

Research Assessment Exercise 2020

Impact Case Study

University: The Hong Kong Polytechnic University |

Unit of Assessment (UoA): Accountancy (UoA20) |

Title of case study: Information Dynamics in Contracting

(1) Summary of the impact

Disclosure can help mitigate information asymmetry problems, which in turn facilitates contracting. For this case study, we highlight the research of three faculty members, Prof. Walid Saffar, Prof. Jeffrey Ng and Dr Liangliang Jiang. They are active in disseminating their research to non-academics through writing short practitioner-targeted articles based on their research. Their work has been cited in books and by the media. Standard setters have considered their work to be impactful in policy-making. Impact has also been achieved through active engagement in knowledge transfer with different practitioners at different forums, including via webcast and YouTube. |

(2) Underpinning research

Prof. Saffar is our School's most multidisciplinary faculty member, as evidenced by the diversity in his publications. He has published several papers on the role of information in various settings. In [R1], using a sample of 15,174 firms from 24 countries which participated in the 2009 World Bank Enterprise Survey, he investigates the impact of disclosure standards and auditing infrastructure on the practice of bribing public officials to secure government contracts. He finds that firms are less likely to offer gifts to secure a government contract in countries with more extensive financial reporting requirements and in those where audit firms have higher litigation and sanction risk. His findings also show that firms are less likely to bribe bureaucrats when their financial statements are reviewed by external audit firms.

In [R2], Prof. Saffar extends recent research on the links between political connections and financial reporting by examining the role of auditor choice. His evidence that public firms with political connections are more likely to appoint a Big 4 auditor, supports the intuition that insiders in these firms are eager to improve accounting transparency to convince outside investors that they do not exploit their connections to divert corporate resources. He also reports that firms connected with Big 4 auditors exhibit less earnings management and enjoy greater transparency, higher valuations, and cheaper equity financing.

In [R3], Prof. Saffar finds that a firm's CSR engagement increases in areas where such engagement is dense and when the firm is located near a large city. In such areas, peers, labor unions, the news media, universities, and community organizations tend to be concentrated in large cities, and transmit their norms, values, and knowledge related to CSR to firms via face-to-face meetings and frequent social interactions. His findings further highlight that CSR engagement reduces equity financing costs for firms in areas where CSR is widely practiced.

Prof. Ng is active in research on the role of information in corporate governance. In [R4], he builds on the recent literature on corruption in bank lending. He examines the effect of country-level timely loan loss recognition by banks on lending corruption using a unique World Bank dataset of more than 3,600 firms across 44 countries. He finds evidence consistent with the notion that timely loan loss recognition constrains lending corruption because it increases the likelihood of problem loans being uncovered earlier.

[R5] examines how board co-option, defined as the fraction of the board made up of directors appointed after the CEO assumed office, is related to clawback adoption. He finds that co-opted boards have a lower probability of adopting a clawback provision. He also finds that board co-option is an important mechanism through which longer-tenure CEOs reduce the likelihood of clawback adoption.

In [R6], Dr Jiang investigates the role of audit verification in the resolution process following debt covenant violations. She finds that covenant violations result in a demand for differentially higher levels of audit verification. Overall, her research suggests that covenant violations increase the demand for audit services to help control post-violation contracting costs. |

(3) References to the research

[R1] “Disclosure Standards, Auditing Infrastructure, and Bribery Mitigation”. Samer Khalil, **Walid Saffar**, and Samir Trabelsi, *Journal of Business Ethics* 132, (2015), 379-399.

[R2] “Auditor Choice in Politically Connected Firms” with Omrane Guedhami, Jeffrey Pittman, and **Walid Saffar**. *Journal of Accounting Research* 52, (2014), 107-162.

[R3] “Near and Dear? The Role of Location in CSR Engagement”. Bryan Husted and Dima Jamali, and **Walid Saffar**. *Strategic Management Journal* 37, (2016), 2050-2070.

[R4] “Corruption in bank lending: The role of timely loan loss recognition”. Brian Akins, Yiwei Dou, and **Jeffrey Ng**. *Journal of Accounting and Economics*, 63 (2–3), (2017), 454-478.

[R5] “Not clawing the hand that feeds you: The case of co-opted boards and clawbacks”. Sterling Huang, Chee Yeow Lim, and **Jeffrey Ng**. *European Accounting Review*, 28 (1), (2019), 101-127.

[R6] “The role of audit verification in debt contracting: Evidence from covenant violations”. **Liangliang Jiang** and Hui Zhou. *Review of Accounting Studies*, 22, (2017), 469-501. |

(4) Details of the impact

One of Prof. Saffar’s many research interests is corruption, which is an important problem faced by many societies today. Prof. Saffar’s research has been discussed in several books targeted at practitioners. In *Open Data Exposed* - a book that supports open data practitioners in their endeavors to promote open data implementation and research [S1; p. 72], [R1] was depicted as providing evidence that “open data can have a positive effect on detecting and combatting corruption, especially in developing countries”. [R1] was also mentioned in another book entitled *Corruption, Social Sciences and the Law: Exploration across the Disciplines* [S2] in a discussion of disclosure as a practical anti-corruption step.

[R2] was mentioned in “The China Business Model: Originality and Limits”, which aims to examine the development and transformation of the Chinese business model and helps practitioners to have a better understanding of the business world in China [S3]. Page 57 reads: “Another study examined auditor choice (Guedhami, Pittman, & Saffar, 2014). Public firms with political connections are more likely to appoint a Big Four auditor, for the purpose of improving accounting transparency to outside investors.”

Prof. Saffar’s work on CSR in [R3] has also received significant attention in the active debate about the perspective of firm stakeholder value, as opposed to the shareholder value perspective. Simply stated, according to the stakeholder value perspective, the firm has a responsibility to all stakeholders (including shareholders), who might have conflicts of interest. Moreover, his work has been discussed in books such as [S4] and [S5] that try to improve awareness of the importance of CSR as part of the corporate strategy. For example, [S5], a handbook on international corporate and public affairs intended for practitioners and students of global corporate and public affairs, states that it contains

contributions from thirty global-thought leading scholars in the field today to serve the needs of professionals and students.

Prof. Ng's primary research involves many issues related to loan loss reserves. His work has also reached beyond academia. For example, his research has been recently cited by the European Systemic Risk Board (ESRB), an independent body of the EU and part of the European System of Financial Supervision (ESFS) that is hosted and supported by the European Central Bank. Page 74 of its 2017 report entitled "Financial stability implications of IFRS 9" discusses Prof. Ng's research as follows: "The amount of loan loss allowances included in Tier 2 regulatory capital is positively associated with the risk of bank failures during the 2007 financial crisis (Ng and Roychowdhury (2014)). Failing banks that recognise additional provisions may have to engage in excessively risky activities in a sort of 'bid for resurrection'. To provide further evidence of Prof. Ng's research impact on policy-making, some excerpts from an email by Rebecca Villmann, who is a director at Financial Reporting & Assurance Standards Canada [S6], are given below:

- i) "With the recent release and application of the new loan loss provision requirements, research across jurisdictions into how those forward-looking judgements were made and explained could provide insights on whether there is more relevant and timely reporting of credit impairments."
- ii) "There are several issues in accounting that are never settled. Whether goodwill should be amortized is one of those and it is being debated again. The IASB has a project on Goodwill and Impairment and will be issuing a discussion paper in Q4 of this year. Understanding the effects of such decisions is important. I will share paper with the Canadian Board staff team to consider. I encourage you and the authors to respond to their request for comment."

Prof. Ng actively shares his research with practitioners, typically in a form that is catered to their needs. For example, [R4] was converted into a practitioner-targeted article entitled "How Speedy Loan-Loss Recognition Can Save Banks Billions", which was disseminated on September 4, 2018, via *Rice Business Wisdom* [S7] whose mission is to get ideas from academic researchers to the general public. As for another example, in collaboration with Dr Jennifer Cronin (President of Wharf Hotels) and Prof. Michael Hui (Professor of Marketing at CUHK), Prof. Ng presented insights from research and practice at the "Cultural Influences on Business" symposium held on May 28, 2018 by the Caritas Institute of Management. In particular, using insights from [R4], he discussed how corruption is a significant problem in many countries and how timely loan loss recognition could be one solution to it.

The final example is in his speech entitled "Accounting is not just about numbers, it affects real decision-making too – Insights from the case of banks", in which he shared his insights from [R4] at a Knowledge Transfer Forum "Star Professors x Top Business Management" held at PolyU on December 13-14, 2018 [S7]. Distinguished speakers including Professor Mark Grinblatt (UCLA Anderson School of Management), Professor Shiva Rajgopal (Columbia Business School) and Professor Karthik Ramanna (University of Oxford's Blavatnik School of Government) shared their research insights with around 150 on-site participants. Attendees included industry partners from leading companies e.g. Haitong International Securities Group, China Minsheng Fin, Grand Cartel Securities Company, Finet Group, Shenzhen Investment Limited, China Resources, ABC International, CCT Technology Holdings Limited, China Life (Overseas), and China Taiping. The event was also streamed online and reached over 100,000 real-time audience via live streaming (WIND Financials terminals) and attracted over 70,000 views via Tencent Inews over the two-day event.

[R5] is another indication of the practitioner-relevance of his work, which has been featured in the Harvard Law School Forum on Corporate Governance and Financial Regulation, a blog serving as a forum for debate and the exchange of ideas among lawyers, executives, institutional investors, academics, and regulators [S8]. Practitioners have also discussed Prof. Ng's work. For example,

Winston & Strawn LLP, an international law firm with nearly 1,000 attorneys in 16 offices in the United States, Europe, Asia, and the Middle East, produces a weekly publication *Financial Services Update* which covers news pertinent to the financial services industry and provides a summary analysis of developments at the SEC, CFTC, OCC, and self-regulatory organizations. In one issue, a feature article on corporate governance discusses Prof. Ng's findings in [R5] that co-opted boards are less likely to use clawbacks if there is a higher likelihood that the boards will have to act against the CEO in the future by enforcing clawback provisions [S9].

Finally, Prof. Saffar and Dr Jiang have worked together to create impact on accounting practice. In a joint impact case study presentation entitled "Information Dynamics and Contracting" [S10], they shared their findings in [R1-R3] and [R6] at the China Accounting and Finance Research Knowledge Transfer Forum held in Hong Kong on September 20, 2019 and in Dongguan on September 21, 2019. The objective of this forum was to provide a forum for academics and practitioners to engage in an exchange of ideas that create impact for industry and society. Impact case studies and practice-based theses were presented, followed by a corporate visit to Huawei in Shenzhen. This event attracted more than a hundred participants, including Mr Andrew Fung, CFO of Henderson Land Development Company Ltd, and Dr Ricky Szeto, General Manager and Executive Director of Hung Fook Tong Group Holdings Ltd. A survey conducted after the forum indicated that the participants were satisfied with what they learnt through the forum and they commented that the materials discussed in the forum were very well-grounded and effectively delivered with the down-to-earth language, and were useful in understanding the latest research on multiple disciplines related to accounting and finance. |

(5) Sources to corroborate the impact

[S1] van Loenen, B., Vancauwenberghe, G., & Cromptvoets, J. (2018). *Open Data Exposed*. The Hague: T.M.C. Asser Press.

[S2] Ellis, J. (2019). *Corruption, Social Sciences and the Law: Exploration across the disciplines*. Abingdon, Oxfordshire: Routledge.

[S3] Paulet, E., & Rowley, C. (2017). *The China Business Model: Originality and Limits*. Sawston, Cambridge: Chandos Publishing.

[S4] Crane, A., Matten, D., Glozer, S., & Spence, L. (2019). *Business Ethics: Managing Corporate Citizenship and Sustainability in the Age of Globalization*. 5th Edition. Oxford University Press.

[S5] Harris, P., & Fleisher, C.S. (2017). *The SAGE Handbook of International Corporate and Public Affairs*. SAGE Publications Ltd.

[S6] Email entitled "Impact of Research" from Rebecca Villmann on September 4, 2019.

[S7] Knowledge Transfer Forum, December 13-14, 2018. Knowledge transfer presentation "Accounting is not just about numbers, it affects real decision making too – insights from the case of banks". YouTube video clip:

https://www.youtube.com/playlist?list=PLVJECmUfEOSH0HCwF0hEcoP_QZeeHZKj-

[S8] "Not Clawing the Hand that Feeds You". Harvard Law School Forum on Corporate Governance and Financial Regulation. <https://corpgov.law.harvard.edu/2015/03/03/not-clawing-the-hand-that-feeds-you/>

[S9] "Feature: Corporate Governance". Winston & Strawn LLP's 2015 Financial Services Update Volume 10, No.11. <https://www.winston.com/images/content/9/4/v2/94762/Fin-Serv-Volume-10-No.-11.html#winstonpubs>

[S10] China Accounting and Finance Research Knowledge Transfer Forum, September 20-21, 2019. Impact case study presentation "Information Dynamics and Contracting". YouTube video clip: <https://www.youtube.com/watch?v=FtWIMcXdPMs&feature=youtu.be.>