Earnouts in M&A deal structuring: The impact of CEO prevention focus

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Abstract

This empirical study leverages the theoretical underpinnings of the regulatory focus theory to investigate the impact of CEO prevention focus on a firm’s deal structuring choices in mergers and acquisitions. Building on the argument that the prevention focus of an individual is associated with vigilant behavior and preference for non-losses, this study suggests a positive relationship between the acquiring firm CEO’s prevention focus and the firm's propensity to use earnouts, as a post-closing risk-mitigating instrument in the deal consideration structure. Also, this study examines the moderating impact of M&A deals involving foreign targets and the acquiring firm's acquisition experience on the baseline relationship. We tested our predictions on a dataset comprising of 242 deals from 2006 to 2011 in the United Kingdom. Building on the micro-foundations of strategy, these findings contribute to the literature on deal structuring choices in mergers and acquisitions.

Keywords: CEO prevention focus, Deal structuring, Earnouts, Mergers and Acquisitions, Regulatory focus theory, Self-regulatory attributes

1. Introduction

Deal structuring in mergers and acquisitions (M&As) is a critical phase involving decisions on payment mode, deal premium, the extent of equity ownership stake, and so forth (Cuypers *et al.*, 2015; Kim *et al.*, 2011; Malhotra *et al.*,2016). Empirical evidence demonstrates that deal structuring decisions are critical for the acquirer firm as they impact post-deal performance, acquirer's business operations, and risks associated with M&As (Barbopoulos *et al.*, 2018; Dutta *et al.*, 2013; Fuller *et al.*, 2002). To mitigate post-closing risks in M&As, acquiring firms adopt risk-mitigating tools such as earnout[1], which is a contractual agreement between the acquirer and the target firm in their deal consideration structure (Ragozzino and Reuer, 2009). Prior studies on deal-structuring have primarily assessed the effects of firm and industry-specific antecedents that could influence the usage of earnouts (Barbopoulos and Sudarsanam, 2012; Datar *et al.*, 2001; Reuer *et al.*, 2004). It is well established that CEOs of acquiring firms are generally held responsible for the performance consequences of M&As (Zhao, 2002); hence they exercise a significant latitude in such decisions (Malhotra *et al.*, 2018). Attesting this argument, a recent study by Meyer-Doyle *et al.* (2019) finds that CEO related factors explain up to 46.8% variance in M&A associated decisions. Yet, research in M&A literature has not examined the role of CEOs in deal structuring decisions. The current study addresses this oversight by using the theoretical underpinnings of regulatory focus theory to investigate the impact of a critical self-regulatory attribute, the acquiring firm CEO's prevention focus on the firm's propensity to use earnouts in the consideration structure of M&As.

Regulatory focus theory advances the concept of self-regulation, which proposes that individuals have two distinct regulatory foci through which individuals approach goal attainment — promotion and prevention foci (Higgins, 1997, 1998). Levels of prevention and

[1] Earnouts facilitate the acquirer firm in partially transferring the risk to the target by paying a part of the deal consideration up front and the rest is contingent upon the achievement of the pre-defined metrics of target firm's financial or non-financial performance (Barbopoulos and Sudarsanam, 2012; Reuer *et al.*, 2004).

promotion foci in individuals drive distinct needs, trigger goal pursuits through varying means, and shape specific orientations towards loss and gain situations (Crowe and Higgins, 1997; Higgins, 1997, 1998). While needs for growth and advancement drive individuals having high promotion focus, requirements for safety and vigilance drive individuals with high prevention focus (Crowe and Higgins, 1997; Higgins and Spiegel, 2004). The pursuit of *ideal* end-states drives individuals with higher promotion orientation, which determines their focus on achieving gains. On the other hand, people with high prevention focus pay attention to what they *ought* to do, which is consistent with their inclination towards avoiding undesirable end states, by avoiding loss situations (Bilgili *et al.*, 2020). In mergers and acquisitions, the usage of earnouts reduces valuation and adverse selection risks for the acquiring firm in the pre-deal phase and increases the target firm's commitment in the post-merger integration period (Barbopoulos *et al.*, 2018; Kohers and Ang, 2000). Since individuals with high prevention focus prefer to avoid losses and adopt vigilant means of safety and security (Crowe and Higgins, 1997), this study hypothesizes that CEO prevention focus is positively associated with the likelihood of using earnouts in the consideration structure of an M&A deal.

Literature documents that prevention and promotion foci represent orthogonal orientations and are independently connected to other theoretical constructs (Forster *et al.*, 2003; Gorman *et al.*, 2012; Lanaj *et al.*, 2012). As a result, individuals could be high in both foci, high in one and low in one, or low in both the regulatory foci (Bilgili *et al.*, 2020; Lanaj *et al.* 2012). Although CEOs high in promotion focus have concerns for gains and advancement, it does not imply that they pursue M&As at the cost of safety. Further, it is also possible that such CEOs may adopt earnouts as the usage of earnouts is associated with higher returns to the acquirer firm (Barbopoulos *et al.*, 2016). Therefore, due to the lack of theoretical support, we don't predict any relationship between CEO promotion focus and the firm's propensity to use earnouts and limit our inquiry to understanding the influence of prevention focus of acquiring firms' CEOs.

Research documents that the effect of psychological attributes on behavior is not uniform; instead, it varies depending on the situational cues (Malhotra *et al.*, 2018; Mischell, 1977). Relatedly, the current study examines the impact of situational factors on the relationship between CEO prevention focus and firm's propensity to use earnouts by using the conceptualization of regulatory fit and misfit. Regulatory fit (misfit) theory postulates that the effect of a person's regulatory focus on behavior is enhanced (diminished) when the individual regulatory orientation and the situational characteristics are congruent (incongruent) (Higgins, 2000; Johnson *et al.*, 2015). Accordingly, we submit that the context of M&A deals involving foreign targets is one such potential situation that could induce regulatory fit. This is because cross-border transactions involve higher information asymmetry owing to differences in the cultural and institutional norms between home and host countries (Boeh, 2011; Reuer *et al.*, 2004). Also, such deals may pose increased governance risk (Huang *et al.*, 2016), making it difficult for acquiring firms to evaluate the target firm and hence magnify the risk of overpayment (Hansen, 1987). Research also documents that cross-border deals may yield negative returns to the acquiring firm (Moeller and Schlingemann, 2005). Hence, we suggest that the acquiring firm's participation in cross-border transactions creates a regulatory fit with the CEO prevention focus, further enhancing their focus on potential losses. Thus, we hypothesize that M&A deals involving foreign targets accentuate the relationship between CEO prevention focus and the firm's propensity to use earnouts. Next, we conceptualize that if the acquiring firm has prior experience in managing M&As, it renders the CEOs that are high in prevention focus more confident about the focal M&A deal. Because such firms may have acquisition capabilities and well-developed acquisition routines (Finkelstein and Haleblian, 2002), it mitigates prevention-focused CEO's concern for losses, resulting in a regulatory misfit. Therefore, we hypothesize that the acquirer's acquisition experience weakens the relationship between CEO prevention focus and the firm's propensity to use earnouts.

By testing our predictions on a sample of 242 M&A deals by public firms from the United Kingdom during 2006-2011, we hope to enrich the literature on deal structuring in M&As in the following ways. Earnouts are considered effective risk-mitigating mechanisms, and few studies in finance and strategy have analyzed firm and industry level antecedents of earnouts (Barbopoulos and Sudarsanam, 2012; Datar *et al.*, 2001; Ragozzino and Reuer, 2009). We wish to build on this nascent but a growing stream of research by including the role of psychological attributes of CEOs in deal structuring. Specifically, by incorporating the role of CEO prevention focus as an important self-regulatory attribute, we establish the role of human agency in the deal structuring phase, an area of significant interest to strategic management and international business scholars (Contractor, Foss, Kundu, and Lahiri, 2019; Danbolt *et al.*, 2018; Ragozzino and Reuer, 2009; Reuer *et al.*, 2004). By undertaking this study, we also respond to recent calls to further incorporate the role of the psychological characteristics of key decision-makers in the pre-deal phase of M&As (Welch *et al.*, 2019). In M&A literature, a majority of the studies focus on CEO psychological attributes that induce varying risk-taking behavior, the most prominent being the impact of hubris (Hayward and Hambrick, 1997), narcissism (Chatterjee and Hambrick, 2007), and positive emotional traits (Delgado-Garcia *et al.*, 2010). However, what leads to heterogeneity in adopting risk-mitigating approaches is missing so far. The current study addresses this oversight and is probably the first to provide evidence of CEO attributes, which leads to risk-mitigating approaches in M&As. Finally, we also contribute to recent calls to expand the literature on regulatory focus theory in the realm of contracts (Johnson *et al.*, 2015) by suggesting that CEO prevention focus plays a decisive role in the usage of contingent contracts in the context of mergers and acquisitions.

2. Conceptual development

Though M&As are ubiquitous vehicles of corporate strategy (Cartwright and Schoenberg, 2006), acquirers invariably face significant information asymmetry leading to valuation challenges, risks of overpayment, adverse selection and moral hazard problems (Akerlof, 1970; Balakrishnan and Koza, 1993; Graebner, 2009; Kohers and Ang, 2000; Varaiya and Ferris, 1987). Additionally, M&As not only involve significant resource commitments (Shimizu *et al.*, 2004) but also run risks due to integration difficulties arising from non-participation or attrition of the target firm's top management team (Krug *et al.,* 2014). To reduce exposure to such post-closing risks, acquiring firms adopt deal structures that are flexible in terms of payments such as contingent value rights or performance-contingent payout structures, commonly referred to as earnouts, (Kohers and Ang, 2000; Ragozzino and Reuer, 2009).

Earnouts are contingent payments structured in two parts – an initial upfront payment to the target firm and a subsequent payment that is contingent upon the target's achievement of performance goals during the post-acquisition phase (Reuer *et al.*, 2004). Structuring the consideration through earnouts partially transfers the valuation risk to the target firm by deferring a contingent payment based on mutually agreed-on pre-specified goals (Kohers and Ang, 2000; Ragozzino and Reuer, 2009). A high-quality target firm will view this arrangement favorably because it may gain more accurate value for its resources. On the other hand, the acquirer is safeguarded against making higher payments (Barbopoulos and Sudarsanam, 2012). Also, recent empirical studies find that acquiring firms incorporating earnouts in their deal structures experience positive returns (Barbopoulos *et al.*, 2016; Barbopoulos *et al.*, 2018).

Extant literature notes the proliferating use of earnouts in M&A deals that involve unlisted targets (Barbopoulos and Sudarsanam, 2012), or targets that belong to high-technology (Reuer *et al.,* 2004), or fast-growing industries with unrecorded assets (Datar *et al.,* 2001). Empirical evidence also provides evidence of higher usage of earnouts in situations where the acquirer and the target firm operate in unrelated businesses (Datar *et al.,* 2001). Despite these valuable contributions, the literature has not considered the role of the CEOs of acquiring firms, essentially assuming that all executives perceive risk similarly. This omission is significant, mainly because CEOs bear the terminal responsibility of performance issues in M&A deals (Hambrick, 2007; Zhu and Chen, 2015) and hence exercise considerable latitude in influencing decisions related to the whole M&A process (Malhotra *et al.,* 2018). Recent research also reveals that relative to other firm-specific factors attributes specific to the CEO explain higher variance in M&A decisions (Meyer-Doyle *et al.*, 2019). Thus, we believe it is pertinent that M&A scholarship must assess the role of the CEO in impacting the design of deal structuring that could reduce the acquiring firm's exposure to risks.

Psychological attributes of the CEO's personality, self-concept, and self-regulation have been subjects of growing interest in the M&A literature (Chatterjee and Hambrick, 2011; Gamache *et al.,*2015; Malhotra *et al.,* 2018). Earlier studies investigate and find that personality traits such as CEO extraversion (Malhotra *et al.,* 2018), CEO overconfidence (Billett and Qian, 2008) and self-regulatory attributes such as CEO regulatory focus (Gamache *et al.*, 2015) impact the firm's likelihood of engaging in acquisitions in terms of the number and size. Furthermore, self-concept and personality-related attributes ─ CEO hubris (Hayward and Hambrick, 1997) and CEO narcissism (Chatterjee and Hambrick, 2007, 2011), are found to influence the magnitude of acquisition premia positively. In comparison to the psychological attributes of personality and self-concept, the individual regulatory focus is likely to have a more direct effect on individual behavior (Barrick *et al.*, 2002; Gamache *et al.*, 2020; Lanaj *et al.*, 2012). Consequently, a growing stream of literature in entrepreneurship and strategic management analyzes the influence of the CEO regulatory focus on strategic actions and responses (Gamache *et al.*, 2020; Kashmiri *et al.*, 2019; Weber and Mayer, 2011; Wowak and Hambrick, 2010).

Introduced by Higgins (1997, 1998), regulatory focus theory explains dual, orthogonal mechanisms of self-regulatory motivations ─ promotion and prevention foci that determine goal attainment behavior. Individuals with a high promotion focus are concerned about *ideal* states and hence focus their attention on opportunities for advancement, engaging in actions that maximize gains and minimize non-gains (Bilgili *et al.*, 2020; Crowe and Higgins, 1997; Higgins, 1998; Pennington and Roese, 2003). However, people with high prevention focus are more concerned with *ought* states and sensitive to the presence and absence of negative outcomes (Higgins, 1998). This concern reflects their preference for strategic means, which is related to a vigilant strategy that ensures “correct rejections and insures against errors of commission” (Crowe and Higgins, 1997: p.120). Hence, individuals with higher prevention focus are more likely to engage in actions that maximize non-losses and minimize losses (Higgins and Spiegel, 2004; Zou *et al.*, 2014).

Research chronicles that biological dispositions influence individual preferences for approach and avoidance strategies, such that they remain mainly consistent over time (Brockner and Higgins, 2001; Higgins, 1997). However, similar to the constraining effects of situations on the relationship between individual personality and behavior (Meyer *et al.*, 2010; Mischell and Shoda, 1995), situational cues also influence the effect of individual regulatory foci on behavior (Higgins, 2000). A match between individual regulatory focus and the situational characteristics leads the regulatory focus to grow stronger and generates a sense of “feeling right” resulting in the phenomenon of regulatory fit (Higgins, 2000; Zou *et al.*, 2014). Conversely, a misalignment between individual regulatory focus and situational characteristics attenuate the effect of a person’s regulatory focus and diminishes the sense of "feeling right" resulting in regulatory misfit (Adomako *et al.*, 2017; Fasaei *et al.*, 2018). In summary, the individual regulatory focus is a function of both the person's disposition and the environment within which they operate.

In comparison to personality traits and self-concept attributes that exhibit indirect effects on behavior, the individual regulatory focus being a self-regulatory attribute influences goal attainment strategy, is proximal to behavior; hence is expected to be a better predictor of individual behavior (Hoyle, 2010; Lanaj *et al.*, 2012; Scholer and Higgins, 2008). Prior studies indicate a relationship between an individual's regulatory orientation, risk perception, and risk-taking (Bryant and Dunford, 2008; Lin *et al.*, 2012). Individuals with high prevention focus are sensitive to negative consequences of action, perceive risk as unfavorable, and exhibit risk avoidance propensity in situations that could lead to a loss (Bryant and Dunford, 2008; Grant and Higgins, 2003; Higgins, 1998). They are more aware of the negative consequences of any action and perceive risk as negative (Crowe and Higgins, 1997). Since prevention focus is associated with a higher preference for safety and vigilance, the current study takes a closer look at M&A deal structuring by evaluating how CEO regulatory orientation, mainly CEO prevention focus influences the firm's propensity to use earnouts as a payment structuring solution.

2.1. CEO prevention focus and the likelihood of using earnouts

As discussed previously, acquisitions are challenging decisions because of their inherent ex-ante and ex-post complexities, which expose acquiring firms to risk (Harford and Li, 2007; Lehn and Zhao, 2006; Nadolska and Barkema, 2007). However, in the pursuit of acquisitions, CEOs may perceive these risks differently based on their regulatory orientation, which is likely to impact their emphasis on safety and security protocols, hence guiding the design of deal structures. Some CEOs might engage in strategic avoidance behaviors (Higgins, 1998) by being more careful and over-analytical to ensure non-losses (Brockner and Higgins, 2001). Bryant and Dunford (2008) argue that people with high prevention focus exhibit risk avoidance behavior, particularly while making decisions involving potential losses. Since acquisitions are events that often fail to realize their intended objectives and result in wealth losses for the acquirers (King *et al.*, 2004; Moeller and Schlingemann, 2005), Gamache *et al.* (2015) ascertain that CEO prevention focus is negatively associated with the likelihood of making acquisitions.

Building on the above stream of research, we submit that once the firm decides to acquire, the structure of the deal would be impacted by the regulatory attributes of the CEO. We argue that when CEOs having high prevention focus undertake acquisitions, they remain stimulated by the need for safety and security and tend to exhibit vigilant behavior (Brockner and Higgins, 2001). For example, they might worry about executing a bad acquisition or paying higher premia, which could result in losses for the acquiring firm (Lehn and Zhao, 2006). Moreover, CEOs with high prevention focus are also guided by a sense of responsibility and obligation (Higgins, 1997), particularly towards the firm's stakeholders (Gamache *et al.*, 2020; Kammerlander *et al.*, 2015). Since most of the M&As may yield negative returns to the acquirer firm shareholders (King *et al.*, 2004), CEOs with high prevention focus may be more inclined to risk-reducing deal structuring arrangements to minimize or avoid losses. Motivated by these concerns, such CEOs might consider adopting flexible deal structuring devices such as earnouts that partly transfer risks to the target firm (Ragozzino and Reuer, 2007).

Put-together, we posit that there is heterogeneity in the risk perceived by CEOs, based on their regulatory orientation. CEOs with high prevention focus perceive higher risk in M&As, remain more vigilant and careful in deal structuring, and are more likely to adopt earnouts to mitigate potential risks. Formally, we hypothesize:

> *H1:* The acquiring firm CEO’s prevention focus is positively associated with the likelihood of using earnouts in the consideration structure of M&As.

2.2. CEO prevention focus, regulatory fit and misfit, and the likelihood of using earnouts

Situational characteristics also influence the extent to which psychological attributes impact behavior. For instance, psychological attributes related to an individual's personality are subject to the constraining effects of situations that affect behavior (Chatterjee and Hambrick, 2011; Malhotra *et al.*, 2018; Mischell, 1977; Mischell and Shoda, 1995). Similarly, in regulatory focus theory, there is an inherent concept of regulatory fit and misfit, which emphasizes the role of situational cues in augmenting and diminishing the impact of an individual's regulatory orientation (Brockner and Higgins, 2001; Higgins, 2000). The congruence between the situational factors and an individual's regulatory focus leads to a phenomenon called regulatory fit, wherein the effects of individual regulatory focus are accentuated (Higgins, 2005). For example, under conditions of increasing competitive intensity, firms are required to formulate strategies based on competitor moves. In such instances, inaction by firms could lead to failure in exploratory projects, which is congruent with CEO prevention focus need for responsibility and attention towards ensuring non-losses, thereby creating a regulatory fit (Kammerlander *et al.,* 2015). In contrast, the incongruence between the situational factors and the individual regulatory foci results in the phenomenon of regulatory misfit (Johnson *et al.*, 2015), which ensues in a diminished impact of the individual regulatory focus. For instance, environments characterized by dynamic conditions need firms to be creative, show greater willingness to adapt and explore new business opportunities to be effective. This situation is at odds with CEO prevention focus that is associated with a lack of creativity and preference for the status quo, resulting in regulatory misfit (Wallace *et al.*, 2010). Prior literature accounts for the role of situational factors such as executive compensation (Gamache *et al.,* 2015), performance feedback, organizational culture (Brockner and Higgins, 2001), competitive intensity (Adomako *et al.,* 2017), and environmental dynamism (Wallace *et al.*, 2010) leading to regulatory fit or misfit. Taking cues from the M&A literature, and by building on the regulatory fit or misfit perspective (Higgins, 2000, Johnson *et al.,* 2015), we explore two situational characteristics – First, when acquirers engage in cross-border deals and second when the acquiring firm has prior experience in making acquisitions. We develop our next two hypotheses based on these two situational contexts.

2.2.1. Cross-border M&A deals

We suggest that M&A deals involving foreign targets may impact the relationship between the prevention focus of acquiring firm's CEO and the usage of earnouts. Information asymmetry, an issue associated with M&A deals (Akerlof, 1970), is significantly higher in cross-border deals compared to domestic deals, which leads to the liability of foreignness (Zaheer, 1995). Besides, acquiring firms may find it challenging to evaluate the target firm and could experience a higher risk of overpayment (Reuer *et al.*, 2004; Shimizu *et al.*, 2004). The cultural and the institutional differences between the acquiring and the target firm nations further widen the information gap (Huang *et al.*, 2016; Markides and Ittner, 1994; Nadolska and Barkema, 2007; White *et al.*, 2018) and thereby enhances deal uncertainty (Lee and Caves, 1998). Cross national acquisitions also encompass normative and cognitive differences between home and host countries (Chao and Kumar, 2010). Therefore, cross-border acquisitions might be value-destroying for acquiring firms (Moeller and Schlingemann, 2005). Research also suggests that country-specific governance factors such as labour market regulations impact cross-border M&A deal synergies and acquirer returns (Alimov, 2015; Levine *et al.*, 2020). Besides, cultural and linguistic differences between the acquiring and the target firm also pose significant challenges in the post-merger integration phase (Brouthers and Brouthers, 2000; Graebner *et al.*, 2017). Put-together, cross-border M&A deals expose an acquiring firm to the possibility of substantial losses. Hence, M&A deals involving foreign targets is a crucial contingency influencing the CEO's risk perception about the focal deal.

For CEOs with high levels of prevention focus, M&A deals involving foreign targets parallels their loss frame focus since such deals are regarded riskier and ridden with more challenges for the acquiring firm. Hence, such CEOs with high prevention focus may seek to reduce the uncertainty associated with deals by taking a more vigilant stance and insure against errors of commission. Moreover, cross-border M&A deals may result in extreme negative returns to the acquirer firm (Moeller and Schlingemann, 2005), which may adversely affect the firm's shareholders. This could further increase the sense of responsibility of CEOs with higher prevention focus towards their shareholders, creating a situation of regulatory fit and consequently augmenting their need to protect the potential wealth erosion of the firm’s shareholders. As a result, we expect that M&A deals involving foreign targets will exacerbate the impact of CEO prevention focus on the propensity to use earnouts in their deal consideration structure. Against this backdrop, we hypothesize:

> *H2:* M&A deals involving foreign targets strengthen the positive relationship between CEO prevention focus and the likelihood of using earnouts in the consideration structure of M&As.

2.2.2. Acquisition experience

A rich body of research in the M&A literature has emphasized the importance of organizational acquisition experience in determining the firm's future acquisition behavior and outcomes (Finkelstein and Haleblian, 2002; Haleblian *et al*., 2006). Organizational acquisition experience leads to the accumulation of knowledge and the formation of routines that are programs of action that firms refer to in future decision-making processes (Barkema and Vermeulen, 1998; Levitt and March, 1988). These routines act as templates for acquiring firms while identifying, evaluating and selecting target firms (Capron and Shen, 2007; Haleblian *et al.*, 2006), and reducing chances of adverse selection (Akerlof, 1970; Balakrishnan and Koza, 1993). Evidence shows that acquisition experience also helps in setting guidelines for managing the post-acquisition integration process (Zollo and Singh, 2004) through the identification and integration of resources, thereby avoiding integration-related problems

(Haspeslagh and Jemison, 1991; King *et al.*, 2004). Acquisition experience serves context specific knowledge to tackle acquisitions and consequently reduces the chances of failure (Elango *et al.*, 2013) as research also points out that acquisition experience assists in realizing better post-acquisition performance (Bruton *et al.*, 1994; Haleblian and Finkelstein, 1999). In summary, we submit that organizational acquisition experience benefits the acquirer firm in managing subsequent acquisitions more effectively.

According to the theory of regulatory fit and misfit (Higgins, 2000; Johnson *et al.*, 2015), a misfit between the individual regulatory orientation and the situational conditions attenuates the effects of the individual regulatory foci. Building on this line of argument, we posit that organizational knowledge resulting from prior acquisition experiences renders the CEO, less worried about the organization’s capabilities in managing the risks associated with the focal deal. Besides, prior experience guides the evaluation and selection of subsequent target firms, which may assist the CEO in assessing the true quality of the target firm. Finally, as firms with prior organizational acquisition experience perform better than firms without any experience (Lubatkin, 1983), the CEO is expected to perceive less performance risk associated with the focal M&A deal. Consequently, prior acquisition experience may mitigate the vigilant stance of CEOs with a high prevention focus, resulting in reduced risk perception about the focal M&A deal. Hence, this creates a situation of a regulatory misfit with the CEO prevention focus, wherein the acquirer's prior acquisition experience acts as a counteracting force that attenuates the impact of acquiring firm CEO's prevention focus. Thus, we hypothesize that:

> *H3:* Greater acquisition experience of the acquiring firm weakens the positive relationship between CEO prevention focus and the likelihood of using earnouts in the consideration structure of M&As.

Figure 1 illustrates the conceptual model with baseline and moderating hypotheses.

Insert Figure 1 about here

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3. Data and Methods

3.1 Data

We tested our theoretical model on completed and majority stake[2] acquisitions of private target firms by public firms of the United Kingdom from 2006 to 2011. We collected data on M&A deals and other related variables from the SDC Thomson database (Ragozzino and Reuer, 2009). Additionally, we used the Thomson Reuters Eikon database for extracting financial fundamentals data and annual reports of our sample firms (Aguilera *et al.*, 2017).

We started with the whole population of completed and majority stake acquisitions of private targets by listed firms of the United Kingdom. We then applied the following filters to arrive at our final sample. (i) A deal should not be related to regulated industries, such as energy, power, real estate, and financial services sectors (Aguilera *et al.*, 2017; Barbopoulos and Sudarsanam, 2012). (ii) Annual reports of the acquirer firms for the preceding year to the focal deal should be available. (iii) In the annual reports of acquiring firms, CEO letters to shareholders or CEO reviews should be available. (iv) Financial data across the sample years (2006 to 2011) should be available. This data filtering and cleaning process led us to a final sample of 242 deals.

3.2. Variables and measurements

3.2.1. Dependent variable

Earnouts. Following existing literature, we used a dichotomous variable to indicate usage of *earnout* in an M&A deal consideration structure (Barbopoulos and Adra, 2016;

[2] To focus on significant deals, prior studies (for e.g., Capron and Shen, 2007; Gubbi *et al*., 2010; Kroll *et al.*, 1990) have sampled majority acquisitions where more than 50% stake in target firm is acquired.

Kohers and Ang, 2000). This variable would take the value of ‘1’ if *earnout* was incorporated in the deal consideration structure and ‘0’ otherwise.

3.2.2. Explanatory variables

CEO prevention focus. Consistent with the prior literature (Keil *et al.*, 2015; Nadkarni and Chen, 2014), we used CEO letters to shareholders/CEO reviews[3] to capture *CEO prevention focus*. We conducted a computer-aided content analysis of these letters of CEOs or CEO reviews available in annual reports of firms in our sample. Recorded statements such as CEO’s letters to shareholders and reviews are considered relevant in capturing the beliefs and cognitive representations of the top management team, as they are devoid of individual biases and beliefs (Fiol, 1994; Nadkarni and Barr, 2008). Although this approach comes with a limitation that ghostwriters may write such portions on behalf of the CEO and are targeted towards specific audiences, however, literature has argued that the CEO holds legal obligation for these two portions of the annual report (Craig and Amernic, 2011). Since the CEO must attest the content in the letters, s/he is significantly involved in crafting the letters to shareholders (Duriau *et al.*, 2007). Content in these letters is also similar to the speeches by the CEO in public, answers to questions in the press conferences, and speeches in press releases (Nadkarni and Chen, 2014). In previous studies, such sources have been extensively used by scholars to operationalize latent constructs related to CEO cognition (Amernic and Craig, 2004; Craig and Amernic, 2011; Hambrick *et al.*, 1993; Nadkarni and Chen, 2014). Relative to interviews, content analysis technique also offers certain advantages: This technique is unobtrusive and overcomes issues of non-availability of CEOs and recall biases of informants (Duriau *et al.*, 2007; Gaur and Kumar, 2018; Morris, 1994).

[3] In some annual reports, in the place of CEO letters to shareholders CEO reviews addressing the shareholders were available and thus we used CEO reviews (Nadkarni and Chen, 2014) in the cases where CEO letters to shareholders were absent.

For each focal deal in our sample, we collected the annual report of the preceding year from the Thomson Reuters Eikon database. The missing reports were supplemented by online websites and resources such as Morningstar, London Stock Exchange, Company websites, and Google search. We then extracted CEO letters to shareholders or CEO reviews from the annual reports. For content analysis of CEOs' letters to shareholders/reviews, we used the dictionary of regulatory focus words developed and validated by Gamache *et al.,* (2015) (see Appendix). The regulatory focus dictionary conforms to content validity, convergent validity, and discriminant validity. The dictionary consists of 25 prevention focus words and their alternative tenses to capture the prevention focus of CEOs. For executing the content analysis of CEOs' letter to shareholders, we wrote a program in R-software. Using this program, we generated the total number of words in letters to shareholders and also the total number of prevention focus words spoken by the CEO. Further, we normalized the words by calculating the percentage of prevention focus words in the letter to shareholders or reviews to account for the differences in the size of CEO speeches. Thus, the percentage of prevention focus words in the letters to shareholders indicates the prevention focus score.

Cross-border. As previously discussed, compared to domestic deals, cross-border deals entail relatively higher risks due to cultural and institutional differences (Nadolska and Barkema, 2007). Accordingly, we used a binary variable, *cross-border,* to classify deals into cross-border (coded as '1') and domestic (coded as ''0').

Acquisition experience. Consistent with the literature, we measured *acquisition experience* as the number of acquisitions made by the acquiring firm in the preceding five years to the focal deal (Hayward, 2002).

3.3. Control variables

To control for the potential confounding effects, we controlled for several variables that could impact the likelihood of using earnouts in a deal consideration structure. We controlled for the acquirer's *financial leverage* as better financial health may induce the risk appetite of the acquiring firm (Ragozzino and Reuer, 2009). We measured it as the ratio of total assets to total liabilities four weeks before the deal. We also controlled for the acquirer's *price-to-earnings ratio* four weeks before the focal deal as the acquirer's profit could impact the deal consideration structure (Barbopoulos and Sudarsanam, 2012).

High technology industries are associated with rapid changes that generate risks (Reuer *et al.*, 2004) that could impact the influence of prevention focus due to regulatory fit. Hence, we included *target high technology industry* as a control variable. Consequently, following prior research (Reuer *et al.*, 2004), we classified the target firms into high technology (coded as '1') and low-technology industry (coded as '0') based on standard industry classification codes[4]. Since unrelated acquisitions carry more risk than the related ones, we used a binary variable to measure *industry relatedness* with two-digit codes (Graffin *et al.*, 2016), and we coded this variable as '1' for related industry and '0' otherwise. Higher equity control is associated with more risks due to resource commitments (Chari and Chang, 2009), which may induce acquirers to adopt earnouts in the consideration structure. Therefore, we controlled for *equity control* by the acquirer. We measured the *equity control* as the percentage of shares acquired by the acquirer firm in the target at the time of the deal announcement.

Since young CEOs have an appetite for higher risks and growth (Yim, 2013), we included *CEO age*, measured at one year preceding the focal deal. As discussed previously, regulatory focus theory postulates that two regulatory foci are orthogonal and are uniquely related to other theoretical constructs (Gorman *et al.*, 2012). Accordingly, we used *CEO*

[4]Standard industry classification codes of high technology industries are as follows- computer equipment-357X, computer software and computer services – 737X and 874X, bio-technology-873X, electronics and communications-360X-367X, 48XX, 50XX, 7319 and other high technology industries -272X, 282X, 283X, 371X, 372X, 305X, 381X-384X.

promotion focus[5] as a control to demonstrate that it has no impact on the dependent variable of this study. Further, to account for the fixed effects of the acquiring firm's industry, we also included industry dummies (using two-digit industry standard industry classification codes) as control variables in the analysis. Finally, we also included year dummies to account for the year fixed effects.

3.4. Empirical analysis and results

Since our dependent variable, called *earnouts*, has dichotomous states, we used binary logit regression to examine our hypotheses. We used the following mentioned binary logit models to estimate the hypothesized effects.

Model 1: $\ln\left[\frac{P}{1-P}\right] = \beta_0 + \beta_1(\text{Controls}) + \boldsymbol{\varepsilon}$

Model 2: $\ln\left[\frac{P}{1-P}\right] = \beta_0 + \beta_1(\text{Controls}) + \beta_2(\text{CEO prevention focus}) + \boldsymbol{\varepsilon}$

Model 3: $\ln\left[\frac{P}{1-P}\right] = \beta_0 + + \beta_1(\text{Controls}) + \beta_2(\text{CEO prevention focus}) + \beta_3(\text{Cross-border}) + \beta_4(\text{CEO prevention focus} \times \text{Cross-border}) + \boldsymbol{\varepsilon}$

Model 4: $\ln\left[\frac{P}{1-P}\right] = \beta_0 + \beta_1(\text{Controls}) + \beta_2(\text{CEO prevention focus}) + \beta_3(\text{Cross-border}) + \beta_4(\text{CEO prevention focus} \times \text{Cross-border}) + \beta_5(\text{Acquisition experience}) + \beta_6(\text{CEO prevention focus} \times \text{Acquisition experience}) + \boldsymbol{\varepsilon}$

Where, p = Probability of using earnouts and

ε = Error term.

Table 1 provides descriptive statistics for the variables used in the study. Low correlation values among independent variables indicate no multicollinearity problem. However, we calculated the variance inflation factor, which is well below the cut-off limits,

[5] Similar to prevention focus, using the regulatory focus dictionary developed by Gamache *et al.*, (2015), we measured *CEO promotion focus* as the percentage of promotion focus words in the letters to shareholders by the CEO. As previously discussed, Gamache *et al.*, (2015) developed and validated the dictionary of regulatory focus words where they have categorized 27 words and their alternative tenses as the promotion focus words.

mitigating any concerns of multicollinearity (Burns and Bush, 2000). Similar to the previous studies in the literature (Gamache *et al.*, 2015; Kammerlander *et al.*, 2015), we found a low and insignificant correlation (r = -0.08, $p > 0.1$) between *CEO prevention focus* and *CEO promotion focus* which asserts that prevention and promotion foci are independent constructs.

Insert Table 1 about here

Table 2 presents the results of the binary logit regression models. Model 1 includes only control variables. The insignificant coefficient of *CEO promotion focus* (Model 1: -0.072, $p >$ 0.1) indicates that the *promotion focus* of acquiring firm's CEO has no impact on the likelihood of using *earnouts*. Furthermore, we found a negative relationship between *relative size* and the likelihood of using earnouts (Model 1: β = -2.084., $p < 0.1$), suggesting that acquirer firms may avoid using *earnout* contracts in large-sized acquisition deals.

In Model 2, we included the main independent variable of *CEO prevention focus*. Our first Hypothesis (H1) predicts that the CEO prevention focus is positively related to the likelihood of using earnouts in the deal consideration structure. A positive and significant coefficient of variable *CEO prevention focus* (Model 2: β = 0.906, $p < 0.01$) provided support for Hypothesis 1 that a relatively more vigilant CEO is likely to include the post-closing risk instrument of *earnouts* in M&A deals. Our results complement the findings of previous studies (Kammerlander *et al.*, 2015; Kashmiri *et al.*, 2019) that prevention-focused CEOs tend to mitigate risks.

Since, in non-linear models such as binary logit regressions, we cannot just rely on the value of regression coefficients and p values (Ge and Whitmore, 2007). Hence, we calculated the magnitude of effect using the odds ratio formulae $\ln\left[\frac{P}{1-P}\right] = \beta_0 + \beta_1(X)$ where p is the probability of an event occurring or likelihood of using earnouts, β_0 and β_1 are the regression coefficients of constant and the main covariate in the main model (Model 2 in Table 2).

Keeping the other effects constant, when *CEO prevention focus* is at its mean value (0.64), the probability of using earnouts is 0.64. Furthermore, an increase in the magnitude of *CEO prevention focus* by one standard deviation (0.56) to the mean increases the probability further by 0.1. These values reassert the positive relationship between *CEO prevention focus* and the likelihood of using earnouts.

The second Hypothesis (H2) checks whether *cross-border* transactions create a situation of regulatory 'fit' and strengthen the relationship between CEO prevention focus and usage of earnouts. To test the same, we created an interaction term *CEO prevention focus* × *Cross-border* and added it in Model 3. The insignificant and negative coefficient of the interaction term *CEO prevention focus* × *Cross-border* (Model 3, $\beta = -0.037$, $p > 0.1$) does not offer support for H2. This result is surprising and warrants further attention of international business scholarship. However, we surmise that when targets are located in other countries, the uncertainties related to determinacy of law enforcement in contractual obligations (Weitzel and Berns, 2006) may outweigh the risks associated with M&As. Hence, the expected positive moderation effect on the relationship between our base-line hypothesis could not establish its significance

In the third Hypothesis (H3), we aim to test the concept of regulatory misfit that acquisition experience of the acquirer firm should reduce the vigilant stance of the CEO with a high prevention focus. To test the same, we created an interaction term *CEO prevention focus* × *Acquisition experience* and included it in Model 4. In Model 4, the coefficient of the interaction term is negative and significant (Model 4: $\beta = -0.160$, $p < 0.05$). As mentioned earlier, in the non-linear models such as binary logit models, we could not depend on the regression coefficients to interpret the results. Hence, similar to the interpretation of our base-line hypothesis, we used the odds ratio formulae $\ln [\frac{P}{1-P}] = \beta_0 + \beta_1(X)$ where p is the probability of an event occurring or likelihood of using earnouts, β_0 and β_1 are the regression coefficients of the constant and the interaction term *CEO prevention focus* × *Acquisition experience* (Model 4 in Table 2). Keeping the other effects constant, at the mean value of *acquisition experience* (6.24), the probability of using earnouts is 0.269. The addition of one standard deviation of *acquisition experience* (4.49) to its mean decreases the probability of earnouts by 0.117, asserting that greater *acquisition experience* weakens the relationship between *CEO prevention focus* and the likelihood of using *earnouts.*

Insert Table 2 about here

Figure 2 illustrates the interaction effect of *CEO prevention focus* and acquirer's *acquisition experience* (from Model 4 in Table 2). The values of the mean and standard deviation of CEO prevention *focus* intensity are 0.64, and 0.56, respectively. In Figure 2, the low and high values of *CEO prevention focus* are calculated as one standard deviation below (0.09) and above the mean value (1.20). Further, the mean and standard deviation values of *acquisition experience* are 6.24 and 4.49, respectively. Low and high *acquisition experiences* are one standard deviation below (1.75) and one standard deviation above (10.73) the mean value of acquirer *acquisition experience*. The positive relationship between *CEO prevention focus* and the likelihood of using *earnouts* is relatively weaker for the deals with high values of acquirer's *acquisition experience* and stronger for the deals with low values of acquirer's *acquisition experience*.

Insert Figure 2 about here
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4. Discussion and conclusion

Leveraging on the regulatory focus theory as the guiding theoretical lens, in this paper, we find that prevention focus of the acquiring firm CEOs influences their perceptions of risks and impacts the usage of risk-mitigating instruments such as earnouts in M&A deal structuring.

M&As entail a lot of potential risks for the acquirer firm such as the issues of overpayment (Ragozzino and Reuer, 2009), adverse section (Reuer *et al.*, 2004), attrition of target firm's top management team (Krug *et al.*, 2014; Lee and Alexander, 1998), and issues concerning post-merger integration difficulties leading to the potential erosion of wealth (Ellis *et al.*, 2011; Graebner *et al.*, 2017; Kohers and Ang, 2000). To alleviate these risks, organizations adopt appropriate deal structures that include flexible payment mechanisms such as earnouts. While the literature has predominantly assessed the effect of firm and industry-specific attributes on the acquiring firm's propensity to use earnouts in the M&A deal structure (Barbopoulos and Sudarsanam, 2012; Datar *et al.*, 2001), the role of the CEO, albeit important, remain under-researched (Contractor et al., 2018). Prior studies note that the acquiring firm's CEO enjoys significant latitude in M&A related decisions (Chatterjee and Hambrick, 2011; Malhotra *et al.*, 2018), with CEO specific effects explaining up to 46.8% of the total variance in various decisions associated with the M&A process (Meyer-Doyle *et al.*, 2019). As such, this study is focused on examining the effect of CEO regulatory focus; specifically, the influence of CEO prevention focus on the acquiring firm's propensity to use the post-closing risk-mitigating instrument of earnouts.

The regulatory focus theory explains the self-regulation mechanism of individuals through two orthogonal approaches - promotion and prevention foci in guiding goal-directed behavior (Higgins, 1997, 1998). An individual's regulatory focus influences perception of risk (Bryant and Dunford, 2008), determines the preference for safety (Higgins, 1997), and is an important individual-level determinant of firm-level strategic outcomes (Wowak and Hambrick, 2010). In particular, individuals with high prevention focus are driven by needs of safety, obligation, and adopt a vigilant strategy (Crowe and Higgins, 1997). Thus, we submit that self-regulatory characteristics, as manifested in the prevention focus of the acquiring firm's CEO, influences the firm's perceptions about risks involved in M&A deals, which in turn affect the firm's propensity to adopt risk-mitigating instruments of earnouts. In a sample of 242 M&A transactions involving the majority-stake acquisition of private targets by public firms from the United Kingdom, our findings attest to our theorization for the positive relationship between the CEO prevention focus and the propensity to use earnouts.

The effect of psychological attributes on behavior is influenced by the situational influences too (Malhotra *et al.*, 2018; Meyer *et al.*, 2010; Mischell and Shoda, 1995) and regulatory focus theory conceptualizes this with regulatory fit and misfit. The congruence (incongruence) between the situational stimuli and the individual regulatory focus leads to regulatory fit (misfit), culminating in an enhanced (diminished) effect of individual regulatory focus on behavior. Therefore, building on the concept of regulatory fit and misfit, we posit that situational factors strengthen and weaken the impact of individual regulatory focus on behavior (Higgins, 2000, 2005). We advance two such situational factors ─ M&A deals involving foreign targets and the acquirer's acquisition experience, respectively. We maintain that in M&A deals involving foreign targets, acquirers may experience information disadvantages, overpayment risks, negative returns (Shimizu *et al.*, 2004), and post-merger integration issues (Graebner *et al.*, 2017). Hence, we theorize that cross-border deals accentuate the impact of prevention focus of the acquiring firm’s CEO leading to higher vigilant behavior. However, our empirical results do not offer support for our theorization about the positive moderation effect of the cross-border deals on the relationship between CEO prevention focus and the likelihood of using earnouts in the deal structuring phase. We conjecture that the possible contractual hazards rising from the complexities embedded in cross-border deal terms (Weitzel and Berns, 2006) and regulatory constraints may outweigh the risks of M&As as perceived by the prevention-focused CEOs and as a result the moderation effect has a muted significance. Additionally, we post that that on account of acquisition experience, the acquirer firm builds well-defined acquisition routines (Barkema and Vermeulen, 1998), and gains capabilities to evaluate the target (Capron and Shen, 2007). Consequently, the acquirer firm understands the nuances to realize better acquisition performance (Vermeulen and Barkema 2001), which acts as a counterbalancing force to CEO prevention focus. Accordingly, using the concept of regulatory misfit, we hypothesized and found support that the acquirer's acquisition experience weakens the impact of the prevention focus of the acquiring firm's CEO on the likelihood of using earnouts.

We wish to offer some vital contributions. First, we extend nascent but a growing stream of literature on deal structuring by recognizing the role of human agency – in particular the role of CEO self-regulatory attributes. The prior research examining antecedents that influence the usage of earnouts in M&A deals have yielded interesting results, but predominantly it has remained focused on the firm and industry level characteristics (Datar *et al.,* 2001; Mantecon, 2009; Reuer *et al.,* 2004), while the role of acquiring firm's CEO has remained under-researched. This study is probably the first to attest the impact of CEO psychological attributes as a critical antecedent impacting the design of deal structures. Through this, we attempt to respond to recent impetus and calls in strategy and international business scholars to focus on micro-foundational underpinnings (Danbolt *et al.*, 2018; Contractor *et al.*, 2019). Through this paper, we also respond to recent calls to include psychological explanations in the pre-deal phase of M&As (Welch *et al.*, 2019). Second, while prior research has assessed the effect of CEO psychological attributes such as personality attributes, narcissism, and hubris on risk-taking behavior (Chatterjee and Hambrick, 2011; Hayward and Hambrick, 1997; Malhotra *et al.*, 2018), yet how CEO self-regulatory attributes influence risk tolerance and direct the incorporation of risk mitigation plans, is seldom studied. We believe that these novel findings complement and extend the scholarship examining the role of CEOs in M&As. Furthermore, by positioning CEO regulatory focus as a crucial factor that influences the choice of contingent contracts such as earnouts in M&A, we attempt to answer recent calls for research into the link between regulatory focus theory and contractual mechanisms (Johnson *et al.*, 2015).

We believe that these findings also have significant implications for management practice, especially for CEOs and boards of directors. Earnouts have been associated with positive returns to the acquirer (Barbopoulos and Sudarsanam, 2012), but they can also lead to contractual hazards (Reuer, 2005), especially in countries with weak contractual enforcements. Therefore, CEOs should take cognizance of their regulatory orientation before deciding to use this instrument in uncertain institutional environments. Since congruent situational factors can enhance the impact of CEO prevention focus, boards of directors should be mindful of factors that might enhance or mitigate this self-regulating orientation.

As is the case with all empirical research, this study has limitations, which could spur further action in this field. Although CEOs have a proportionately higher say in strategic decision making (Finkelstein *et al*., 2009), firm-level decision making also involves the active participation of other members of the top management team (Chen *et al*., 2018; Hambrick, 1987; Papadakis and Barwise, 2002). Future studies could analyze the combined impact of the regulatory foci of the CEO and other members of the top management team together in M&A deal structuring (Johnson *et al.,* 2015). While the current study focuses on the moderating effect of the firm-level acquisition experience, future studies could assess how the CEO's acquisition experience influences the impact of their regulatory orientation, thereby impacting firm behavior. Moreover, the current study is contextual and is based on M&A deals in a single country; hence additional studies should explore multi-country samples to examine whether cultural attributes (Hofstede, 1980), such as high or low uncertainty avoidance, have direct or interactive effects on the CEO self-regulatory attributes. The unavailability of data related to target firms in our sample restricted us from exploring other target-related situational factors such as target performance that might influence the impact of CEO prevention focus. Also, since earnout is a contractual arrangement with the target firm, so it could lead to contractual enforcement issues and conflicts; hence it is indeed pertinent to look at long-term performance for the acquirer. Finally, future studies could also explore the impact of CEO psychological attributes on the structure of earnouts, mainly the terms of the contract and contract size (Barbopoulos and Adra, 2016). On the empirical front, we followed other studies (Gamache *et al.*, 2015; Kaplan, 2008) in using the letter to shareholder section presented in annual reports to capture CEO regulatory orientation. However, earnings conference call transcripts could also be an option because responses of CEOs during these such meetings are impromptu and could be better indicators of CEO characteristics (Malhotra *et al.*, 2018) and hence future studies could use such transcripts to capture CEO regulatory focus.

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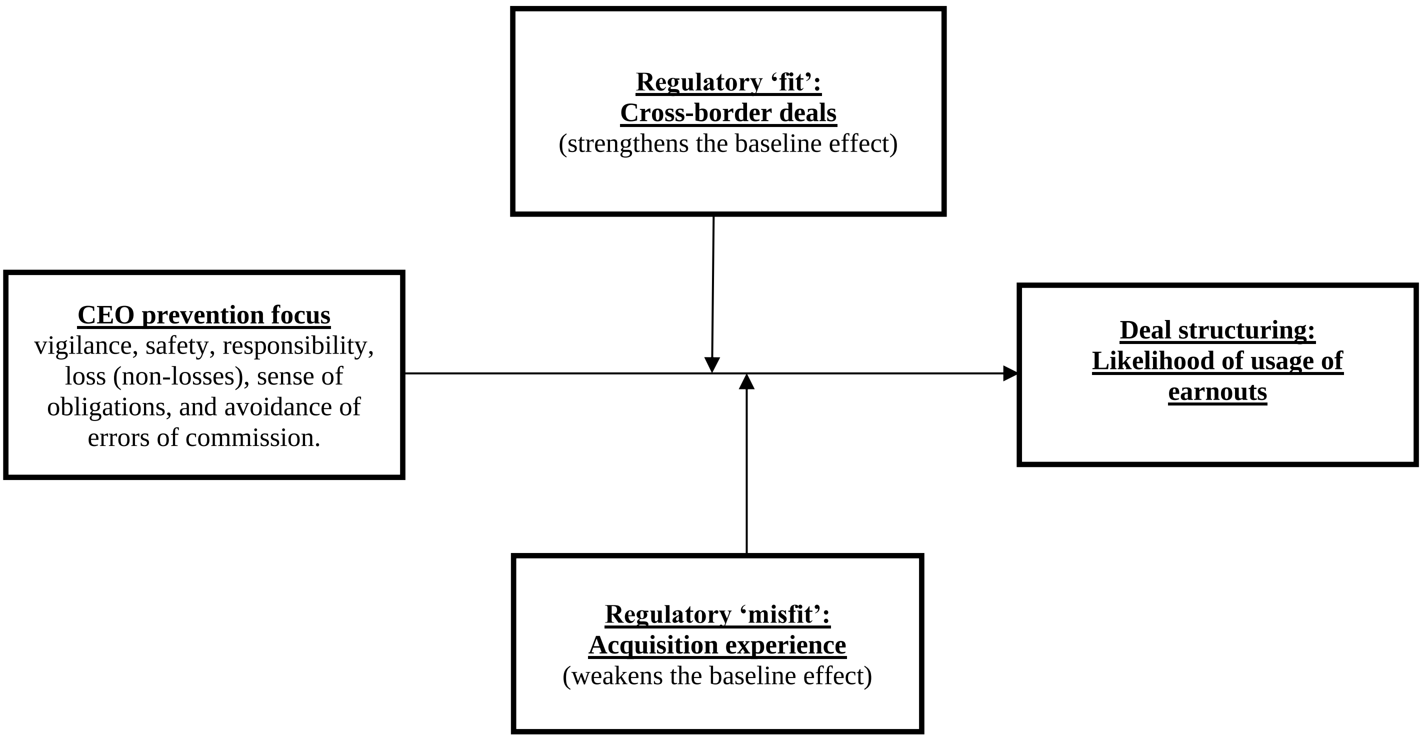

Figure 1. Conceptual model

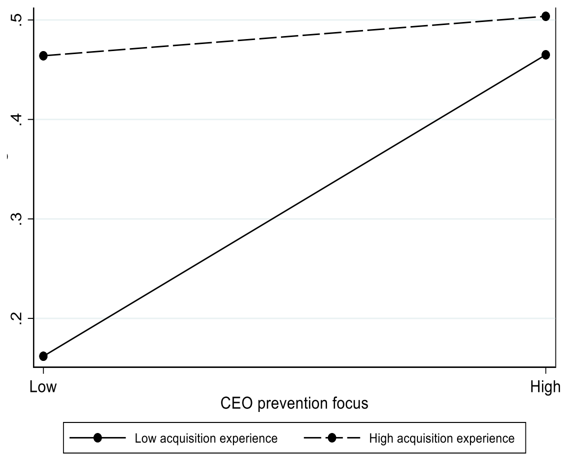

Figure 2. Interaction effect of acquisition experience on the relationship between CEO prevention focus and the likelihood of using earnouts (Table 2: Model 4).

Table 1
Descriptive statistics.

	Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
(1)	Earnouts	1											
(2)	CEO prevention focus	0.13+	1										
(3)	CEO promotion focus	-0.02	-0.08	1									
(4)	Cross-border	-0.13*	-0.05	0.14*	1								
(5)	Acquisition experience	0.12+	0.08	0.08	0.14*	1							
(6)	Equity control	0.07	0.13+	-0.05	-0.16	0.04	1						
(7)	Relative size	-0.1	-0.09	0.1	0.16*	0.13*	0.04	1					
(8)	Industry relatedness	0.006	-0.08	-0.01	-0.09	-0.09	0.12+	0.02	1				
(9)	Target high technology industry	0.08	0.05	0.08	0.04	0.1	0.06	0.01	0.01	1			
(10)	Financial leverage	-0.03	-0.07	-0.01	0.08	-0.28***	-0.01	-0.12+	0.08	0.06	1		
(11)	Price-to-earnings ratio	0.07	-0.05	-0.07	-0.05	0.03	0.03	-0.04	-0.09	-0.02	-0.003	1	
(12)	CEO age	0.02	-0.07	-0.25***	0.11+	0.2**	-0.05	0.02	-0.04	-0.09	-0.16*	-0.06	1
	Mean	0.38	0.64	2.62	0.49	6.24	97.71	0.09	0.57	0.35	0.98	32.09	51.03
	Std. Dev.	0.49	0.56	1	0.5	4.49	8.86	0.15	0.5	0.48	0.92	180.8	6.4
	Min	0	0.06	0.67	0	0	50.1	0.002	0	0	0.06	2.8	33
	Max	1	2.66	5.67	1	16	100	1	1	1	8.51	2792.21	76

Number of observations = 242, +p<0.1, *p<0.05, **p<0.01, ***p<0.001.

Table 2
Binary logit regression results for impact of CEO prevention focus intensity on likelihood of using earnouts.

	Dependent variable: Likelihood of using earnouts			
Variables	Model 1	Model 2	Model 3	Model 4
Equity control	0.017	0.011	0.004	-0.005
	(0.019)	(0.020)	(0.020)	(0.020)
Relative size	-2.084+	-1.985	-1.648	-1.846
	(1.226)	(1.227)	(1.264)	(1.232)
Industry relatedness	0.061	0.127	0.127	0.239
	(0.333)	(0.342)	(0.345)	(0.361)
Target high technology industry	0.354	0.384	0.313	0.419
	(0.368)	(0.377)	(0.385)	(0.402)
Financial leverage	-0.146	-0.105	-0.06	0.052
	(0.180)	(0.187)	(0.192)	(0.199)
Price-to-earnings ratio	0.001	0.002	0.002	0.002
	(0.002)	(0.001)	(0.002)	(0.002)
CEO age	0.006	0.014	0.022	0.007
	(0.025)	(0.026)	(0.027)	(0.029)
CEO promotion focus	-0.072	-0.059	-0.018	-0.008
	(0.165)	(0.171)	(0.175)	(0.179)
H1: CEO prevention focus		0.906**	0.921*	1.859**
		(0.301)	(0.408)	(0.577)
Cross-border			-0.672	-0.726
			(0.511)	(0.532)
H2: CEO prevention focus × Cross-border			-0.037	0.071
			(0.573)	(0.596)
Acquisition experience				0.213**
				(0.066)
H3: CEO prevention focus × Acquisition experience				-0.160*
				(0.073)
Constant	-2.349	-2.912	-2.632	-2.313
	(2.610)	(2.692)	(2.767)	(2.775)
Year dummies	Yes	Yes	Yes	Yes
Industry dummies	Yes	Yes	Yes	Yes
Observations	242	242	242	242
Pseudo R^2	0.092	0.123	0.136	0.172
Log-likelihood	-146.346	-141.436	-139.306	-133.439
Log-likelihood chi-square	29.714	39.535	43.795	55.529

Note: Unstandardized coefficients are reported. Standard errors are reported in parentheses. +p<0.1, *p<0.05, **p<0.01, ***p<0.001.

APPENDIX

Regulatory focus words				
Prevention focus words	**Prevention focus words**	**Promotion focus words**	**Promotion focus words**	**Promotion focus words**
Accuracy	Fearing	Accomplish	Gaining	Promoted
Afraid	Feared	Accomplishes	Gained	Speed
Carefully	Loss	Accomplishing	Grow	Speeding
Anxious	Obligation	Accomplished	Grows	Sped
Avoid	Ought	Achieve	Growing	Swift
Avoids	Pain	Achieves	Grown	Toward
Avoiding	Pains	Achieving	Hope	Velocity
Avoided	Paining	Achieved	Hopes	Wish
Conservative	Pained	Advancement	Hoping	Wishes
Defend	Prevent	Aspiration	Hoped	Whishing
Defends	Prevents	Aspire	Ideal	Wished
Defending	Preventing	Aspires	Improve	
Defended	Prevented	Aspiring	Improves	
Duty	Protect	Aspired	Improving	
Escape	Protects	Desire	Improved	
Escapes	Protecting	Desires	Momentum	
Escaping	Protected	Desiring	Obtain	
Escaped	Responsible	Desired	Obtains	
Evade	Risk	Earn	Obtaining	
Evades	Risks	Earns	Obtained	
Evading	Risking	Earning	Optimistic	
Evaded	Risked	Earned	Progress	
Fail	Safety	Expand	Progresses	
Fails	Security	Expands	Progressing	
Failing	Threat	Expanding	Progressed	
Failed	Vigilance	Expanded	Promote	
Fear		Gain	Promotes	
Fears		Gains	Promoting	

Note: The prevention and promotion foci words are adapted from Gamache *et al.*, (2015), who developed and validated the dictionary of 25 prevention focus words and 27 promotion focus words and their alternative tenses to capture CEO prevention and promotion foci. Thus, we also used 25 prevention focus words and 27 promotion focus words and their alternative tenses to measure CEO prevention and promotion foci scores.