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Family Firms, Directors' Remuneration, Expropriation and Firm Value: Evidence of the Role of Independent Directors' Tenure within the Remuneration Committee in Malaysia

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Research Highlights

- This manuscript is about the influence of directors' remuneration on firm performance and whether independent directors' tenure in the remuneration committee moderates this relationship.
- The results show that within family corporations in industries which are not exclusive, non-executive directors' remuneration have a significant negative relationship with firm performance.
- Family firms have a stronger significant negative relationship than non-family firms.
- Within family firms in non-exclusive industries, there is also a positive moderating effect of independent directors' tenure within the remuneration committee on the influence of non-executive directors' remuneration on firm performance.
- In this case, corporations owned by families have a stronger positive moderating effect compared to non-family firms.

Research Objectives

This research explores a relatively unexplored issue of expropriation i.e. how directors' remuneration influence firm value. Secondly, it shows how independent directors' tenure within the remuneration committee moderate the influence of directors' remuneration on the performance of the corporation. The lessons from this research can serve as a good corporate governance reference for other emerging markets in East Asia which share the same structural characteristic of highly concentrated ownership and predominantly family-owned as well as encountering the same potential Agency Type II problems. As such, our research can also enhance the understanding of corporate finance in emerging markets which possess such structural characteristics and problems.

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Methodology

Panel data is used in this research. Specifically, the Fixed Effects Model (FEM) is used because the FEM can reduce effectively the endogeneity problem of unobserved heterogeneity which is time invariant (Chi, 2005).

Results

The results show that within family corporations in industries which are not exclusive, non-executive directors' remuneration have a significant negative relationship with firm performance. Family firms have a stronger significant negative relationship than non-family firms. Within family firms in non-exclusive industries, there is also a positive moderating effect of independent directors' tenure within the remuneration committee on the influence of non-executive directors' remuneration on firm performance. In this case, corporations owned by families have a stronger positive moderating effect compared to non-family firms.

Findings

For family firms in non-exclusive industries, longer tenure of independent directors within the remuneration committee can significantly help mitigate the firm value effects of independent directors' compensation which is negative and this mitigation is higher in firms controlled by families compared to firms controlled by non-families within the context of a developing country. When independent directors within the remuneration committee receive higher non-executive directors' remuneration and simultaneously serve longer, they become more incentivized to reduce their conflict of interests with other investors as well as more motivated to perform their duties better. This significantly help mitigate the negative firm value effects of the compensation of independent directors. Conversely, for family firms in exclusive industries; longer tenure of independent directors within the remuneration committee together with their higher non-executive directors' remuneration also increase firm value due to the same reasons discussed previously. However, there is no significant mitigation of negative firm value effects of non-executive directors' remuneration. One possible explanation for this occurrence is that controlling shareholders are not motivated to

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divert resources from these firms through non-executive directors' remuneration because their firms' profits and stock prices are higher due to less market competition. Hence, controlling shareholders' wealth is higher as compared with those in non-exclusive industries. Therefore, less expropriation occurs and as a result, there is no significant mitigation of negative firm value effects of non-executive directors' remuneration within this type of firm.

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