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# Managing human resources in small organizations: What do we know?

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**Abstract**

While much of our knowledge concerning traditional HR topics (e.g., recruiting, compensation, or performance management) in large firms may also apply in small or emerging organizations, evidence suggests that new ventures are different and that management of people within them may not clearly map to management within larger, more established organizations. This paper reviews extant research on managing people within small and emerging ventures and highlights additional questions that have not yet been addressed. Our review suggests that as scholars, our understanding of the HR issues important to small and emerging firms is limited. While we have begun to understand how these firms should hire, reward, and perhaps even motivate their employees, we lack much of the theory and data necessary to understand how small and emerging firms train their employees, manage their performance, promote or handle organizational change, or respond to potential labor relations and union organization issues. The existing literature presents an often-confounded relationship between size and age, between the issues important to small firms and the issues important to young ones. Given the potential early HR decisions have to impact the organization's downstream success, it is important that we understand how these functional areas of HR (as well as their integration and evolution) affect small and emerging firms, and how the HR decisions made during the formative stages of firm development impact the firm's long-term goals.


*Keywords:* Human resource management; Entrepreneurship; Small firms

## 1. Introduction

"Firms profess that people are the source of their competitive advantage, whether they be technological experts, accommodating customer service experts, or visionary managers...At a time of unparalleled

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technological development, it is the human resources that paradoxically spell success or failure for all firms, and especially entrepreneurial ones" (Katz, Aldrich, Welbourne, & Williams, 2000, p. 7).

In a recent special issue of *Human Resource Management Review*, Baron (2003, p. 253) argued that the field of human resource management could benefit from looking more closely at HR processes within new and small firms. He suggested that new ventures started by entrepreneurs offer a "unique and potentially valuable business context for testing the principles and theories of HRM." Human capital in new ventures has been recognized as critical to venture success for some time (Deshpande & Golhar, 1994; Hornsby & Kuratko, 1990), but it is only recently that scholars have meaningfully explored this aspect of new venture creation. In order to successfully add to the literature on HRM in entrepreneurial ventures, it is essential to know what work has already been done, and what we still do not understand well about new venture HRM. This paper reviews what we know about HRM in entrepreneurial organizations in order to highlight important gaps in this understanding.

An emerging area of study has focused on the role of the founder in new venture creation, specifically on the characteristics of those individuals, such as leadership (Vecchio, 2003), self-efficacy, perseverance, risk-taking ability, and role transitions they experience during venture emergence (e.g., Johnson & Bishop, 2002). This stream of research is clearly essential to our understanding of new ventures, including their development process and their performance. However, the focus on the entrepreneur or founding team as the only source of human capital fails to recognize the important role that other employees in the new venture may play.

We know that as new firms grow in sales or production rates, they must also grow in the number of people they employ. However, few studies have examined how these individuals are recruited, hired, trained, motivated, or rewarded for their contributions to the venture (for recent notable exceptions, see Katz & Welbourne, 2002). While much of our knowledge concerning these traditional HR topics in large firms may also apply in small or emergent ventures, evidence suggests that new ventures are different and that management of people within them may not clearly map to management within established organizations (Barber, Wesson, Roberson, & Taylor, 1999). For example, new and small firms may have more difficulty recruiting employees (Williamson, Cable, & Aldrich, 2002) and often lack formal HR policies or systems (Markman & Baron, 2003). In general, liabilities of newness and smallness leave new ventures with fewer resources and greater challenges than their large established organization counterparts (Stinchcombe, 1965). Moreover, although not often clarified in the literature, issues concerning smallness and newness are not necessarily the same for entrepreneurial organizations, as some small firms are simply emerging nascent firms that will continue to grow as they become more established, while other small firms are already well established yet remain small for the life of the venture.

Keeping these distinctions in mind, we use a functional HR framework to explore extant literature on HRM in small and emerging organizations. While a functional approach to human resource management research has been criticized (e.g., Heneman, 1969; Ulrich, 1997), traditional HR topics are widely understood by both scholars and entrepreneurs and therefore offer a useful framework for highlighting currently underdeveloped areas of inquiry concerning managing others in emerging ventures. Furthermore, even recent theoretical frameworks that seek to move us past a functional HR view (e.g., Heneman & Tansky, 2002) still incorporate common HR practices such as compensation, staffing, and training in their model. This suggests that a functional perspective of HR remains valid, and we use this framework through the paper.

The purpose of this paper is to review research on managing people within new ventures and to highlight additional questions that have not yet been addressed. Within each section below, we provide a table that summarizes academic journal articles and book chapters about each area of HR in an entrepreneurial context and discuss key questions that need additional study. In these tables, we distinguish between theoretical and empirical papers and note whether each article discusses small or medium, and emerging or established firms, if such a distinction could be found. After reviewing prior research in the areas of recruitment and selection, compensation, training and development, performance management, organizational change, and labor relations, we suggest that we do not yet have much theory or data concerning issues of training, performance management, organizational change, or labor relations in small and emerging firms. Therefore, our understanding of key HR challenges in emerging ventures, including establishing firm identity and legitimacy, attaining critical skills and capabilities, maintaining flexibility, and developing sustainable practices is limited. Further, underlying these functional areas are three fundamental aspects of human resource management we do not yet understand in this context: retention and ongoing employee issues, the integration and interaction among HR practices, and the development and changes in HR practices throughout firm emergence. After reviewing what we already know about managing nonfounder employee assets in new ventures, and recognizing what we have yet to understand, these areas for additional inquiry and for greater synergy between HR and entrepreneurship will be discussed. First, we explore further the distinction between small and emerging ventures and explain our approach to reviewing relevant literature.

## 2. Liabilities of smallness and newness are real, but distinct

Entrepreneurial firms face unique burdens, based on their youth and small size at inception. These two liabilities, shared by many entrepreneurial ventures, present distinctly different challenges, both for the entrepreneurial firm and for human resource management within the firm. Young firms face the liabilities of newness, or the challenges of entering unknown industries or groups. They must find ways to gain legitimacy in the industry without the track record that experience and performance often provide (Hannan & Freeman, 1984; Stinchcombe, 1965). Small firms, regardless of age, face the liabilities of smallness and often lack the resources required to seek out new opportunities or, in many cases, to weather bad markets or periods of heavy competition (Bruderl & Schussler, 1990; Ranger-Moore, 1997). These firms must form alliances, purchase opportunities, and tailor themselves after more successful or larger firms in order to gain access to the resources they require to grow (Aldrich & Fiol, 1994). While virtually all emerging firms are small at inception, not all small firms are emerging, and thus the challenges such firms face may primarily concern resource constraints rather than legitimacy and experience deficiencies.

In entrepreneurial firms, the liabilities of both smallness and newness are likely to manifest themselves in how the firm addresses human resource issues. In small firms, where resources are likely to be scarce, there may be a very small number of formal HR departments or professionals, increased difficulty in recruiting and retaining employees due to lack of financial resources, and an increased reluctance to engage in costly or restrictive practices. In young firms, where experience is likely to be lacking, we may expect to see a reduced reliance on formalized training, difficulty recruiting due to lack of legitimacy, and more informal and potentially haphazard employee management systems. In both cases, the distinct liabilities presented in size and age make the study of human resources in entrepreneurial firms different than the study of them in large and established firms, as evidenced in both the scholarly and practical press (Heneman & Tansky, 2002). Small firms face many unique HR challenges (Greening, Barringer, & Macy, 1996), including an often ambiguous firm identity that is easily impacted by new employees (Cardon & Tolchinsky, in press), difficulty in attracting and retaining key talent and skills (Barber et al., 1999; Williamson et al., 2002), lack of legitimacy as an employer organization (Williamson et al., 2002), maintaining flexibility in staffing (Cardon, 2003), and developing sustainable human resource policies that endure market and organizational fluctuations. A graphic depiction of these challenges, and the HR systems that may help address them, is in Fig. 1. In short, “Human resources are critical for new organizations in ways often unappreciated by researchers who study only established organizations” (Katz et al., 2000, p. 7).

Because management of HR in small firms poses challenges distinct from those of their larger firm counterparts, several scholars maintain that further study of HR in small firms is warranted. We contend, as have others (e.g., Heneman & Tansky, 2002), that organizational approaches to staffing, compensation, training and development, performance management, organizational change, and labor relations have profound effects on the firm’s ability to address these challenges and therefore on the firm’s effectiveness and survival. Moreover, not all entrepreneurial firms are the same, and therefore distinctions in the size of the firm (small or medium) and the firm’s life cycle stage (emerging or established at a minimum) are important.

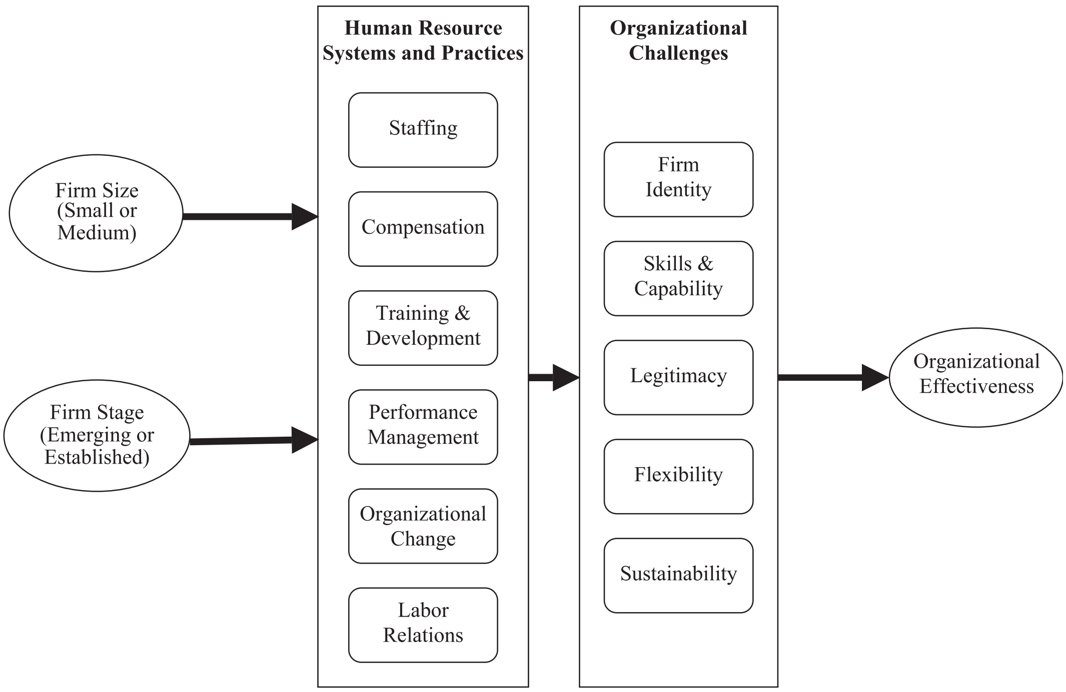


Fig. 1. Conceptual overview of literature on HRM and entrepreneurship.

We sought out scholarly articles concerning human resource practices in entrepreneurial organizations, as defined by the authors of those articles. We found 83 articles across several journals in general management (*Academy of Management Journal*, *Strategic Management Journal*, and *Administrative Science Quarterly*), entrepreneurship (*Journal of Business Venturing*, *Journal of Small Business Management*, and *Entrepreneurship Theory and Practice*), and human resource management (*Human Resource Management Review*, *Human Resource Management Journal*, and *Human Resource Planning*), as well as several scholarly book chapters in this area. We then coded each article to determine if it was theoretical or empirical and the size and life cycle stage of the organizations it discussed.

Of the 83 articles we originally began with, we eliminated over half based on one of three criteria. First, we removed the articles contained in the popular press and textbooks, as our aim was to explore the scientific examination of entrepreneurship and HR. We also removed a substantial number of articles that deal specifically with medium- or large-sized firms, given our interest in maintaining a small-firm perspective. Finally, we eliminated articles that addressed HR issues in all organizations, or where the analysis of issues affecting small firms was only conducted as a result of the sample taken. In these instances, the research questions were not driven by entrepreneurship—entrepreneurship played a role only in that entrepreneurs were part of the sample. In the end, 37 articles survived this evaluation.

This review of the literature on HR in small and emerging firms was somewhat troubling, as we discovered that many papers do not distinguish whether they are talking about small or large firms, emerging or established firms, or even small or medium enterprises, as the term SME (which includes firms ranging from 1 to 250 employees) indicates. The management needs of a firm of 1, 10, 50, and 250 are significantly different, so to co-join these organizations into one overall category is problematic. In particular, of the 37 articles we reviewed, 16 of them confound emerging and small ventures, making no distinction between them, and thus failing to clarify the different HR challenges resulting from newness and smallness and how they are overcome. Twenty-three of the articles confound small and medium enterprises, and less than half of them are based on empirical data. In most cases, the articles reviewed focus on issues of smallness rather than newness. Moreover, the balance of articles is disproportionately about staffing and compensation, to the detriment of research concerning training and development, performance management, organizational change, and labor relations.

## 3. What we know about staffing

Recruiting and staffing is perhaps the HR topic most widely examined in the context of new ventures, and a summary of the literature in this area is in Table 1. While most small businesses do not have formal HR departments, all firms have recruitment and HR policies, even if they are only implicit (Aldrich & Von Glinow, 1991). Selection is very important for small ventures (Hornsby & Kuratko, 1990) and may even be the key component of overall effective management of a firm's human resources (Heneman & Berkley, 1999). Twenty-five percent of small businesses view a lack of qualified workers as a threat not only to their plans to grow and expand, but more importantly as a threat to their very survival (Mehta, 1996).

Despite its importance, recruiting is often quite problematic for small organizations (Gupta & Tannenbaum, 1989) due to limited financial and material resources (Hannan & Freeman, 1984), lack of legitimacy as an employer-of-choice (Williamson, 2000), and the high number of jobs where employees typically perform multiple roles with unclear boundaries and job responsibilities (May, 1997). Further, although small firms may need to acquire additional employees to fuel their growth, often

Table 1
Entrepreneurship literature on staffing

| Cite | Contribution | Article (theory/empirical) | Size of firm (small/medium) | Life stage (emerging/established) |
|---|---|---|---|---|
| Aldrich and Von Glinow (1992) | Examines the effect prior founder experience can have on HR policies in start-ups. Finds that significant deviations from normal HR policies may violate employee notions of fairness, and that such actions may be undertaken by the founder based on their previous business experience, without recognition of their effect in the new organization. | Empirical | Small | Emerging |
| Baker and Aldrich (1994) | Examines the hiring practices of entrepreneurs in the early stages of firm development. Finds that entrepreneurs tend to hire at the top and bottom of the organization, without focusing much attention on the middle of the organization, and that hiring practices seem to be erratic and loosely planned. | Empirical | Small | Emerging |
| Barber et al. (1999) | Compares the recruitment practices of large and small firms, noting the practices that differ greatly between the two. Notes that employees have definite size preferences in the firms they apply to and that this forms part of the employee's selection criteria. Advocates treating large and small firm labor markets as nearly distinct entities. | Empirical | Small/medium | Established |
| Cardon and Tolchinsky (in press) | Examines the roles different staffing methods can play in small and emerging firms. Offers the view that the mix of direct hire, contingent labor, and PEO-based hires should vary in the firm based on the desired speed, flexibility, mental model, HR commitment, and control over firm dynamics. | Theoretical | Small/medium | Established |
| Cardon (2003) | Examines the role of contingent labor in emerging firms. Suggests that given their reduced size, payroll capabilities, HR staffing, and legitimacy concerns, emerging firms may be able to use contingent labor to supplement their workforce and provide labor, talent, and outside knowledge unavailable to them via traditional staffing methods. Suggests that contingent labor can form a source of competitive advantage for these firms as they emerge, expand, and diversify. | Theoretical | Small/medium | Emerging |

Table 1 (*continued*)

| Cite | Contribution | Article (theory/ empirical) | Size of firm (small/medium) | Life stage (emerging/ established) |
|---|---|---|---|---|
| Deshpande and Golhar (1994) | Examines the differences between desired personnel characteristics, recruitment techniques, selection instruments, and HR practices among small and large firms. Finds that personnel characteristics are more important at small firms and that recruitment/selection differs among them, but that firms seem to share many of the same HR practices and problems. | Empirical | Small/medium | Established |
| Greer et al. (1999) | Examines the role of outsourced HR operations, with an empirical rationale for why firms choose to outsource HR functions. Outsourcing was found to be both an operational and strategic choice, and relationships with outsource partners were, in many cases, found to strengthen the HR value chain. | Empirical | Small/ medium/large | Emerging/ established |
| Heneman and Berkley (1999) | Discusses applicant attraction practices and their links to various outcomes for small businesses. Notes that different attraction practices show benefits in different areas, and that organizations must tailor their policies towards the desired outcomes, be that employee acquisition or retention. | Empirical | Small | Established |
| Heneman et al. (2000) | Qualitative survey of the HR issues confronting SMEs and the current topics in HR related to SMEs—attempts to highlight the gaps in the literature. Highlights the need for more research into organizational fit and the development of multitasking individuals as the biggest gaps. | Empirical | Small/medium | Established |
| Hornsby and Kuratko (1990) | Identifies expected trends in HR practices for small firms. Finds that many more small firms engage in “sophisticated” HR practices than the literature would indicate and that small firms tended to share the same HR concerns as large firms, indicating that policies might not differ that much between them. | Empirical | Small | Established |
| Klaas et al. (2000) | Highlights the advantages of using PEOs in small firms, who cannot or will not employ HR professionals. | Empirical | Small/medium | Established |

(*continued on next page*)

Table 1 (*continued*)

| Cite | Contribution | Article (theory/ empirical) | Size of firm (small/medium) | Life stage (emerging/ established) |
|---|---|---|---|---|
| McEvoy (1984) | Examines the effectiveness of personnel management in small firms versus the expectations of such programs in larger firms. Finds that small firms seem to be overconfident about the effectiveness of their personnel programs and suggests that much of this may relate to employing few dedicated or trained HR personnel. | Empirical | Small | Established |
| McLarty (1999) | Examines the level of managerial development effort put forward by SMEs, specifically with regard to efforts to attract graduate talent and the use of technology to do so. Finds that very few SMEs have made the effort to attract graduate talent and that telematics may help this effort. | Empirical | Small/ medium | Established |
| Williamson et al. (2002) | Examines the methods small businesses use to overcome recruitment hurdles. Suggests that organizational adoption of recruitment policies only because they have been successful for other firms may be in error. Firms should consider the potential employee's knowledge of the firm and their desire for legitimacy when adopting recruitment techniques. | Theoretical | Small | Emerging/ established |
| Williamson (2000) | Develops a strategic model of recruitment for small business, which focuses on the need to gain legitimacy and the need to develop individual firm character. Advocates that firms may need to duplicate the HR policies and processes of those firms they see as legitimate, in order to gain legitimacy themselves. | Theoretical | Small | Emerging/ established |

recruiting strategies are sporadic or ad hoc (Heneman & Berkley, 1999). This may not been seen as proper and appropriate by job applicants (Williamson, 2000), which undermines the firm's legitimacy and decreases their potential to hire qualified candidates.

Very small firms, those with fewer than 20 employees, are most likely to use ad hoc or "muddle through" practices (Windolf, 1986) and may also have little recent experience in filling job vacancies (Heneman & Berkley, 1999). Since many specialized HR activities such as recruiting are infrequently performed in these ventures (Cook, 1999), the costs of hiring highly trained HR professionals are likely to be prohibitive (Arthur, 1995). As a result, HR activities often become the responsibility of general managers (Longenecker, Moore, and Petty, 1994), rather than HR professionals. Given the instability of HR demands, small firm managers are least likely to develop the skills and tacit knowledge required to perform needed HR activities well (Barney, 1991), and when performed, these HR tasks may interfere with managerial responsibilities that are directly related to revenue production (Cook, 1999). This is especially problematic for small venture managers who are already resource and time constrained (Klaas, McClendon, & Gainey, 2000).

Several comparative studies of small and large firms (e.g., Deshpande & Golhar, 1994; Heneman & Berkley, 1999; Hornsby & Kuratko, 1990; McEvoy, 1984) indicate that recruiting in small ventures primarily involves use of sources that are convenient, inexpensive, and directly controllable by the company, such as direct applicants, personal and employee referrals, and newspaper ads (Heneman & Berkley, 1999). Small venture managers appear to be quite willing to provide realistic job previews (Wanous, 1973), communicating both positive and negative attributes of the job to applicants. Selection is based mostly on interviews (Deshpande & Golhar, 1994), training experience, and education requirements for jobs, plus reference and background checks, and selection is done in consultation with hiring supervisors and work unit employees of the job being filled (Heneman & Berkley, 1999).

Small firms also extensively consider noninstrumental factors in their hiring, including the norms, values, and beliefs of the organization and the applicants (Williamson, 2000; Williamson et al., 2002), and person–organization fit (Chatman, 1991) is often an important factor in the selection decision. Often managers focus on the match of applicant competencies to general organization needs rather than to specific job requirements (Heneman, Tansky, & Camp, 2000). This involves "aligning the applicant competencies with organizational values and culture rather than aligning basic knowledge, skills, and abilities with minimum qualifications for the job" (Heneman & Berkley, 1999, p. 17).

The fundamental recruiting challenge for small firms is effectively attracting and selecting candidates in the absence of trained HR personnel or significant managerial expertise in this area (Arthur, 1995). There are several suggestions in the literature for how small firms may address this challenge, in addition to the "muddle through" approach. Williamson and colleagues (2002, 2000) suggest that small firms need to gain legitimacy in their industries by adopting recruiting practices that reflect industry norms. For example, imitating standard forms of job advertisement and providing recruitment brochures may increase the likelihood that potential applicants will understand the advertisements and convey legitimacy to the firm (Aldrich & Fiol, 1994; Williamson et al., 2002). Using common recruitment practices such as newspapers ads, college recruiting offices, and well-defined job positions may also aid in successful recruiting efforts (Baker & Aldrich, 1994) and may help firms fill their vacancies faster and retain employees longer (Heneman & Berkley, 1999). Attending job fairs may also provide small firms with access to a larger pool of applicants and help them stay abreast of current industry trends (Buss, 1996), further enabling them to establish and implement legitimate and effective recruiting practices (Williamson, 2000).

In contrast, for some small businesses, uniqueness rather than imitation provides the organization with competitive advantages in acquiring labor resources (Barney, 1991), where firms purposely adopt practices that are a radical departure from industry norms (such as having vague or nonexistent job descriptions, or not using stock-based compensation) (Alexander, 1999). Many companies are founded with the idea that they will be antibureaucratic, for example, and are able to successfully recruit employees based on their informal, empowered approach to work, and small size of workforce (Cardon & Tolchinsky, in press). This begs the empirical question of whether and under what conditions a strategy of imitation and legitimacy is more (or less) effective than a strategy of uniqueness in attracting job candidates.

One relatively new avenue of thinking concerning recruiting in small organizations concerns outsourcing recruiting through the use of professional employer organizations (Klaas et al., 2000) or contingent labor brokers (Cardon, 2003). Professional employer organizations can provide firms with highly trained HR experts and HR services, such as recruiting, for significantly lower time and financial investments than firms can provide alone. The firm outsources its HR function in varying degrees to the PEO, and the PEO handles their workforce by providing compensation programs, regulatory compliance, and other HR-related services (Klaas et al., 2000). By focusing on HR management for a number of firms, PEOs can get better rates on benefits and provide access to a large team of HR experts for small firm managers (Greer, Youngblood, & Gray, 1999). Small firms are increasingly relying on PEOs to provide HR services (Cook, 1999), and these services may include benefits, payroll, worker's compensation, safety and health, incentive pay, staffing, performance evaluations, discipline, employment policies, training, employee relations, job design, and even financial planning (Klaas et al., 2000).

Firms can also recruit necessary skills through engagement of contingent labor, such as temporary workers, independent contractors, interns, and consultants (Cardon, 2003). Using contingent labor throughout organizational growth "may enable the firm to both lower its cost structure and to respond more quickly to changing market conditions" (Matusik & Hill, 1998, p. 682). Because contingent workers are engaged only when their specific skill set, knowledge, or productivity is needed, they represent a variable rather than fixed cost for the firm and can be released more easily once their contribution is no longer needed (Foote & Folta, 2002). Cardon (2003) suggests differing uses of contingent workers throughout a firm's life cycle.

While multiple models of recruiting and staffing for small ventures exist, work on nontraditional staffing models has only been developed recently, and examination of the trade-offs between using nontraditional models such as PEOs and contingent labor has not yet been considered (Cardon & Tolchinsky, in press). The critical empirical question remaining concerns the performance, cost, and employee relations trade-offs between multiple staffing approaches. What has been established is that small businesses need to view and treat their attraction and selection practices as strategic choices to be made in order to achieve desired outcomes (Heneman & Berkley, 1999). This takes a combination of strategic thinking and "gut feel" combined with knowledge of research results such as those obtained by Deshpande and Golhar (1994), Hornsby and Kuratko (1990), McEvoy (1984), and Heneman and Berkley (1999).

## 4. What we know about compensation

"Developing a pay plan is as important in a small firm as a large one" (Dessler, 2003).

Compensation is perhaps the second most attended to topic at the nexus of human resource management and entrepreneurship, and a summary of this literature is in Table 2. Heneman et al. (2000) found that publications within HR in general and HR within small firms focus most heavily on staffing, compensation, and reward issues, which are consistent with the three primary HR concerns of small firm CEOs and founders. Compensation is a particularly important topic because often compensation significantly affects recruiting and retention efforts of small firms; if they cannot pay applicants enough, then they cannot recruit or retain critical skills or knowledge they need to operate effectively. Further, the compensation and reward system can be an important communication device to nurture and emphasize desired entrepreneurial activities and to signal legitimacy to external stakeholders (Graham, Murray, & Amuso, 2002; Suchman, 1995).

As with recruiting, there is some evidence that compensation is different in small firms, not only because of scarce resources, but also because of the great ambiguity concerning the firms' future. Entrepreneurial firms have lower survival rates and shorter life cycles (Katz et al., 2000), which may translate into different

Table 2
Entrepreneurship literature on compensation

| Cite | Contribution | Article (theory/empirical) | Size of firm (small/medium) | Life stage (emerging/ established) |
|---|---|---|---|---|
| Balkin and Logan (1988) | Contrasts effective pay policies in entrepreneurial firms with those of large corporations. Notes that pay policies used in large corporations may not be effective for promoting entrepreneurial development in the firm. | Theoretical | Small/ medium | Emerging/ established |
| Balkin (1988) | Advocates the use of variable compensation and pay incentives to promote growth in firms that emphasize a growth strategy. | Theoretical | Small/ medium | Emerging/ established in emerging industries |
| Balkin (2003) | Proposes a model of compensation and rewards for entrepreneurial firms, emphasizing growth. Asks how compensation should change for the firm's early and key employees as the firm's life cycle evolves. | Theoretical | Small | Emerging |
| Barringer et al. (1988) | Examines how rapidly growing firms manage shortfalls in management capacity/capability. Finds that many firms in rapid-growth environments mitigate these concerns by forming alliance relationships, creating cash forms of compensation, and empowering employees. | Empirical | Small/ medium | Emerging/ established |
| Chandler et al. (2000) | Identifies the characteristics of innovation-supportive cultures according to employees. Emphasizes the use of reward systems. | Empirical | Small/ medium | Established |
| Graham et al. (2002) | Presents a social psychology perspective on employee rewards and staffing. Suggests that employees' rewards should be tailored to meet the objectives and competitive advantage of the firm in question—that entrepreneurial firms should target their competitive advantage and design compensation plans that contribute to it. | Theoretical | Small/ medium | Emerging/ established |
| Welbourne and Andrews (1996) | Examines the role HRM policies can have in predicting initial public offering amounts and the likelihood of long-term sustainability. Finds that two HRM attributes —reward systems and human resource value—had significant predictive effects on both IPO pricing and sustainability. | Empirical | Small/ medium | Established |

rewards strategies for these ventures (Balkin, 1988; Heneman et al., 2000). Key behaviors that are being rewarded may differ in entrepreneurial organizations from their larger counterparts. For example, creativity, innovation, willingness to take risks, cooperation, interactive behavior, and tolerance for ambiguity are important behaviors in small and emerging firms (Balkin & Logan, 1988) but may not be as important in larger more established firms. Differences in compensation based on organizational size and age have been observed in both the popular and academic press (Graham et al., 2002).

Compensation involves a series of decisions a firm makes concerning payment of its workers, including pay levels, pay mixes, pay structure, and pay raises. Pay level is how salaries compare to the external market; pay mix is the proportion of salary, benefits, and incentives in the total pay package; pay structure refers to the hierarchy of pay rates among jobs in the organization; and pay raises concern the administration of pay increases with the organization (Balkin & Logan, 1988). The majority of work on small firm compensation has focused on pay mix, and in particular the emphasis has been on variable pay incentives.

Because of the conditions that entrepreneurial firms face, the pay mix often puts more emphasis on variable at-risk pay (Balkin & Gomez-Mejia, 1984; Barringer, Jones, & Lewis, 1988; Milkovich, Gerhart, & Hannon, 1991). "Because entrepreneurial firms are likely to have less programmable and more fluid jobs, fewer resources with which to monitor worker performance, and employees with relatively short organizational tenures, we expect the greater use of performance-related incentives and stock-related rewards in entrepreneurial firms as compared to nonentrepreneurial firms" (Graham et al., 2002, pp. 120–121). Small firms usually put a significant portion of potential earnings (10–50% more than large U.S. firms) at risk in the form of pay incentives (Balkin & Logan, 1988). By doing so, ventures are most able to reinvest significant portions of their labor expenses in the business when it is most vulnerable and in need of cash and are also able to give greater pay to workers when significant goals are met, sales are good, or productivity is high. From an organizational perspective, variable pay systems allow the firm greater flexibility by sharing risk and deemphasizing base pay, which should make it easier for firms to respond to volatile environments (Graham et al., 2002).

Short-term pay incentives in small firms may include profit sharing and stock sharing, where a significant portion of employee pay is only given when organizational-level profits meet specific preset targets. In entrepreneurial firms, these sharing plans may be quite motivational, even more so than in large organizations, since in small ventures workers have greater ability to directly control organization-level outcomes (Heneman & Tansky, 2002). This also supports teamwork within the organization because profit sharing is an egalitarian reward offered to all employees of the venture (Balkin & Logan, 1988), encouraging workers to cooperate to achieve collective goals.

Long-term pay incentives may include some form of equity ownership, such as stock, stock options, or incentives based on venture stock performance since stock options are an excellent retention tool (at least in large organizations), and because employees who have an equity stake in the firm may better identify with firm management, thinking more like owners than employees (Graham et al., 2002). This model is widely used in high-technology ventures, where technology mangers, scientists, engineers, and other R&D employees are likely to have a large portion of their pay contingent on the achievement of technological milestones (Balkin & Gomez-Mejia, 1987; Gomez-Mejia & Balkin, 1989), which enhance their motivation to achieve individual and organizational performance goals. Risk sharing in this way is consistent with an agency theory perspective, arguing that workers who have a significant financial interest in the venture will be less likely to behave opportunistically and more likely to act in the best interests of the overall venture (Graham et al., 2002).

Pay mix has also been shown to differ systematically over a firm's life cycle, such as when an organization moves from a growth stage to a mature stage of its products (Balkin & Gomez-Mejia, 1984). Employees may receive a different form and amount of compensation as the organizational strategy evolves, and as the risk and uncertainty concerning the firm, and its ability to pay its workers changes (Nesheim, 2000). For example, as a firm matures and the novelty and excitement of assuming risk wear off for employees, cash compensation must increase to competitive market levels in order for the firm to retain employees (Graham et al., 2002).

Pay structure may also differ between small and large firms, as small firms tend to have flat organizational structures with few levels of management and tend to treat employees in an egalitarian way with regard to compensation and rewards (Graham et al., 2002). Balkin and Logan (1988) argue that in small firms, traditional hierarchical distinctions are kept to a minimum so that rewards are not indicative of status differences among employees. Pay raises are also different in these organizations since automatic annual salary increases, which are common in large organizations, are not affordable to small ones (Balkin & Logan, 1988). Salary is a fixed cost, and without certainty of sales or profits automatically increasing at a rate greater than salaries, small firms cannot provide fixed annual raises. Instead, they argue that perhaps lump sum salary increases, more like bonuses, should given to employees to reward individual performance that significantly helps the organization's success.

Benefits in small firms also may differ from those in larger firms, where benefits in the former are likely to be more modest. While resource and cash constraints are clearly of paramount importance, logic suggests that benefits that offer long-term security to employees, like life insurance or company-funded pension plans, may never be realized since small and new ventures have very high failure rates. One of the most costly benefits, retirement, is often funded by a profit-sharing plan in fast-growth organizations (Gomez-Mejia & Balkin, 1989), where funding of the plan is timed with organizational success so that scarce cash is used to fund employees' retirements only when profit targets are achieved. Employee stock ownership plans (ESOPs) are also a benefit than can support the goals of the small firm, where instead of employees being given stock (as discussed above under long-term incentives), they are allowed to purchase it at a significant discount. This still provides the benefits of employee ownership, such as identification with management and focus on organizational outcomes, but here the stock is paid for by employees rather than given to them outright, which saves the organization money.

Balkin and Logan (1988) argue that education benefits are also highly appropriate for small firms. Employees in small firms often encounter gaps in their education due to their changing roles within the organization and changing organizational and market conditions, so education funding in the form of travel, tuition, and supplies is important. As will be discussed in the next section, small firms usually cannot afford in-house training or high-priced consultants, so it must send employees to universities or professional seminars and workshops to gain new knowledge and skills (May, 1997). This is especially crucial in knowledge-intensive industries.

There is some question as to whether small firm managers take a systematic and rational approach to compensation, as traditional HR research would suggest is best. Small business compensation practices are often uncoordinated and ad hoc, which may complicate their consistent implementation and impact on worker behavior. More recently, scholars have suggested that compensation practices should be viewed from a total rewards perspective (Parus, 1999), where compensation includes psychological rewards, learning opportunities, and recognition in addition to monetary rewards in the form of base pay and incentives (Graham et al., 2002; Heneman et al., 2000). The rewards of employment with an entrepreneurial firm are multidimensional, including the risk and potential payoff from gambling on an innovation, invention, or business prospect and the satisfaction of ownership (even if only partial), experienced responsibility of having a tangible stake in the business, or the opportunity to work in an environment unencumbered by traditional constraints of bureaucracy (Graham et al., 2002). Case study evidence suggests that smaller organizations are more likely to view compensation from a total rewards perspective than are larger companies (e.g., Nelson, 1994), but more research is needed on this (Heneman et al., 2000).

Some of the differences in long-term compensation schemes that exist between emerging and established firms may have to do with their tendency to be privately held in their early stages. Prior to large-scale or public investment, the firm may have a limited amount of equity with which to offer employees participation in ESOPs, stock sharing, or long-term ownership of other forms. In addition, firm owners may be reluctant to break apart the concentrated ownership that typically exists in the early stages of a firm's life. As a result, the differences in compensation between emerging and established firms may hinge, at least concerning equity compensation, on whether they are in a pre- or post-IPO phase. Privately held firms, especially small ones, may have less latitude in the equity-based long-term compensation they are able to provide. This subject has not yet been addressed in the literature.

Further, although academics are beginning to focus more intently on issues of compensation in small firms, perhaps extension of this focus to more integrative and balanced compensation programs would be useful. For example, there is some evidence that firms giving ownership as part of their compensation system can potentially have lower innovation (Nesheim, 2000), and that while risk itself may be an attractive feature to small firm employees, rationality will motivate withdrawal from the venture if continued poor performance decreases the likelihood of acceptable financial returns to employees (Graham et al., 2002). An integrative study that considers not only financial components such as pay level, structure, mix, and raises, but also recognition, innovative benefits, relaxed environments, and experienced responsibility, for example, would shed light on the relative importance of these extrinsic and intrinsic motivators and rewards for employees of small firms. Even better would be such a study that also incorporates factors such as life cycle stage, industry, and legitimate compensation norms to provide a more holistic and comprehensive view of this phenomenon.

## 5. What we know about training

Since employee roles and responsibilities shift rapidly in small and new firms, it follows that some sort of training and development concerning new roles is vital to the success of the employees and the business. However, there is very little research on training nonfounders within entrepreneurial organizations. A summary of the available literature is in Table 3. Perhaps this paucity is due to the notion that in human resources training is viewed as a distinct formalized event, you "go to training," whereas in entrepreneurship training may be more associated with ongoing activities related to individual development (Jones, Morris, & Rockmore, 1995). Perhaps additional insights on employee skill development and learning could be gained if a broader perspective on training is taken, such as the original conception of McGehee (1949) that training concerns individual processes involving gaining proficiency in a specific skill or competence (Bishop, 2003). As Bishop (2003) suggests, many theoretical frameworks have been developed to better understand skill acquisition processes, retention, and transfer of knowledge (Tannenbaum & Yukl, 1992), and this work may be usefully applied in an entrepreneurial context.

Table 3
Entrepreneurship literature on training and development

| Cite | Contribution | Article (theory/ empirical) | Size of firm (small/ medium) | Life stage (emerging/ established) |
|---|---|---|---|---|
| Banks et al. (1987) | Examines who makes training and development decisions within small firms, focusing on the CEO/owner as the key decision maker. | Empirical | Small/large | Established |
| Bishop (2003) | Offers theoretical perspectives on the intersections of training and entrepreneurship. References two previous studies to justify that entrepreneurship and training studies are converging. | Theoretical | Small | Emerging |
| Chandler and McEvoy (2000) | Analyzes the role of a total quality management (TQM) strategy in SMEs. Indicates that TQM programs are most effective when paired with strong training and group-based compensation. Emphasizes the benefit of a "fit" model of HR practices in encouraging programs such as TQM. | Empirical | Small/medium | Established |
| Johnson and Bishop (2003) | Highlights the demands on founders in fast-growth firms. Identifies potential role and behavioral demands on founders and suggests avenues for potential research into the effect role and behavior requirements can have on firm growth stages. | Theoretical | Small/medium | Emerging/ established |
| Rollag and Cardon (2003) | Examines the role socialization processes play in large and small organizations and whether a difference exists between the effectiveness of formal and informal socialization efforts. Finds that informal efforts are more effective than formal ones, and that in startups, much of the socialization process is via informal activities. | Empirical | Small | Established |
| Rollag (2002) | Examines the effect first-week activities had on the assimilation of new employees in high-technology startups. Provides direction on techniques that did and did not aid assimilation, in lieu of expensive training for fast-growth firms. | Empirical | Small | Established |

In terms of formal training, research in large firms suggests that training consistently has a positive impact on individual worker productivity (Guzzo, Jette, & Katzell, 1985). In an examination of differences in formal training between large and small organizations, Banks, Bures, and Champion (1987) discovered that for small organizations, the cost of training programs and time spent away from productive work are important considerations for determining what training opportunities to provide to workers, as resources of both money and worker time are constrained (Banks et al., 1987). Sources of formal training are also more restricted for small firms than for large ones, and small organizations typically rely upon trade associations, short college seminars, and in-house training for employee development. Interestingly, at the time of this study, 87% of small businesses had some form of educational assistance program (Banks et al., 1987), indicating that despite limited resources, development and advancement of employee skills are quite important to small firm managers.

In a study of small manufacturing firms, Chandler and McEvoy (2000) discovered that in order for specific strategic initiatives, such as implementation of total quality management (TQM) practices, to positively impact firm earnings, extensive training is needed, as well as a group-based pay system. This suggests that formal training cannot be considered in isolation in SMEs, but rather must be examined in terms of the interaction of training and other human resource and strategic initiatives occurring in organizations.

Furthermore, in small firms, unstructured training, informal on the job instruction, and organizational socialization are also quite important and are often seen as substitutes for formal training processes (Chao, 1997). In fact, many small firms pride themselves on providing workers with more hands-on highly interactive learning opportunities (Rollag, 2002) and avoiding formalized systems and practices more typical of large bureaucratic organizations. It is widely accepted that not all employee learning occurs during formal training (Ford, 1997), and in fact the Bureau of Labor Statistics reports that more than 70% of workplace learning is not formally facilitated and not dependent upon organizational size (Bishop, 2003). This suggests that research on training in small firms could usefully address both formal and informal learning processes, including within organization knowledge transfer, learning-by-doing, and retention of knowledge within the organization throughout turnover events. Despite a general lack of formally codifying and documenting knowledge advancements in smaller organizations, training and learning is occurring, and more careful study of that learning is warranted.

One specific form of training that has been examined recently is the process of socialization of organizational newcomers (Rollag, 2002; Rollag & Cardon, 2003). Socialization is a long-term process where individuals learn their roles within an organization, and adjust to job demands, organizational culture, and other incumbents (Chao, 1997; Van Maanen & Schein, 1979). Socialization includes both formal training, such as through formal orientation programs, and informal training that occurs once newcomers begin performing their jobs. Socialization processes influence learning and career development regardless of organizational size (Chao, 1997). Recent work suggests, however, that socialization processes in small organizations differ from those in large ones. Rollag and Cardon (2003) suggest that the process of socialization occurs more quickly in smaller organizations, as newcomers are more readily incorporated into meetings and social events such as lunch, are given more meaningful projects to work on, and are not isolated from organizational incumbents or senior managers. Due to this faster and more extensive inclusion of newcomers in small firms, their job satisfaction and productivity are greater than their counterparts in larger organizations. Rollag and Cardon suggest that perhaps larger organizations should adopt more inclusive and informal socialization tactics with their newcomers, instead of or along side the highly formalized and structured training events that isolate newcomers from other organizational members and from the work they will eventually be doing.

One additional area of research on training bears mentioning, and that is work focusing on multitasking and role transitions within entrepreneurship. As mentioned above, in small and emerging firms, workers often are not relegated to specific job tasks or roles, but rather must shift between roles and assignments as environmental and organizational conditions warrant (May, 1997), making their management of these role transitions and extensive multitasking important. Recent work has been done on role transitions of organizational founders (Johnson & Bishop, 2003), and this work may be usefully applied to multitasking and role transitions of nonfounder employees to understand their learning and adaptation processes throughout these transitions. It would also be insightful to examine what actions, if any, managers take to help employees make these transitions more effectively, thereby improving both morale and performance. Work by Welbourne, Johnson, and Erez (1998) suggests that differences in work role perceptions between employees and supervisors exist, and that lack of consistent role perceptions between supervisors and subordinates in small firms could signal a need for more formal training processes concerning such roles (Bishop, 2003).

## 6. What we know about performance management

> “Performance appraisal and compensation are the pivotal mechanisms for fostering entrepreneurship. HR practices in these two areas, more than any other, communicate performance expectations and reinforce desired behaviors” (Jones et al., 1995, p. 88).

Interestingly, virtually no work has been done concerning performance management in entrepreneurial organizations. What work has been done is summarized in Table 4. While performance management may include elements of compensation through incentives and rewards, as well as training and development, we focused only on performance evaluation processes, disciplinary procedures, or dismissals of workers. We found no direct study of performance management concerns in small firms (for a recent exception, see Cardy, 2003) and only a few papers that referred directly or indirectly to performance management in this context. Perhaps this is due to the rarity of formalized procedures in small firms for managing performance reviews, disciplinary processes, or dismissals of workers. The relative lack of concern of venture founders on downstream (post-start-up) management issues, particularly those with negative implications such as workers not performing well or the business

Table 4
Entrepreneurship literature on performance management

| Cite | Contribution | Article (theory/empirical) | Size of firm (small/medium) | Life stage (emerging/established) |
|---|---|---|---|---|
| Cardy (2003) | Examines the theoretical requirements for performance management in small, high-growth firms. Suggests that effective performance management requires a system that fits with the environment and the appropriate management skills to interpret and provide direction. | Theoretical | Small | Emerging |
| Chu and Sui (2001) | Proposes a multistep model for “rightsizing” in SMEs. | Empirical | Small/medium | Established |

needing to lay off workers, may also contribute to this void in our scholarship. For example, Verser (1987) studied 25 small business owners, who said they often deal with subordinates arbitrarily rather than consistently and that they did not perceive this arbitrary behavior to contribute to employee morale or productivity problems. It could also be a philosophical approach issue, where managers of young or small firms prefer informal ongoing communication and feedback to highly formalized performance appraisal procedures.

Perhaps also, for organizations that pride themselves on innovation and flexibility, turnover and the resultant steady flow of employees into and out of the firm may be very desirable (Heneman & Tansky, 2002). Indeed, March (1991) tells us that new organizational members are essential for learning and innovation, or changes in the organizational code, to occur. However, given that much of the tacit knowledge in entrepreneurial firms resides within employees (Heneman & Tansky, 2002), significant turnover without ways to institutionalize or capture that knowledge before it leaves the organization would be highly problematic. Further, findings within a high-technology context (Baron & Hannan, 2002) indicate that firms that experience significant turnover see significantly slower revenue growth for the ensuing 2 years, indicating that high levels of turnover can be detrimental to firm success, particularly in knowledge-intensive industries.

## 7. What we know about organizational change

In addition to the vagueness or neglect in the literature concerning how small firm managers handle bad performance or problem employees, issues concerning significant organizational change in small firms have also been ignored. The available literature is summarized in Table 5. One study has been done on how SMEs in Hong Kong change their HR practices in response to bad economic environments (Chu & Sui, 2001). Chu and Sui (2001, p. 846) argue that "with a lean structure, limited resources, and focused core competencies, SMEs face greater difficulties in coping with downturns" than do their larger organizational counterparts. They outline a process through which small firms can cope with such downturns, essentially suggesting that for smaller firms it is more difficult for managers to make layoff decisions, given their greater propensity to be close to employees due to the smaller organizational size.

Another significant body of work concerning organizational change in small firms has evolved from the Stanford Project on Emerging Companies (SPEC), which has tracked the key organizational and HR challenges of a large sample of high-technology start-ups in Silicon Valley (Baron & Hannan, 2002). Scholars working on this project have documented several HR "blueprints" or sets of practices that appear consistently in this sample of firms. An important question they have recently addressed is the implications of changes in these blueprints for employees and organizations. Their findings are that "changes in organizational blueprints are in general very destabilizing to young technology start-ups, adversely affecting employee turnover, bottom-line financial performance, and even mere survival" (Baron & Hannan, 2002, p. 19). Specifically, Baron and Hannan (2002) report that firms that significantly change their HR blueprints experience markedly higher employee turnover, are 2.3 times more likely to fail than firms who retain a stable blueprint, have a slightly higher hazard of IPO, and experience a reduction in market capitalization of the firm by 3% per month following an IPO. This suggests that technology companies pay a significant and enduring price for altering their HR practices at an earlier point in time, especially for firms founded on the idea of commitment to

Table 5
Entrepreneurship literature on organizational change

| Cite | Contribution | Article (theory/ empirical) | Size of firm (small/medium) | Life stage (emerging/ established) |
|---|---|---|---|---|
| Aldrich (1999) | Introduces an evolutionary approach to organizational development and founding, from organizational founding roles to organizational transformation, to the formation and replication of groups within the organization. Offers the view that entrepreneurs within and without the organization play a role in continuously reshaping the organization into new emergent forms. | Theoretical | Small/medium | Emerging/ established |
| Baron and Hannan (2002) | Via interviews with CEOs, establishes five HR blueprints high-technology firms are likely to adopt in their formation. HR blueprints are likely to be determined by the founders and tend to commit the organization to a particular direction in terms of leadership and personnel management that is difficult to change. Assesses the strengths and weaknesses of each blueprint style. | Empirical | Small/medium | Emerging/ established |
| DeDee and Vorhies (1998) | Examines the implementation of retrenchment activities in small firms during periods of economic decline. Longitudinal analysis indicates that many retrenchment techniques can aid small firms during times of economic decline. | Empirical | Small | Established |
| Michael and Robbins (1998) | Examines the role retrenchment plays in small businesses during economic downturns. Offers that retrenchment is a common occurrence among small firms and identifies firm characteristics that are likely to be favorable to retrenchment. | Empirical | Small | Established |

employees and where employees have personal relationships with the founders (Baron & Hannan, 2002).

If significant changes in HR practices have such negative impacts on employees and organizations, then understanding the initial choices founders make concerning organizational administration and employee issues is essential. These early imprints have a more powerful bearing on later administration (even 8 years later in SPEC) than does the model of the present-day CEO, providing compelling evidence of the highly constraining impact of early choices on how companies develop over time (Baron & Hannan, 2002). Further, the SPEC research indicates that considerable transformations in HR practices do take place after firm inception, and that there is much left to understand about how small and emerging firm managers decide when to change practices and how to manage these organizational transitions. These changes may antagonize incumbent employees by eroding skills, altering bases of power and status, and calling cherished belief systems into question (Baron & Hannan, 2002), making management of these transitions and specifically managing worker performance during these transitions important. Our theoretical and empirical understanding in this area is severely lacking.

## 8. What we know about labor relations

The impact of unionization on the small or emerging firm has been virtually ignored in the HRM literature (Deshpande & Flanagan, 1995; Flanagan & Deshpande, 1996), with the exception of three important studies, summarized in Table 6. Deshpande and Flanagan (1995) looked at factors influencing union win rates in elections held in small firms; Flanagan and Deshpande (1996) examined perceptions top mangers had concerning changes in HRM practices after union elections in small firms; and Batt and Welbourne (2002) discovered that the presence of unions in small ventures going through the IPO process may have a positive impact on firm performance. The common finding among these studies is that labor unions can have a major impact on HRM practices of firms striving to build a competitive advantage through people (Flanagan & Deshpande, 1996), even for small ventures.

Batt and Welbourne (2002) note that examining labor relations in entrepreneurial companies is an interesting juxtaposition because unions are usually known for their inflexibility and as barriers to change, while entrepreneurial ventures are known for innovation, flexibility, and rapidly changing to market demands. They suggest that in this context, firms and unions both have more opportunities to

Table 6
Entrepreneurship literature on labor relations

| Cite | Contribution | Article (theory/empirical) | Size of firm (small/medium) | Life stage (emerging/established) |
|---|---|---|---|---|
| Batt and Welbourne (2002) | Examines the impact unionization has on the financial performance of entrepreneurial firms. Finds that there may not be a direct tie between unionization and declines in financial performance. | Empirical | Small/medium | Established |
| Deshpande and Flanagan (1995) | Compares the frequency and success rate of union elections in small and large firms. Smaller firms were found to have significantly higher rates of successful union votes and a higher frequency of union votes occurring. | Empirical | Small/large | Established |
| Flanagan and Deshpande (1996) | Examines the impact of union elections in small firms, specifically as to how the success or failure of a union vote influenced the firm's ability to institute HR practices that were considered innovative or to their competitive advantage. Small firms where union votes failed were more able to institute these policies than firms that became unionized. | Empirical | Small/medium | Established |

adopt new forms of work organization and better labor–management relationships (Batt & Welbourne, 2002). Perhaps this cooperative climate has led to the paucity of research on labor relations in small firms since union membership in small firms is likely to be small. Findings by Batt and Welbourne (2002) support this notion in that they find that union presence is stronger in larger organizations and weak in smaller ones.

Examining small firms where attempts to organize labor have not been successful is also quite revealing. In a study comparing how staffing, training, compensation, and other workplace issues had changed following successful and unsuccessful union elections in small firms, Flanagan and Deshpande (1996) discovered several important features of these relationships. First, simply the presence of a union election in a small firm significantly impacted HR practices in those firms, such as greater budget allocation to training and development and greater training activity for workers. This indicates that perhaps union elections alone operate as a wake-up call for small firm managers, forcing them to address issues of employee dissatisfaction or desire for training and advancement (Flanagan & Deshpande, 1996).

Secondly, the results of a union election have an important effect on several HRM practices and employee reactions. More specifically, where union elections are successful, decreases in merit-based compensation, promotions, and layoffs occur, as well as decreases in wages compared to industry standards. Union success also results in increases in employee turnover and decreases in commitment to the firm and worker flexibility. In contrast, when a union election is unsuccessful, the result is increases in merit-based promotions, compensation, and layoffs and increases in employee wages. Union losses also lead to significant increases in employee commitment, team work, worker flexibility, labor management communication, and employee participation initiatives (Flanagan & Deshpande, 1996). This seemingly counter-intuitive study indicates that various innovative HRM practices significantly increase only in those companies where unions lost elections, despite the intention of unions to protect and help workers. Interestingly, this study did not compare small firms with failed and successful union elections to firms that had no union activity at all. It could be that the simple threat of unionization prompted small firm managers to focus attention on worker-friendly HRM practices, and that firms without that threat of unionization will not implement these innovative approaches.

Flanagan and Deshpande (1996) argue that their findings should be a wake-up call to managers to attend to worker concerns and to adopt more progressive strategies to keep their organizations nonunion. Often entrepreneurs are so focused on getting sales and meeting demand for their products that they are lax with overtime, pay scales, personnel manuals, and may even be amazingly ignorant of basic labor law (Rohling, 2003), which could pose problems for the organization. Some popular HR textbooks, such as Dessler (2003), suggests that managers of small firms should revise or enact written personnel policies and practices so that union organizers have less reason to view the firm as loosely run and vulnerable target; improve security of employee record files, so it's not easy to for union organizers to get access to names and home addresses; and to be sure to stay in touch with employees to make sure the work environment is desirable and their concerns are being heard as well as addressed.

It is important to come back to the findings of Batt and Welbourne (2002) that union presence is not necessarily a bad thing for organizations. In their sample of IPO firms, union membership positively impacted firm performance, even 3 years after the IPO date. Although they did not measure detailed employee implications such as turnover and commitment, their work suggests that perhaps small firm managers need not be focused on avoiding unionization, but rather should ensure that whether workers are unionized or not, the organization's strategies are aligned with appropriate and considerate human resource practices.

## 9. Discussion: What we do not know about managing employees in new ventures

The preceding discussion demonstrates that as scholars, we are beginning to understand how to hire, pay, and perhaps even motivate workers within small firms. However, we do not yet have much theory or data concerning issues of training, performance management, organizational change, or labor relations in small firms. Table 7 provides a summary of what we know and do not know about HR in small firms. Further, underlying these functional areas are three fundamental aspects of human resource management we do not yet understand in the context of small firms: retention and ongoing employee issues, integration and interactions of HR practices, and the evolution of HR practices within evolving organizations.

### *9.1. Retention and ongoing employee issues*

Although issues of not only recruiting, but also retaining, qualified employees "whose knowledge often represents the firm's most valuable asset" (Baron & Hannan, 2002, p. 21) are clearly important, our scholarship does not yet fully address issues of retention. Hardly any studies look at factors influencing employee turnover or retention in small firms, although "few imperatives are more vital to the success of young technology companies than retaining key technical personnel" (Baron & Hannan, 2002, p. 21). Perhaps a more holistic view of compensation, which includes cultural and intrinsic factors that reward employees, would be helpful, but also useful would be more holistic views of the HR experience in small firms as they are understood by employees themselves. What drives people to seek out work in these firms and what keeps them there? A recent paper by Graham et al. (2002) takes a firm step in the right direction by examining the social psychological aspects of stock-related rewards that influence employee retention in small firms.

Heneman and colleagues (2000) suggest that we need more research on how entrepreneurial organizations develop high potential employees who can perform multiple roles during growth periods in the venture, and we believe this might usefully be paired with notions of how employees manage these multiple roles and multitasking responsibilities within their venture employment experience (Bishop, 2003). While work–life balance issues are important for entrepreneurial leaders, they are also quite important for employees of these firms, who often have similar feelings of responsibility and ownership for the ventures as the founder or CEO does. This suggests that additional work on roles such as that done by Welbourne et al. (1998) should be continued and extended to include not only work roles including job, career, innovation, and team, but also more broadly construed life roles, such as parent, spouse, neighbor, and community member. How do aspects of HR practices, such as equity-sharing compensation plans, impact work–life balance and the ability to transition between roles for small firm employees, and does this differ for employees of larger organizations that also utilize such compensation plans?

Finally, while several scholars allude to the importance of relaxed and friendly relationship-based work environments for small firms, our scholarship often does not model these factors or their

Table 7
Summary of literature on human resources in small and emerging enterprises

| Area of HR | What we know about this | What we do not know about this |
|---|---|---|
| General HR | All firms have some form of HR, even if informal | How do SMEs retain and develop high value-added employees? |
| | Most organizations do not have HR professionals in house | How do HR practices integrate and interact within SMEs? |
| | SMEs with more than 100 employees are likely to develop formal HR practices and departments | How do HR practices and systems evolve in emerging ventures? |
| | Early HR choices significantly impact later firm performance | |
| Staffing (recruiting, selecting, hiring) | Staffing is very important, but is problematic | When is a strategy of imitation/legitimacy versus uniqueness effective in attracting job candidates? |
| | Strategies employed are often ad hoc | What are the performance, cost, and employee relations trade-offs between multiple staffing models (direct hires, contingents, PEOs)? |
| | SMEs may lack legitimacy as employers | |
| | Fit is an important selection criteria | |
| | The focus is on general fit, not specific job requirements | |
| Compensation (pay mix, level, structure, raises) | Compensation is different in SMEs that in large firms, especially in that there is more at-risk pay in the mix in SMEs | Does employee ownership decrease risk taking and innovation? |
| | Pay mix changes over the life cycle of the firm | What is the relative importance of extrinsic and intrinsic rewards for SME employees? |
| | SMEs have a greater focus on a total rewards perspective than do large firms | How does this change over the life cycle of the firm? |
| | SME often provides educational benefits and recreational facilities | How long can or do employees delay gratification of their financial or other needs in SMEs? |
| Training and development | Training employees to constantly changing roles and expectations is important in SMEs | How do employees in SMEs multitask multiple roles effectively, especially under conditions of organizational uncertainty? |
| | Cost of training and time away from work for it are essential considerations | What actions do SME managers take to help employees make effective role transitions? |
| | Unstructured training, informal job instruction, and socialization are a big part of the training process in SMEs | What is the optimal balance of formal and informal training within SMEs? |

*(continued on next page)*

Table 7 (*continued*)

| Area of HR | What we know about this | What we do not know about this |
|---|---|---|
| Performance appraisals | Formal appraisals are usually not done in SMEs | How are employee performance deficiencies handled in SMEs? |
| | Employee issues are often handled arbitrarily | What are equity, fairness, or justice perceptions within SMEs, and how does this impact employee or organizational performance? |
| Organizational change | SMEs experience a lot of change | How do HR systems change to grow with the organization? |
| | SMEs have a harder time coping with economic downturns than do large firms | What are the key transition points in emerging and ongoing HR systems? |
| | Changes in organizational practices are very destabilizing to SMEs: + turnover, + likelihood of failure, − financial performance | Do these follow typical life cycle models? |
| Labor relations | The presence of unions in SMEs going through an IPO process may have a positive impact on performance | Does the threat of unionization prompt SME managers to focus on worker-friendly HRM practices? |
| | Presence of union elections leads to greater $$ allocation to training and development | Does the presence of written personnel policies and/or their systemic implementation reduce the threat of unionization? |
| | In SMEs where a union has lost an election, various innovative HRM practices significantly increase | |

influence on individual or organizational performance outcomes. Scholarship that focuses on the areas in which scant attention has yet been paid, such as training, performance management, and labor relations, as well as that which extends these traditional notions of HR into ideas of role transitions, work-life balance, and organizational culture might shed light on what draws and keeps employees engaged and on what drives their performance.

### *9.2. Integration and interaction of HR practices*

We echo Heneman and Tansky (2002), who suggest that simply extending existing HRM models to small firms would not be meaningful, since it has not worked well to extend HR practices from large firms to small ones (Barber et al., 1999). Instead, we should develop theories specific to small firms and their strategic practices (Heneman & Tansky, 2002) and should focus on multiple characteristics of not only the firm, but also of its employees. In small and emerging firms, founders do not talk about HR, but rather as a flow of interrelated activities that they deal with concerning their employees, activities that fluctuate and change over time. In applying the "muddle through" strategy, many CEOs stumble upon synergistic ways to manage their personnel that do not easily fit into our preconceived traditional HR notions. We suggest that a great deal of empirical data should be gathered concerning what these CEOs are actually doing and the impacts of those activities on employee satisfaction, commitment, productivity, and firm performance. It is not necessarily that there is a "right" way of doing HR that small firms should adopt, which seems to be what we have been searching for theoretically, but rather that as scholars we need to go into the field to explore the interaction of HR practices and other factors, and their influence on individual and firm performance. Barney and Wright (1998) suggest that the challenge for HRM is to develop systems of practice that create synergistic effects rather than to develop independent sets of best practices, yet perhaps entrepreneurs have already discovered synergistic HR practices (Heneman et al., 2000), and the challenge as scholars is to access and better understand them.

### *9.3. Evolution of HR practices*

One way in which to do so is to examine HR practices as they evolve in emerging organizations. Aldrich (1999) rightly points out that we know very little about how HR evolves in firms until those firms reach older stages of growth and have become medium or large in size. Our own literature review reveals that very few studies focus on issues concerning emerging firms, and instead focus on HR within small yet established organizations. While recent models have begun to incorporate growth stage or life cycle of the venture (e.g., Balkin, 2003; Cardon, 2003) they have only been applied in the context of single elements of HR practices, such as compensation or recruiting. Perhaps looking at the informal as well as formal mechanisms through which very small and small firms manage their employees would provide a better practical and theoretical view of truly small and emerging firms and how their synergistic HR approaches develop.

While we have just argued that we should look more closely at how HR practices evolve during the growth of the firm, it is important to note that many small firms do not have the capability for growth though they are assumed to be growth oriented. Many scholars have mistakenly assumed that small firms are embryonic large firms (McLarty, 1999), even though we know that many small firms remain small indefinitely. The ultimate result of growth in most models of small and emerging organizations is the formalization of HR so that it mirrors that of larger, older firms. However, development of formalized human resource practices tends to have a negative influence on perceptions of innovation-supportive culture, even after controlling for the size of the organization (Chandler, Keller, & Lyon, 2000). This indicates that perhaps formalization is not a desirable evolution of HR systems in small and emerging firms, and that instead these systems may stifle creativity (Robey, 1991) and reduce opportunities for initiative and individual contribution (Harrison, 1987). This suggests that we must be careful in our conceptualizations and empirical studies to ensure that we capture not only size or age of venture, but also their life cycle stage and propensity or desire for future growth. More careful empirical delineation of size and age within the overall distinction of "entrepreneurial organization" or "SME" would also be useful, for HR practices for firms of 15 people are apt to be quite distinct from those of 100 or 250 or even 500 that marks the top of the SME category for some. Unfortunately, most of the research done in this area has so far included all firms with anywhere between 1 and 250 employees in the category of a small and medium enterprise.

## 10. Conclusion

"Once a new venture is founded, becomes an organization, and hires its first employees, human resource issues and forces that exist in—and influence the success of—all organizations come into play. Indeed, growing evidence suggests that an inability on the part of some founders of new ventures to successfully manage HRM issues is an important factor in their ultimate failure'' (Baron, 2003, p. 253).

Effective management of human resources is one of the most crucial problems faced by small firms (Deshpande & Golhar, 1994; Hornsby & Kuratko, 1990). ''A new organization's division of labor emerges through a series of local adaptations only partially controlled by founders' plans'' (Katz et al., 2000, p. 10). Yet often founders spend more time worrying about the scalability of their phone system or IT platform rather than the scalability of their culture and practice of managing workers (Baron & Hannan, 2002). This occurs even when ''that same founder would declare with great passion and sincerity that ''people are the ultimate source of competitive advantage in my business'' (Baron & Hannan, 2002, p. 29).

Our literature review suggests that HR decisions made early in a venture's creation process profoundly impact downstream success of businesses, these choices evolve and change over time and organizational development, and that practitioners and scholars, in fields of both HR and entrepreneurship, do not spend enough time focused on the downstream impacts of these choices. ''Any plan for launching a new enterprise should include a road map for evolving the organizational structure and the HR system, which parallels the timeline for financial, technological and growth milestones'' (Baron & Hannan, 2002, p. 30). So too should our scholarship concerning human issues in entrepreneurial ventures include a more careful and comprehensive understanding of the evolving and dynamic nature of HR management in small and emerging enterprises. In short, our responsibility as scholars is to design carefully thought-out integrative studies that explore what we do not yet know about managing nonfounder employees in entrepreneurial ventures.

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