



Discussion of Ra & Kim 'Perils of Limiting the Coverage of Mandatory Pay Disclosure: The Korean Experience'

Tobias H. Tröger
GCGC, June 8, 2019

Summary of the paper

- Uses exogenous shock (regulatory intervention) to test “evasive” behavior of corporate directors (compensation disclosure)
 - Rule (promulgated 5/28/13; effective 11/29/13) mandates any director with pay beyond threshold discloses individual compensation from FY2013 onwards
 - Sample comprises 195 board members who disclose compensation for FY2013 but not for FY 2014 (80 family, 115 non-family)
 - Investigates three possible reasons for “going dark” - (1) deregistration (2) pay cuts below threshold (3) retirement - and relates them to director and firm characteristics
- Relevant for policy-makers contemplating design of disclosure regime in similar CG environment

Main results

- “Evasive” high executives
- Preference

– Two firms in FY2013 respectively

– Family firms

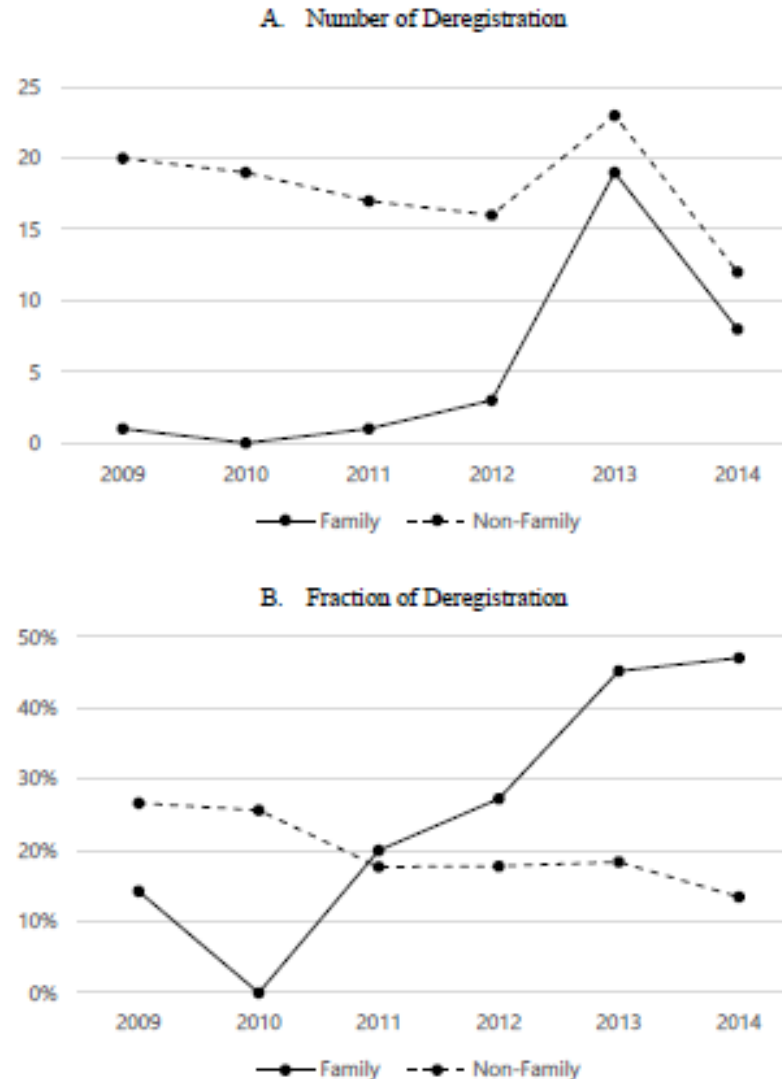
– Family firms higher

– Likelihood between

– Family companies

Figure 2: Deregistration Trend Over Time

These figures compare the number and the fraction of deregistration between family and non-family executives from 2009 to 2014. An executive is engaging in deregistration in year t if he or she is registered as a director in year $t - 1$, but listed as a non-registered executive in year t . The fraction of deregistration is the number of deregistration divided by the sum of deregistration and retirements.



firms with

% of
rule?

non-

hains
end

o

2013

HOUSE OF
FINANCE

S A
F E

What we don't learn from the paper...

- Political and broader legal landscape → potential driver of deregistration if being director less attractive overall
 - What's different from 2006 and 2009? Generally more hostile environment vis-à-vis chaebols (“public outrage”)? → Family directors' deregistration seem to pick-up before 2013
 - Any other relevant reform, eg tightening of liability regime?
- What happens in the investor community and the general public in reaction to 2013 disclosures (anecdotal evidence purported to be representative)?
- Motivation of “evasion” as determinant of social impact → Behavior driven by (fear of) shareholder or public discontent? Efficiency vs. distributive concerns
- Any adaptation in compensation of other directors?

Are pay cuts really „evasion“

- Paper establishes that some (family) executives respond to the law and gives observation negative spin
- Policy maker signals that any compensation below threshold is deemed unsuspicious
 - Distributional concern regarding absolute levels (not efficient structure which matters more from shareholder perspective, Jensen & Murphy, 1991)
 - Pay cuts are real (despite potential compensation through other tunneling transactions)
 - Policy objective achieved because (family) directors take economic hit → route for rent seeking partly closed

Think again also about deregistration

- Deregistration can have serious consequences for family director → *ceteris paribus* scenario only if non-director position grants same power, prestige, compensation etc.
- Deregistration may have negative welfare effects

Family director premium (Cheong & Kim, 2019) as tunneling

- Pay for non-performance
- Deregistration impedes rent-seeking (at the margin) → effect hinges on effectiveness of RPT regime
- (Shareholder) welfare enhancing

Family director premium as monitoring compensation

- Costly blockholder mitigation of PA conflict compensated through „optimal tunneling“, Gilson & Schwartz, 2015
- Deregistration hinders blockholder monitoring power → effect hinges on controller's access to non-family directors (more severe PA conflict)
- Potentially (shareholder) welfare decreasing

Difference in value of firms with many deregistrations compared to those with few deregistrations?

Minor points

- Executive Pay based on annual financial statement → accounting standards matter, eg with regard to incentive compensation (fair value at grant vs. pay-out)
- No clear explanation for “listing” of non-registered executives → legal obligation to do so?
- Qualification of “retirement” hinges on observable retirement payment in FY2013 → hidden parachute in RPT; yet, bias (overstating retirements) works in authors’ favor
- High foreign ownership expected to decrease evasive behavior → foreign investors may be good monitors only *after* disclosure (enforcers not investigators)
- Any sanctions for non-disclosure/“evasion”? → fraudulent evasion, misuse of legal form etc.

Tobias H. Tröger

SAFE professor of private law, commercial and business law,
jurisprudence

Goethe University House of Finance

Theodor-W.-Adorno-Platz 3

60629 Frankfurt am Main

Germany

p +49 69 798 34391

f +49 69 798 34536

troeger@jur.uni-frankfurt.de



Goethe University | House of Finance
Grüneburgplatz 1 | 60323 Frankfurt am Main
Phone +49 69 798 30080 | Fax +49 69 798 30077
info@safe-frankfurt.de | www.safe-frankfurt.de



LOEWE

Exzellente Forschung für
Hessens Zukunft