

COMPLETION REPORT

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Sustainability and CEO Compensation Structure in Japanese and ASEAN Companies

This research examined the association between sustainability performance in terms of the overall environmental, social, and governance (ESG) score and level of board compensation (including the CEO if a board member) in Japan and ASEAN-5 countries. Next, we examined each of the individual ESG pillar scores and their association with level of board compensation. Drawing on agency and stakeholder theories, and using a sample of sustainability-friendly companies rated by Thomson Reuters Asset4/Refinitiv Eikon for the period 2015 to 2019, we find, first, that in both Japan and the ASEAN-5, ESG scores are positively associated with level of board compensation, and, second, that in the ASEAN-5, the social pillar score is positively linked with level of board compensation. However, at Japanese companies, the governance pillar score is positively related to level of board compensation.

This research extends past studies on the linkage between ESG or sustainability performance and compensation for board directors. Consistent with the notion of the agency and stakeholder theories, sustainability-friendly firms should give their directors incentives to encourage high sustainability performance. Thus, board engagement in sustainability activities can reduce agency problems and, therefore, satisfy stakeholders' expectations. Global issues such as an alarming number of corruption scandals and rising poverty rates have put a spotlight on sustainability matters in the ASEAN member countries. In addition, companies in ASEAN countries have insufficient protection for minority shareholders and are therefore relatively less stakeholder-oriented companies doing business in these areas strengthen their legitimacy by focusing primarily on social pillars, managing local dependencies, and building a community of trust. The findings in Japan can be attributed to the Ministry of the Environment Japan (MOEJ) playing an important role in promoting sustainable corporate governance and the inclusion of ESG criteria in decision-making.

In addition to its academic relevance, the research also has practical implications for companies, regulators, practitioners, and investors. First, to ensure that sustainability is completely integrated into the business strategy, companies need to add sustainability strategy targets to the boards' compensation contracts as motivation. Second, companies and practitioners should consider that each ESG dimension influences sustainability performance and board compensation schemes differently. These dimensions need to be well defined in achieving sustainability objectives; otherwise, sustainability performance can be an elusive goal. Further, we suggest that companies seek external independent assurance to assess the quality of the ESG metrics and reporting. Thus, the findings in this study have practical implications for investors and key stakeholders, who appear to be increasingly interested in integrating ESG with performance evaluation. The limitation of this research is that CEO compensation is omitted if the CEO is not a board member. Another limitation of the research is the sustainability performance is based on ESG score provided by a third party rating agency. Future studies may consider other ESG rating agencies.

Publication of the Results of Research Project:

Verbal Presentation (Date, Venue, Name of Conference, Title of Presentation, Presenter, etc.)

Virtual conference: BLM2-ICAM4

AN INTERNATIONAL JOINT E-CONFERENCE (organizer: CIRI (Centre for Industrial Revolution and Innovation), Taylors University, and University of Kelaniya (Sri Lanka))

Title of presentation: IMPACT OF BOARD SIZE AND INDEPENDENT DIRECTORS ON SUSTAINABILITY REPORTING IN JAPAN

Presenter: Dr. Sahar E-Vahdati

Date: 11th Sep 2021

Thesis (Name of Journal and its Date, Title and Author of Thesis, etc.)

1. First paper which is accepted currently and it will be published by the end of Dec 2022

Name of Journal: "Borsa Istanbul Review (Elsevier). (top 10 in list of Web of Science with impact factor of: 4.288, Q1; cite score: 5.3)

Title: "Sustainability Performance and Board Compensation in Japan and ASEAN-5 Countries"

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2. Second paper which is currently under review

Name of Journal: Sustainability (impact factor in Web of Science 3.889, citesscore:5.0); Publisher: MDPI

Title: The value relevance of ESG practices in Japan and Malaysia: Moderating roles of CSR award, and former CEO as a board chair

Authors: Sahar E-Vahdati, Wan Nordin Wan-Hussin, Mohd Shazwan Mohd Ariffin

Book (Publisher and Date of the Book, Title and Author of the Book, etc.)