

RGC Ref. No.: UGC/FDS16/B03/15 _____ (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><u>Submission Deadlines:</u></p> <ol style="list-style-type: none"> 1. Auditor's report with unspent balance, if any: within six months of the approved project completion date. 2. Completion report: within 12 months of the approved project completion date.
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Part A: The Project and Investigator(s)

1. Project Title

CEO compensation and dividend policy in family firms

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

Research Team	Name / Post	Unit / Department / Institution
Principal Investigator	HUNG Hie Yiin / Senior Lecturer	Lee Shau Kee School of Business and Administration, The Open University of Hong Kong
Co-Investigator(s)	ADITHIPYANGKUL Pattarin / Lecturer	School of Accounting, Curtin University
Others		

3. Project Duration

	Original	Revised	Date of RGC / Institution Approval (must be quoted)
Project Start Date	1 January 2016	NA	29 October 2015
Project Completion Date	31 December 2018	NA	
Duration (in month)	36	NA	
Deadline for Submission of Completion Report	31 December 2019	NA	

Part B: The Final Report

5. Project Objectives

5.1 Objectives as per original application

1. Examine the impacts of family firms on dividend policy
2. Examine the differences in CEO compensation for CEOs working in family and non-family firms and for family-related and hired CEOs
3. Examine whether family-owners use CEO compensation and dividend policy as alternative tunneling tools

5.2 Revised objectives

Date of approval from the RGC: NA

Reasons for the change:

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)

The objectives of the project are achieved through two research outputs. One of the research outputs, a working paper, is currently under review of an indexed journal “Advances in Accounting”, and the other working paper has been submitted to a conference in January 2020 for presentation consideration.

The first working paper achieved the first two objectives by studying the direct and interactive moderating effects of two governance tools, CEO incentive pay and dividend policy on audit pricing and family firms. We found that dividend payouts of family firms do not have significant direct effect on audit fees but CEO incentive pay has a direct negative effect on audit fees. However, when we include the heterogeneity of family firms, we found that the level of family ownership positively (negatively) moderated the relationship between audit fee and dividend payouts (executive incentive pay). This implies auditors:

- (a) are more likely to view dividend payouts as an expropriation tool in firms with higher family ownership and this impact is weakened when we include other moderating variables such as family involvement in management and board of directors.
- (b) are less likely to view executive incentive pay as misappropriation when family ownership increases. In this sense, executive incentive pay in family firms is considered a good governance tool. However, the level of family management (i.e., family CEOs and directors) positively moderate the relationship between audit fee and executive incentive pay.

The second working paper works on the interactive effect of dividend payouts and CEO total compensative in family firms as well as whether family owners make use of these two variables as alternative tool to tunnel firm resources. We find significant differences in CEO compensation and dividend payout between family and non-family firms and family firms led by family-related CEOs and hired CEOs. Our results provide evidence that family owners make use of CEO compensation and dividend policy to engage in tunneling activities. This research output covered all the three objectives.

The major difficulty we encounter in doing this project is data-collection. Our project requires hand-collection of most data – CEO compensation, audit fees, family ownership, Board size, family representation on the board of directors etc. Majority of data can be hand-collected from annual reports which is time-consuming but manageable. The most difficult part is the level of family ownership which needs to be collected by searching the Hong Kong Stock Exchange (HKEx) website on individual firm basis. As family ownership may change over time, we need to cross-check the records of each firm for every year. The level of difficulty increases when some firms changed name or industry coding. We realize this fact rather late and by the time we get ready the data for analysis, the data becomes outdated. We spend much time in the last 12 months updating the sample data of our second research paper so as to increase the chance of getting it accepted and published by an indexed journal in future months.

5.4 Summary of objectives addressed to date

Objectives <i>(as per 5.1/5.2 above)</i>	Addressed <i>(please tick)</i>	Percentage Achieved <i>(please estimate)</i>
1. Examine the impacts of family firms on dividend policy	√	100%
2. Examine the differences in CEO compensation for CEOs working in family and non-family firms and for family-related and hired CEOs	√	100%
3. Examine whether family-owners use CEO compensation and dividend policy as alternative tunneling tools	√	100%

6. Research Outcome

6.1 Major findings and research outcome

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

Using mostly hand-collected data from the largest 150 listed Hong Kong companies from 2011 to 2013, this project investigates the impacts of executive incentive pay and dividend payouts on audit pricing in family firms. Our analyses suggest that the tendency for an auditor to perceive CEO incentive pay or dividend payouts as being used to reduce agency costs is affected by the nature and degree of family involvement in business. We consider three ways in which family shareholders can get involved in their businesses and influence corporate decisions – ownership, management, and board governance. We find that in non-family firms and in family firms with non-family member CEOs, auditors appear to view the use of CEO incentive pay positively as a tool to reduce agency costs (and hence charge lower audit fees for firms with greater CEO incentive pay). The fee-discounting effect is stronger as family ownership increases. However, high incentive pay awarded to a family-member CEO appears to be viewed as a tool for private benefit extraction, resulting in a higher audit fee. As for dividend payouts, while audit fees are not significantly associated with dividend payouts in non-family firms, audit fees decrease as dividend payouts increase in family firms. This suggests that auditors tend to be neutral towards dividend payouts in non-family firms, but they perceive dividend payouts positively as a tool to mitigate agency problems in family firms. The fee-discounting effect is stronger in family firms with greater family representation in boards of directors and in family firms with family-member CEOs.

6.2 Potential for further development of the research and the proposed course of action

(Maximum half a page)

Our examination of the moderating effects of family ownership does not consider the share structure because, in Hong Kong, dual-class share structure is not allowed until after April 30, 2018. Future research can investigate the impacts of dual-class share structure (the control-ownership wedge) on audit pricing. In addition, the analyses in this project are limited to only two governance tools, i.e., CEO incentive pay and dividend payouts. Future studies can investigate the impacts of other governance tools such as board composition. Finally, being interested in an auditor's view, we follow the tradition in the auditing literature and adopt agency theory as our theoretical framework to investigate the merits of governance tools. We acknowledge that there are other theoretical frameworks adopted in previous family business studies, such as resource dependence theory and the socioemotional wealth perspective (Chua

et al, 2012). Future research may investigate the merits of governance tools from other theoretical frameworks.

7. Layman's Summary

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

Agency theorists recommend the use of executive incentive pay and dividend payouts as governance mechanisms to alleviate principal-agent agency problems in widely-held firms. In family firms, however, principal-principal agency problems prevail, and the controlling shareholders can instead use executive incentive pay and dividend payouts to maximize their own private benefits. This research investigates the merits of executive incentives and dividend payouts from an auditor's perspective, as reflected through audit pricing. Our analyses show that the nature and degree of family involvement in business affect the audit fee premiums or discounts associated with CEO incentives and dividend payouts. The audit fee discounts associated with CEO incentives tend to be larger in a firm with higher family ownership and less family involvement in management. In a firm with high family involvement in management (i.e., with a family-member CEO), CEO incentives may instead create an audit fee premium. Also, the audit fee discounts associated with dividend payouts tend to be larger in a firm with higher family involvement in management and board governance. Our findings suggest that auditors consider family firm heterogeneity when they evaluate the merits of incentive pay and dividend payouts in family firms.

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)						
		Yes		Pattarin Adithipyan gkul, H.Y. Hung* and T. Y. Leung	Executive Incentive Pay and Dividend Payouts in Family Firms: An Auditor's Perspective / <i>Advances in Accounting</i>	No	Yes	Yes	Yes

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)
October/ 2018/ Malaysia	Executive Incentive Pay and Dividend Payouts in Family Firms: An Auditor's Perspective	3 rd Applied International Business Conference 2018	No	Yes	Yes	Yes
27-29 March 2020, UK	CEO Compensation and Dividend Policy in Family Firms: Hong Kong Evidence	2nd International Conference on Research in Business, Management and Finance	No	Yes	Yes	Yes

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

(Please elaborate)

This project contributes to the corporate governance and family business literature by providing new evidence from an auditor's perspective on the merits of executive incentive pay and dividend payouts in family firms. Hence, the findings of this project should be relevant to the courses corporate governance and advanced courses in auditing and financial reporting as well as the policy makers in setting the monitoring/disclosure level of the listed firms.

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
NA			

12. Other Impact

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

NA

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.
	1 (paper is under review of <i>Advances in Accounting</i>)	2	0	0	NA	0

14. Public Access Of Completion Report

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

Information that Cannot Be Provided for Public Access	Reasons
NA	