to sell and subsequently the probability of an entrepreneurial firm being sold rather than liquidated. While TPB has mostly focused on modeling behavior that is under an individual's complete volitional control, it allows for incorporating behavior over which an individual has limited volitional control (Ajzen 1991; Netemeyer, Burton, and Johnston 1991) such as the sale of a firm. In an entrepreneurial context, previous studies have highlighted TPB's validity for explaining firm growth (Delmar and Wiklund 2008; Wiklund and Shepherd 2003), which is also an example of behavior that is complex and subject to external constraints.

In this study, firm sale refers to the full transfer of ownership to other parties (for example, family members, employees or external parties) who will continue the firm's operations. It hence includes situations of family succession, either to children or to other family members. Liquidation pertains to the voluntary closure of a firm whose asset proceeds are sufficient to repay all liabilities (Balcaen, Manigart, Ooghe, and Buyze 2011). Both are at least partially under the control of the entrepreneur, whereas a bankruptcy, another important form of discontinuation, is the result of external selection mechanisms. A bankruptcy is typically forced by creditors or court as a result of a firm's failure to fulfill payments (Balcaen, Manigart, Ooghe, and Buyze 2011; Prantl 2003).[1] Given that bankruptcies are legally-induced and involuntary, the applicability of TPB in explaining bankruptcies may be limited; bankruptcies are therefore not included in the current study.

We explore how both entrepreneur and firm characteristics impact the probability of firm sale versus liquidation through their effect on the entrepreneur's sale attitudes and intentions. More particularly, we study the impact of psychological ownership, perceived volition and human capital at the level of the entrepreneur as well as the impact of the number of employees and being a multi-generation family firm at the company level. While

[1] In some cases, entrepreneurs rather than creditors will go to court to file for bankruptcy. They only do so, however, when they are forced to, that is when the value of the firm's assets is lower than the value of its liabilities. If asset value exceeds liabilities, voluntary liquidation will be preferred, as this preserves more value for all stakeholders, including the entrepreneur.

the entrepreneur's human capital (i.e. experience and education) and the number of people employed by a firm have been studied before in relation to exit (for example DeTienne and Cardon 2010; Gimeno, Folta, Cooper, and Woo 1997), we aim to shed more light on the processes through which they affect entrepreneurs' intentions and the subsequent sale or liquidation of their firm. Further, while the effect of psychological ownership and perceived volition have not been examined in this context, the former is expected to be one of the key drivers of entrepreneurs' attitudes towards firm sale versus liquidation (DeTienne 2010). In our particular context, psychological ownership refers to a state of mind in which entrepreneurs feel as though they possess their firms, either material or immaterial (Pierce, Kostova, and Dirks, 2001) whereas perceived volition refers to the extent entrepreneurs perceive the decision to exit their firms as a voluntary one. Finally, we examine the impact of being a multi-generation family firms as compared to a first generation family firm as scholars have recognized that the context in which entrepreneurs are embedded also plays a crucial role in the exit process (Justo and DeTienne 2008). Additionally, previous research has indicated that generational factors can substantially influence strategic decisions, such as financing decisions, in family firms (Westhead, Howorth, and Cowling, 2002; Molly, Laveren, and Jorissen 2011).

We examine the influence of entrepreneur and firm characteristics on firm continuity using a sample of 175 sold or liquidated micro-sized businesses in Belgium. These firms employ fewer than ten employees and are of huge importance to the economy, representing 92 percent of all European companies (Eurostat 2011). Firms of such small size are basically an extension of the entrepreneur, resulting in those individuals playing a crucial role in strategic decision making, including the decision whether or not to continue the firm's activities (Chandler and Hanks 1994; Liberman-Yaconi, Hooper, and Hutchings 2010). We explain the key findings below.

First, the results of this study largely confirm the relationships suggested by TPB. In order of importance, perceived behavioral control, personal attitudes and subjective norms predict an entrepreneur's intention to sell his or her firm. In turn, intentions to sell account for most of the variance in actual firm sale. This suggests that firm sale is a planned behavior as depicted by the TPB-model: entrepreneurial attitudes towards firm sale explain intentions and behavior. This confirms that TPB is not only applicable to actions that are completely under the volitional control of an individual, but also to actions that involve decisions of third parties (the buyers).

Second, our results confirm that an entrepreneur's personal attitude towards sale is positively influenced by the extent to which he or she perceives firm exit to be a voluntary event. No main effect was found for psychological ownership (PO). The failure to uncover a statistically significant effect may be driven by the limited variation in the psychological ownership variable as most entrepreneurs presented high levels of emotional attachment to their firms. The latter should not be surprising as the firm is generally seen as an extension of the individual entrepreneur in micro-sized businesses (Chandler and Hanks 1994).

Third, the pressure felt to sell a firm and continue its activities under new ownership increases when the firm has more employees and has been under multiple generations of family ownership. This provides support for the argument that context should be integrated into the study of firm (dis)continuation (Justo and DeTienne 2008).

Finally, entrepreneurs' general human capital, proxied by entrepreneurial and management experience, is positively related to their perceived behavioral control over selling their firm. This is in line with the argument that larger stocks of general human capital should make entrepreneurs feel more capable of selling their firm, positively impacting their goal-directed efforts to do so. No effects were found for the entrepreneur's education level and for his or her specific human capital. Our (lack of) results are consistent with those of Wennberg, Wiklund, DeTienne and Cardon (2010) who found that entrepreneurial experience, but not education, increased the probability of a firm being sold rather than liquidated. DeTienne and Cardon (2010) also found a similar, insignificant effect of education on entrepreneur's intentions to exit by sale or liquidation. The lack of an effect for specific human capital could be explained by the lack of variation in the sample. Most entrepreneurs of micro-sized firms have not had substantial experience in selling firms.

We believe the results of our study may also inform the broader exit literature. Given the focus of our research on the entrepreneur's decision whether or not to sell the firm upon his or her own exit, we adopted TPB as a theoretical framework because it models behavior as the result of an individual decision-making process. Consequently, TPB may also provide an interesting theoretical lens to study individual-level exit, such as investor exit or entrepreneurs leaving their entrepreneurial teams. For instance, an entrepreneur's attitude towards going public or selling his or her own shares to his co-founders may also positively affect his or her intentions to do so, which in turn may enhance the probability of his or her individual exit actually occurring. While some antecedents of exit attitudes, subjective norms and perceived behavioral control may be similar to those in the current study, others are likely to be different. For instance, when examining subjective norms towards going public, more relevant factors to study may include the amount of venture capital financing received because initial public offerings (IPOs) are the preferred exit mode of such financiers. As such, entrepreneurs may then feel more pressured to exit through an IPO than through selling their shares to co-founders.