

RGC Ref. No.: <u>UGC/FDS15/B02/16</u> (please insert ref. above)
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**RESEARCH GRANTS COUNCIL  
COMPETITIVE RESEARCH FUNDING SCHEMES FOR  
THE LOCAL SELF-FINANCING DEGREE SECTOR**

**FACULTY DEVELOPMENT SCHEME (FDS)**

**Completion Report**  
(for completed projects only)

<p><b><u>Submission Deadlines:</u></b></p> <ol style="list-style-type: none"> <li>1. Auditor's report with unspent balance, if any: within <b>six</b> months of the approved project completion date.</li> <li>2. Completion report: within <b>12</b> months of the approved project completion date.</li> </ol>
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**Part A: The Project and Investigator(s)**

**1. Project Title**

Are Asset Impairment and Earnings Management for Tunneling? Evidence from  
Connected Transactions in Hong Kong

**2. Investigator(s) and Academic Department(s) / Unit(s) Involved**

Research Team	Name / Post	Unit / Department / Institution
Principal Investigator	LEE, Hua/Associate Professor	Department of Accounting/ Hong Kong Shue Yan University
Co-Investigator(s)	N.A.	
Others	N.A.	

**3. Project Duration**

	Original	Revised	Date of RGC / Institution Approval (must be quoted)
Project Start Date	1/1/2017	N.A.	N.A.
Project Completion Date	31/12/2018	30/6/2019	12/12/2018
Duration (in month)	24	30	12/12/2018
Deadline for Submission of Completion Report	31/12/2019	30/6/2020	12/12/2018

## **Part B: The Final Report**

### **5. Project Objectives**

#### 5.1 Objectives as per original application

1. To investigate the association between asset write-downs and asset-sales transactions prior to the related party transactions.
2. To investigate the association between asset write-downs and asset-acquisition transactions subsequent to the transactions.
3. To examine the association between controlling shareholders' entrenchment effect and the asset write-downs.
4. To examine the association between sales price and asset write-downs prior to the asset sales transactions with related parties.
5. To examine the association between acquisition price and asset write-downs subsequent to asset acquisition transactions with related parties.
6. To investigate the association between asset write-downs and accrual earnings management in firms with forthcoming asset sales transactions and in firms with prior asset acquisition transactions with related parties.
7. To investigate the association between asset write-downs and real earnings management in firms with forthcoming asset sales transactions and in firms with prior asset acquisition transactions with related parties.

#### 5.2 Revised objectives

Date of approval from the RGC: N.A.

Reasons for the change: N.A.

### 5.3 Realisation of the objectives

*(Maximum 1 page; please state how and to what extent the project objectives have been achieved; give reasons for under-achievements and outline attempts to overcome problems, if any)*

As some companies' annual reports provide unclear and/or complex contents, PI has contacted a company selling some of the data but was replied its data on specific items in a specific region (Hong Kong) were not separately sold. Data were sold on a batch basis in all regions, which resulted in a high quoted price that was unaffordable by using the unspent balance. Nevertheless, hand collected numerical data on notifiable and connected transactions and ownership structure were reviewed and checked for correctness through browsing companies' annual reports one-by-one. This data combined with other financial data acquired from Taiwan Economic Journal were used to form samples. The asset write-down model and transaction price model were estimated based on the formed samples and results were obtained to test the hypotheses on the associations among asset write-down, asset-transfer transactions, and entrenchment effect for Objectives 1-3, the associations between transaction prices and asset impairments for Objectives 4-5, and the associations between asset write-downs and accrual earnings management and real earnings management for Objectives 6-7.

### 5.4 Summary of objectives addressed to date

<b>Objectives</b> <i>(as per 5.1/5.2 above)</i>	<b>Addressed</b> <i>(please tick)</i>	<b>Percentage Achieved</b> <i>(please estimate)</i>
1. To investigate the association between asset write-downs and asset-sales transactions prior to the related party transactions	✓	100%
2. To investigate the association between asset write-downs and asset-acquisition transactions subsequent to the transactions	✓	100%
3. To examine the association between controlling shareholders' entrenchment effect and the asset write-downs.	✓	100%
4. To examine the association between sales price and asset write-downs prior to the asset sales transactions with related parties.	✓	100%
5. To examine the association between acquisition price and asset write-downs subsequent to asset acquisition transactions with related parties.	✓	100%

6. To investigate the association between asset write-downs and accrual earnings management in firms with forthcoming asset sales transactions and in firms with prior asset acquisition transactions with related parties.	✓	100%
7. To investigate the association between asset write-downs and real earnings management in firms with forthcoming asset sales transactions and in firms with prior asset acquisition transactions with related parties.	✓	100%

## 6. Research Outcome

### 6.1 Major findings and research outcome

*(Maximum 1 page; please make reference to Part C where necessary)*

1. Firms recognize less asset write-down prior to the asset-sales related party transactions, but more when cash flow rights and control rights are more diverged.
2. Firms recognize more asset write-down subsequent the asset-acquisition related party transactions, but this relation is weakened when cash flow rights and control rights are more diverged.
3. The amount of asset write-down loss prior to (subsequent) the asset-sales (asset-acquisition) related party transactions is greater (smaller) for firms with more divergence than for firms with less divergence between cash flow rights and control rights.
4. The selling price varies negatively with the amount of asset write-down. The lower selling price for asset-sales related party transactions is further reduced for firms with more divergence than firms with less divergence.
5. The acquisition price varies positively with the amount of asset write-down. The higher acquisition price for asset-acquisition related party transactions is further increased for firms with more divergence than firms with less divergence.
6. Firms with current or forthcoming asset-sales related-party transactions and firms with more asset write-downs engage in downward earnings management, whereas firms with current or prior asset-acquisition related-party engage in upward accrual earnings management.
7. Firms with asset-sales related-party transactions engage in downward real activities earnings manipulation from discretionary expenditures and production costs, while firms with asset-acquisition related-party transactions engage in real activities earnings manipulation from sales activities and discretionary expenditures.

6.2 Potential for further development of the research and the proposed course of action  
(Maximum half a page)

The evidence of this project suggests the importance of the asset write-down and earnings management strategies for firms with asset-transfer connected transactions. Future research may explore the causes and consequences of other form of connected transactions that controlling shareholders may use to expropriate wealth from minority shareholders.

**7. Layman's Summary**

(Describe in layman's language the nature, significance and value of the research project, in no more than 200 words)

Tunneling occurs when controlling shareholders expropriate wealth from minority shareholders, whereby connected transactions provide a channel to achieve this purpose. This project explores whether firms with asset-transfer transactions with connected parties recognize asset write-downs to affect the transaction price, and as a consequence, whether these firms manage contemporaneous earnings management. The results show the associations among asset write-downs, transaction price of the connected transactions, and the divergence between cash flow rights and control rights. Additionally, firms with asset-transfer connected transactions engage in earnings management using accruals and/or real activities. The evidence suggests that controlling shareholders play a role in the asset-transfer connected transactions and provides policy implication for the mandatory disclosure of connected parties and connected transactions.

**Part C: Research Output****8. Peer-Reviewed Journal Publication(s) Arising Directly From This Research Project**

*(Please attach a copy of the publication and/or the letter of acceptance if not yet submitted in the previous progress report(s). All listed publications must acknowledge RGC's funding support by quoting the specific grant reference.)*

The Latest Status of Publications				Author(s) (denote the corresponding author with an asterisk*)	Title and Journal / Book (with the volume, pages and other necessary publishing details specified)	Submitted to RGC (indicate the year ending of the relevant progress report)	Attached to this Report (Yes or No)	Acknowledged the Support of RGC (Yes or No)	Accessible from the Institutional Repository (Yes or No)
Year of Publication	Year of Acceptance (For paper accepted but not yet published)	Under Review	Under Preparation (optional)						
N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	No	No	No*

\* Will be accessible from the Institutional Repository after the manuscripts are published at journals

**9. Recognized International Conference(s) In Which Paper(s) Related To This Research Project Was / Were Delivered**

*(Please attach a copy of each conference abstract)*

Month / Year / Place	Title	Conference Name	Submitted to RGC (indicate the year ending of the relevant progress report)	Attached to this Report (Yes or No)	Acknowledged the Support of RGC (Yes or No)	Accessible from the Institutional Repository (Yes or No)
5/2018 Baltimore, USA	Asset impairments and tunneling transactions in an emerging market	American Accounting Association 2018 Mid-Atlantic Region Meeting	N.A.	Yes ( <u>Appendix 1</u> )	Yes	No
6/2019 Zagreb, Croatia	Asset write-downs for tunneling and earnings management in an emerging market	2019 Global Finance Conference	N.A.	Yes ( <u>Appendix 2</u> )	Yes	No

**10. Whether Research Experience And New Knowledge Has Been Transferred / Has Contributed To Teaching And Learning**

*(Please elaborate)*

This project strengthens PI's application of knowledge to practical use that can be introduced to students in classroom teaching. Additionally, it allows PI to instruct student helpers to integrate what they have learned from intermediate accounting and finance to real world cases as shown in companies' annual reports.

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**11. Student(s) Trained**

*(Please attach a copy of the title page of the thesis)*

Name	Degree Registered for	Date of Registration	Date of Thesis Submission / Graduation
N.A.	N.A.	N.A.	N.A.

**12. Other Impact**

*(e.g. award of patents or prizes, collaboration with other research institutions, technology transfer, teaching enhancement, etc.)*

N.A.

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**13. Statistics on Research Outputs**

No. of outputs arising directly from this research project	Peer-reviewed Journal Publications	Conference Papers	Scholarly Books, Monographs and Chapters	Patents Awarded	Other Research Outputs (please specify)	
					Type	No.
N.A.	N.A.	2	N.A.	N.A.	N.A.	N.A.

**14. Public Access Of Completion Report**

*(Please specify the information, if any, that cannot be provided for public access and give the reasons.)*

<b>Information that Cannot Be Provided for Public Access</b>	<b>Reasons</b>
N/A	N/A