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Effect of Non-Cash and Non-Operating Related Party Transactions on Board of Directors' Compensation[1]

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Research Paper

INTRODUCTION

Related party transactions can indicate the exercise of power by people within the organization in line with personal interests, or indicate transactions as a result of effective contracts. In general, most of the research shows that the opportunistic related party transactions are related to the inefficiency of investment and capital allocation due to negative consequences such as securing individual benefits.The basis for calculating compensation is based on contracts consisting of accounting figures and in particular net profit, and related party transactions by exercising the authority of managers in choosing accounting and reporting procedures can be used to manage and manipulate profits and secure the interests of certain groups at the cost of reducing the value of the company to other stakeholders. Due to the establishment of a profit-based reward system and the possibility of opportunistic use of related party transactions by managers, to prevent the transfer of wealth and reduce the interests of shareholders, control and monitoring tools are needed that strong corporate governance tools can in this regard prevent the outflow of wealth and devaluation of the company. Considering that non-cash related party transactions are done on an accrual basis and at the end of the year, they are related to the discretion of the management, and as the average period of

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collection or payment of these transactions lengthens, the profit quality decreases. Also, due to the flexibility in financial reporting, it is easier to hide non-cash transactions with related parties than cash transactions, so managers' opportunistic motives will lead to non-cash related party transactions to achieve personal benefits and lower quality profit reporting. Considering the flexibility of standards and managers' discretion in choosing accounting procedures that can affect net profit as the basis for bonus calculation, as well as managers' tendency to hide opportunistic related party transactions and distort financial statements thereby, this question is raised that How does transactions with related parties affect the calculation of the remuneration of the board of directors? The purpose of this study is to investigate the effect of non-cash and non-operating related party transactions on board of directors' compensation

MATERIALS AND METHODS

This research is applied in terms of purpose and correlation and post-event in terms of method. In order to test the research hypotheses, 118 companies were selected in the period 2011-2019 and analyzed using multiple regression models.

RESUALTS AND DISCUTION

The results of test the research hypotheses show that the non-cash and non-operating related party transactions have a positive effect on the board of directors' compensation. Also, the corporate governance quality causes a negative effect on the relationship between the non-operating related party transactions with the board of directors' compensation. While strong corporate governance has no effect on the relationship between non-cash related party transactions and board of directors' compensation. So with increase in the volatility of non-operational related party transactions, the board of directors' compensation has decreased, which indicates the recognition of the risk of these transactions due to their low quality, and indicates the beneficial role of profit quality in the efficiency of contracts and the reduction of agency problems between the owner and the manager. Also, the results showed that strong corporate governance has a significant negative effect on the relationship between non-operational related party transactions and the fluctuation of non-operational related party transactions and the board of directors' compensation.

CONCLUSION

The predictions of the effective contracts hypothesis are: a) related party transactions are related to factors related to strong corporate governance, b) there is no relationship between managers' related party transactions and manager's compensation, and c) a relationship between managers' related party transactions and manager's compensation It is either neutral or negative. The negative prediction from the above discussion about related party transactions indicates the use of these transactions as an efficient means to provide only a part of the managers' remuneration.

The results of the test of the first and second hypotheses of the research show the opportunistic approach and weak management of the company, which despite the high volume of transactions of related parties, which reduces the quality of profit. So despite non-cash related party transactions to easily hide abnormal transactions and despite non-operating related party transactions that are more volatile and less stable, more compensation have been paid to the board of directors. While the volatility of non-operational related party transactions has increased, the remuneration of the board of directors has decreased, which indicates the recognition of the risk of these transactions due to their low quality, and indicates the beneficial role of profit quality in the efficiency of contracts and the reduction of agency problems between the owner and the manager. These transactions took place due to efficient contracts under the supervision and control of strong corporate governance, and given that these transactions are part of the contracts, the profits from these transactions are not the basis for calculating the remuneration of the board of directors and thus management. So strong corporate governance has changed the attitude of related party transactions from an opportunistic approach to a contract efficiency approach. According to the contract efficiency approach, related party transactions are conducted due to strong controls and strong corporate governance and for these transactions which are part of the contracts and demanded by the business unit, no compensation is given and the effect of these transactions is neutral or negative on board of directors' compensation. Also, the results showed that strong corporate governance has a significant negative effect on the relationship between non-operational related party transactions and the fluctuation of non-operational related party transactions and the remuneration of the board of directors. That is, these transactions are

due to the execution of effective contracts under the supervision and control of strong corporate governance, take place and considering that these transactions are considered part of the contracts, the profits from these transactions are not the basis for calculating the board of directors' bonuses, and thus strong corporate governance changes the attitude of related party transactions from the opportunistic approach to the efficiency approach of contracts has done.

Keywords: Board of Directors Compensation, Efficient Contracts, Non-Operating Related Party Transactions, Non-Cash Related Party Transactions.
JEL Classification: M12, G34, L25.

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