GLOBAL JOURNAL OF COMMERCE & MANAGEMENT PERSPECTIVE
(Published By: Global Institute for Research & Education)
www.gifre.org

Directors Share-Based Compensations and Performance: A Case of the Top 100 MCG Index Companies

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1.0 Introduction

Organization or corporation exists based on conviction of an internal and external party. As an internal party, the board of directors (BODs) is the highest governing body and the most important component as a workforce in a company in order to achieve the companies' goals and objectives. Therefore, organization usually compensates the BODs for their effort and their diligence in managing the company through salary, bonus, allowances, fees and shares. In today's practice, the share option or stock option grants are new instrument of compensation introduced for the BODs in aligning their interests with shareholders. As a result, top management will be more motivated to strive towards achieving the firms' performance. However, there is one major issue arise regarding the compensation. It is due to the circumstances where the compensation given and the performance or contributions towards the companies are not aligned.

Consequently, the Board of Directors (BODs) does not serve shareholders' interests which might resulted in agency problem. Particularly, agency cost is borne by the principal but currently, shareholders adjusted the management compensation in order to transfer the agency cost to the agent. One of the mechanisms to make it success is to apply the performance-based pay. The compensation of the BODs is determined by the level of the performance company achievement. One of the determinations is using the share–based payment. Share options and share grants are an entitlement which gives right to the buyers (directors, employees) but it is not an obligation to purchase before the options expiration time and at an agreed price which commonly the price is lower than the market price. As defined by Jeffrey (2008), stock options typically represent a right granted to the holder of the option to acquire shares of a company's stock in the future at a fixed price called the exercise price or strike price.

This research emphasizes on share-based compensation which are designed primarily to motivate directors to exert greater effort. Share options privatize the firm's monitoring task into the hands of its directors. Each director which is equipped with share-based compensation is motivated to monitor other employees to make sure her peers do not harm the firm and that they do their best to maximize its value. Director share options and share grants produce more responsible directors, one would observe better fulfillment of board tasks in order to serve shareholders' interests. It is supported by California Public Employees' Retirement System (CalPERS); one of the nation's largest public pension fund which proposed that 50 percent of director's total compensation are in share-based. In addition to that, the issue also was further explained by the Financial Reporting Standard 2 which emphasized on the measurement and recognition of the share options.

In a nutshell, the fundamental purpose of the study is to synthesize the broad literature on how directors' share-based compensation influences firm performance. Henceforth, the main purpose of this study is to investigate the relevance of directors' share-based compensation in influencing firm performance in Malaysia. Specifically, the study is conducted to achieve the following sub-objectives:

i. To explore on the share option and share option grant as one of the elements used in directors' compensation in Malaysia.

ii. To examine if there are any differences in the share option and share option grant compensated to board of directors in the Bursa Malaysia (MCG and Non-MCG's companies).

iii. To identify the relationship between the directors' share option and share option grants and the corporate performance.

The next section provides the literature review and hypotheses development, followed by research framework in Section 3. The research design and methodology is discussed in Section 4 and the results in Section 5. Finally, Section 5 presents the concluding remarks of the study.

2.0 Literature Review and Hypotheses Development

Agency theory which was developed by Jensen & Meckling (1976) identifies the agency relationship between the principal and agent, whereby the principal engages the agent to perform some services on their behalf and principal will normally delegate decision making authority to the agent. Thus the principal will compensate the agent well enough as their rewards if they perform best. Ionnis (2009) stated that the main responsibility of the boards is to monitor the management of the company and antecedents. There are board incentives like board dependence and equity compensation. This theory is relevant to this research as there is an emerging relationship due to the separation of ownership between the role play by the directors on behalf of the shareholders towards the firm performance. The directors as the agents perform their duties and responsibilities on behalf of the shareholders who are the principal in order to serve shareholders' interests whom in return, shareholders compensate directors with remuneration and benefits.

In fact, by granted the directors with share option as their remuneration, shareholders will always questioning whether it is worth to grant share option upon efforts delivered by the directors. Therefore, there is an approach that shareholders can implement to solve their dilemma which by benchmarking the firm performance in terms of their annual profit or financial ratio analysis as compared to other companies in the same industry.

The current study observes the share options grant employed to the board of directors listed and non-listed under MCG Index due to fulfillment of the aspects stated above. This is supported by the recent study that emphasizes the sample on the MCG Index (Abdul Jalil and Abdul Rahman, 2010). Another study by Kiridaran, Robert and Ramachandran (2003) found where a predominant number of publicly-traded firms grants share options to executives, but there still are quite a few firms that do not grants or lower grant share options. This permits a comparison of firm-specific attributes between these two groups. Another sustenance is from Conyon and Murphy (2000) which the researchers compared the composition of executives' pay in the US with that of the UK. They revealed that stock option grants constitute one-third of total pay of US executives compared to only 10 per cent for UK executives.

Therefore the hypotheses are:

H1**:** There is a significant difference of the share option compensated to the board of directors in the companies listed in MCG Index and non-listed companies.

H2: There is a significant difference of the share option grants granted to the board of directors in the companies listed in MCG Index and non-listed companies.

Most director compensation experts recommend paying directors at least a mandatory minimum in stock (Carey, 1995; Davis & Stobaugh, 1995; Elson, 1996; Hambrick & Jackson, 2000; Wamberg, 1997). This arrangement could improve the alignment of directors' and stockholders' interests, as suggested by the empirical evidence cited above. Increased equity ownership by directors can reduce agency problems by providing directors with a direct financial incentive to vigilantly monitor, direct, and control the actions of top management. Perry (1999) argues that this financial incentive can be significant even in the case of independently wealthy directors. Likewise, Lorsch (1989) noted that director stock ownership not only provided directors with a financial incentive, but also strengthens directors' psychological bonds to the firm. Finally, greater share ownership gives directors the power to challenge executives, which can lessen managerial opportunism and lead to higher firm performance. Thus, greater use of directors' incentive compensation in the form of stock grants and stock options will lower agency costs, leading to superior firm performance.

Therefore the hypotheses are:

H3: The relationship between the directors share options ratio and the firm performance is significant.

H4: The relationship between the directors share grants ratio and the firm performance is significant.

Prior research examines the association of managerial (directors) ownership and share-based compensation with future firm performance, and finds evidence consistent with the incentive-alignment effect of these equity incentive elements (Lambert and Larcker 1987; Morck, Shleifer and Vishny. 1988; Hanlon Raigopal and Shevlin, 2003, among others).

The results of the study by Hanlon et al. (2003) which investigated the association between employee share option compensation and future firm performance verify the incentive alignment perspective as the option grant value attributable to economic determinants was strongly and positively related to future earnings. In addition, they found a statistically significant positive relation between option grant values and investment opportunities. This result suggests that option grants are given to mitigate information asymmetry in firms with large investment opportunities.

3.0 The Research Framework

This section demonstrates the schematic diagram o the research framework of this study.

Figure 1: Schematic Diagram of the Relationship between the Independent and Dependent Variable

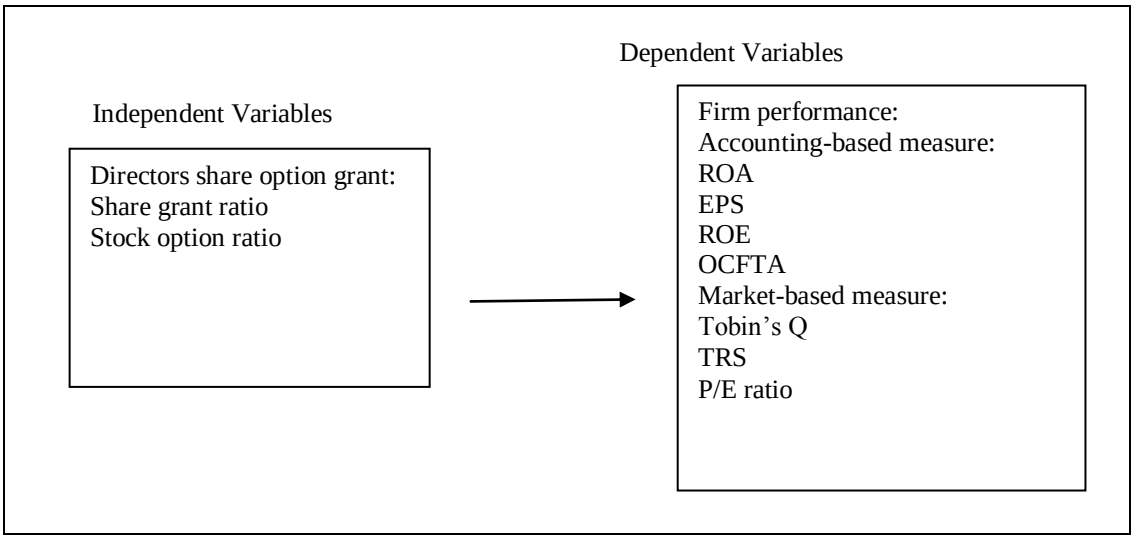


Figure 1 depicts the conceptual framework of this study. As illustrated in the framework, the study examines the relationship between the directors' share-based compensation and the firm performance.

3.1 Measurement of Variables

A summary of the measurement of variables that will be used in the study is depicted in table 1.

Table 1: The Measurement of Variables

Variables	Measurement of Variable
Independent Variables	
Stock option ratio	Ratio of dollar stock option compensation to total dollar directors' compensation
Stock grants ratio	Ratio of dollar stock grant compensation to total director compensation
Dependent Variables	
Accounting-based measure	
Return on assets (ROA)	Ratio of profit before tax to total assets
Earnings per share (EPS)	Net profit or loss attributable to ordinary shareholders to weighted average number of shares
Return on equity (ROE)	Ratio of after tax profit to shareholders' equity as similar to Jorn et al. (2010)
Operating cash flow over total assets (OCFTA)	Profit before tax adjusted for changes in working capital which recently applied by Mohamad Yoosuf et al. (2010) as similar to Abdul Rahman and Limmack (2001). Operating cash flow is used because it is a good indicator of corporate financial performance rather than net income since it is less subjected to distortion from differing accounting policies.
Market-based measure	
Tobin's Q	Formula: $q = \frac{MVE + D}{TA}$ MVE = Market value of equity D = Book value of debt TA = Total Assets Comparing the market value of company stock with the value of company equity book value as similar to Tiago and Walter (2010).
Total one-year shareholder return on common stock (TRS)	Closing price at fiscal year-end plus dividends divided by the closing price of the prior fiscal year-end which had been applied by Mahmoud and Frank (2008)
Price-earnings ratio (P/E)	Formula: $\frac{\text{Market Value per Share}}{\text{Earnings per Share (EPS)}}$ Used because it shows current investors demand for company share which supported by Vorek (2009).

4.0 Research Design and Methodology

The population of this research is MCG Index and Main Market companies. From these, the study identified companies that had granted Executive Share Options Scheme (ESOS) which eliminating firms for incomplete data and other inadequacies. The sample of ESOS spans the two years period from year 2008 to 2009 and cuts across a wide range of industries.

Among this population (Appendix A), 30 companies met requirements to be selected as a sample from top 100 companies listed under MCG Index. Meanwhile, another 30 companies are chosen randomly from non-listed MCG Index which is from Main Market. The law of large numbers says that if a random number is drawn from a population the larger the sample, the closer the mean of the sample to the mean of the population. The larger the sample is the increased resemblance of the sample to the population. The current study is conducted on two different groups to observe whether there is any difference attributes between the groups. However, the present study excluded companies from two

industries; insurance and banking and financial institution. This is because companies in banking and financial institution and insurance are restricted to Bank Negara Malaysia guideline under Banking and Financial Institution Act (1989) and Insurance Act (1996) mean while other companies follow Companies Act. It is aided by the study conducted by Mattar (2006).

The data that are used in this research are collected under secondary source of data. Secondary data is the data that have been already collected and readily available from other sources. In conducting this research the sources are from Bursa Malaysia and Bloomberg. Furthermore, the data also have been collected through the financial report of 2008 and 2009 from the sample corporate websites. This study is based on the content analysis of the annual reports of the sample companies in order to obtain data to measure the dependent and independent variables.

5.0 Finding and Discussion

5.1 Descriptive Analysis

Descriptive analysis is used to describe the huge amount of data that had been collected into numeral values. By using the SPSS version 18.0 it may determine the descriptive statistics of a set of data, namely the scores of mean, median, mode, standard deviation and variance. The descriptive analysis will serve two purposes; the first is to explore the data that had been collected; secondly is to summarize and describe the observation. Besides, descriptive analysis also investigates the possible relationship among variables, whether there are any differences between two or more groups, and the likelihood which also known as inferential statistics.

From Table 2, the mean for directors' share options and share grants in MCG Index are 27,016,676.85 shares and 1,548,475.20 shares respectively. Meanwhile the mean for directors' share options for Non- MCG Index companies is 1,916,367.30 shares while the directors' share grants is 269,456.65 shares. It indicates that on an average 30 MCG Index companies for two years rewarded higher number of shares options and share grants to their directors than Non-MCG Index companies. This is supported by Pete (2011) that corporate executives often received stock option grants as a major part of their compensation. Thus it can be concluded that this is the pattern of current practices in Malaysia.

Table 2: Descriptive Statistics

MCG Index

Descriptive Statistics

No. of Shares	N	Minimum	Maximum	Mean	Std. Deviation
Share Options	60	0	762524000	27016676.85	116584452.62
Share Grants	60	0	68988500	1548475.20	8928675.96
Valid N (listwise)	60				

Non-MCG Index

Descriptive Statistics

No. of Shares	N	Minimum	Maximum	Mean	Std. Deviation
Share Options	60	0	14922650	1916367.30	2795859.953
Share Grants	60	0	7735000	269456.65	1054523.159
Valid N (listwise)	60				

Statistics

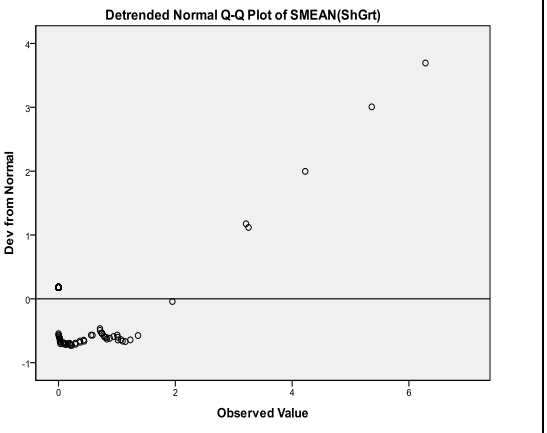
		SMEAN (ShOpt)	SMEAN (ShGrt)	SMEAN(ROA)	SMEAN(ROE)	SMEAN(EPS)	SMEAN (OCFTA)	SMEAN(TQ)	SMEAN(TRS)	SMEAN(PE)
N	Valid	120	120	120	120	120	120	120	120	120
	Missing	1	1	1	1	1	1	1	1	1
Mean		2.366971	.397025	5.032825	8.912342	2.376185	1.870991	1.127650	1.753141E7	32.233598
Median		.461614	.000000	4.470700	8.233750	.134250	.100596	.928250	6.597544E6	10.879950
Std. Deviation		9.5493357	.9664469	6.0543043	10.9066134	16.2957698	9.6809341	1.2565034	3.0538433E7	181.9580079
Skewness		8.908	4.080	-.036	-.530	6.523	6.928	8.323	4.292	10.808
Std. Error of Skewness		.221	.221	.221	.221	.221	.221	.221	.221	.221
Kurtosis		86.521	18.839	4.715	5.205	44.733	50.020	81.576	24.809	117.805
Std. Error of Kurtosis		.438	.438	.438	.438	.438	.438	.438	.438	.438

For standard deviation, the standard deviation of share options and share grants on MCG Index companies are larger than Non-MCG Index companies. Therefore, the data are more spread out the observations in MCG Index companies rather than Non-MCG Index companies.

The present study assumes that when a company complies with corporate governance procedures and policies, it performs far better than company that takes for granted on the corporate governance issue. Thus the company is more stabilize to compensate their directors with higher share-based payments. This does not only motivating the directors to align with shareholders interest but satisfying their self-interest as well encourages them to sustain the good performance. The skewness results in negative values in return on assets (ROA) and return on equity (ROE) indicate a negative skew at value of -0.036 and -5.30 respectively while positive values for kurtosis indicate a distribution that is peaked (leptokurtic).

5.2 Normality Test

Figure 2: Test of Normality for all variables



Tests of Normality

	Kolmogorov-Smirnov[a]			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	df	Sig.
SMEAN(ShOpt)	.402	120	.000	.208	120	.000
SMEAN(ShGrt)	.341	120	.000	.457	120	.000
SMEAN(ROA)	.108	120	.002	.921	120	.000
SMEAN(ROE)	.109	120	.001	.925	120	.000
SMEAN(EPS)	.502	120	.000	.176	120	.000
SMEAN(OCFTA)	.443	120	.000	.185	120	.000
SMEAN(TQ)	.287	120	.000	.366	120	.000
SMEAN(TRS)	.283	120	.000	.550	120	.000
SMEAN(PE)	.430	120	.000	.107	120	.000

a. Lilliefors Significance Correction

From detrended normal Q-Q Plot of ShGrt in Figure 2, there are points that do not assemble around the horizontal line through zero. Thus, the distribution of the sample is not normal since the point of normal distribution should assemble around a horizontal line through zero.

The boxplot illustrated above indicates that a distribution is skewed is now normal because it is skewed in the middle of the upper and lower level. Therefore, a natural logarithmic transformation is appropriate because the distribution of share grant is normal. Based on the results in Kolmogorov-Smirnov and Shapiro-Wilks test, it shows that the test for normality produced is not significant because the level is less than 5% (p-value < 0.05).

5.3 Mann-Whitney U Test

H1: There is a significant difference of the share options compensated to the board of directors in the companies listed in MCG Index and non-listed companies.

H2: There is a significant difference of the share grants granted to the board of directors in the companies listed in MCG Index and non-listed companies.

Based on the Mann-Whitney U test results in Table 3, it is found that there is insufficient evidence to reject the alternate hypothesis for H2 since the test results are significant (p = 0.001). Hence there is significant difference in share grants granted to the board of directors in the companies listed in MCG Index and non-listed companies.

However, the p-value of share options is 0.525. This indicates that it is not significant to accept the H1 hypotheses. This implies that there is no significant difference in the share options compensated to the board of directors in the companies listed in MCG Index and non-listed companies. It can be concluded that there is a difference emerged between these two groups; MCG Index companies and Non-MCG Index companies. This circumstance is similar to Conyon and Murphy (2000) in which the researchers compared two countries (UK and US) and discovered that stock option grants constitute to one-third of the total pay for US executives compared to only 10 per cent for UK executives.

Table 3: Mann-Whitney U Test

Ranks

	Company Listing	N	Mean Rank	Sum of Ranks
SMEAN(ShOpt)	Non-MCG List	60	62.52	3751.00
	MCG List	60	58.48	3509.00
	Total	120		
SMEAN(ShGrt)	Non-MCG List	60	51.11	3066.50
	MCG List	60	69.89	4193.50
	Total	120		
SMEAN(ROA)	Non-MCG List	60	51.72	3103.00
	MCG List	60	69.28	4157.00
	Total	120		
SMEAN(ROE)	Non-MCG List	60	50.50	3030.00
	MCG List	60	70.50	4230.00
	Total	120		
SMEAN(EPS)	Non-MCG List	60	48.07	2884.00
	MCG List	60	72.93	4376.00
	Total	120		
SMEAN(OCFTA)	Non-MCG List	60	47.67	2860.00
	MCG List	60	73.33	4400.00
	Total	120		
SMEAN(TQ)	Non-MCG List	60	45.27	2716.00
	MCG List	60	75.73	4544.00
	Total	120		
SMEAN(TRS)	Non-MCG List	60	43.90	2634.00
	MCG List	60	77.10	4626.00
	Total	120		
SMEAN(PE)	Non-MCG List	60	61.62	3697.00
	MCG List	60	59.38	3563.00
	Total	120		

Test Statistics[a]

	SMEAN(ShOpt)	SMEAN(ShGrt)	SMEAN(ROA)	SMEAN(ROE)	SMEAN(EPS)	SMEAN (OCFTA)	SMEAN(TQ)	SMEAN(TRS)	SMEAN(PE)
Mann-Whitney U	1679.000	1236.500	1273.000	1200.000	1054.000	1030.000	886.000	804.000	1733.000
Wilcoxon W	3509.000	3066.500	3103.000	3030.000	2884.000	2860.000	2716.000	2634.000	3563.000
Z	-.635	-3.239	-2.766	-3.149	-3.915	-4.041	-4.797	-5.228	-.352
Asymp. Sig. (2-tailed)	.525	.001	.006	.002	.000	.000	.000	.000	.725

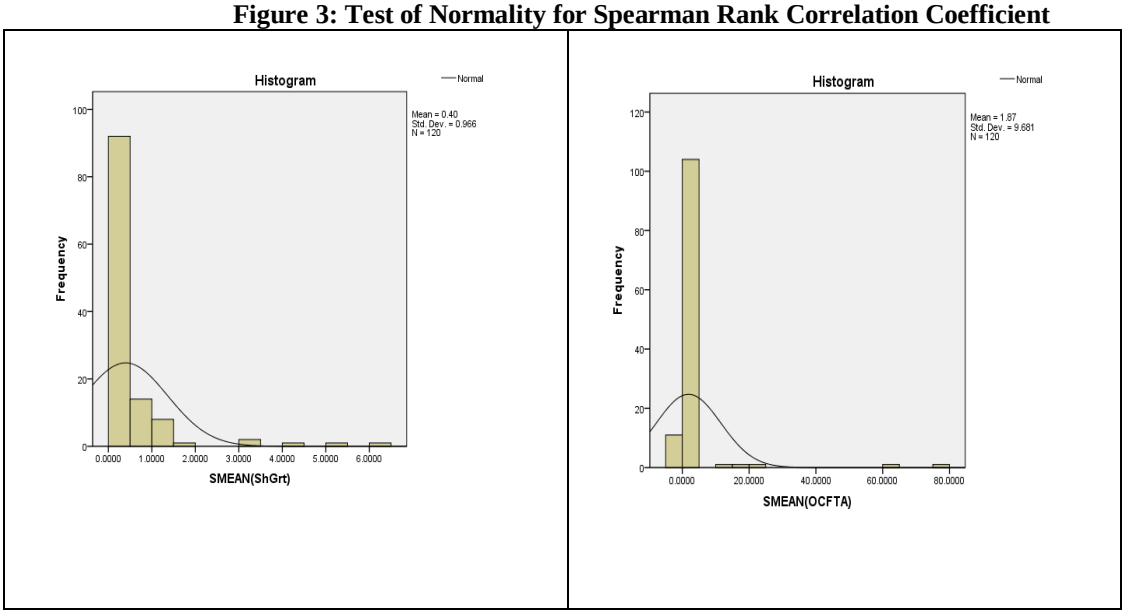
a. Grouping Variable: Company Listing

5.4 Correlational Analysis

H3: The relationship between the directors share options ratio and the firm performance is significant.

H4: The relationship between the directors share grants ratio and the firm performance is significant.

Figure 3: Test of Normality for Spearman Rank Correlation Coefficient



Based on Figure 3, the values on the vertical axis indicate the frequency of cases. The values on the horizontal axis are the midpoint of value ranges. There is no consistency bar for each midpoint which means that the shape of the distribution is not normal. The histograms for share grants (ShGrt) and operating cash flow over total assets (OCFTA) show that the distributions are not normal. The Spearman correlation coefficient is significant ($r = 0.294$, $p = 0.001 < 0.005$). This indicates that there exist a strong significant positive correlation between the share option grants and firm

performance which is operating cash flow over total assets (OCFTA). Meanwhile there is no significant value ($p > 0.005$) between share options and firm performance.

Thus there is a significant evidence to accept H4 and sufficient evidence to reject H3. This result is aligned with the study done by Abdul Rahman and Mohamed Yoosuf (2005) which analyzed the sample further by examining the relationship between the director's remuneration (share grants) and firm performance. Concisely, the results from the study reveal that there is a positive relationship between the director's remuneration (share grants) and firm performance as measured by the operating cash flow to total asset (OCFTA).

Table 4: Table of Correlation - Spearman's Rho

Correlations

			SMEAN(ShOpt)	SMEAN(ShGrt)	SMEAN(ROA)	SMEAN(ROE)	SMEAN(EPS)	SMEAN(OCFTA)	SMEAN(TQ)	SMEAN(TRS)	SMEAN(PE)
Spearman's rho	SMEAN(ShOpt)	Correlation Coefficient	1.000	.039	.094	.178	-.060	.004	.125	.022	-.076
		Sig. (2-tailed)	.	.673	.304	.051	.513	.965	.171	.814	.408
		N	121	121	121	121	121	121	121	121	121
	SMEAN(ShGrt)	Correlation Coefficient	.039	1.000	.065	.104	.159	.294**	.094	.030	-.028
		Sig. (2-tailed)	.673	.	.477	.258	.082	.001	.307	.743	.758
		N	121	121	121	121	121	121	121	121	121
	SMEAN(ROA)	Correlation Coefficient	.094	.065	1.000	.851**	.613**	.429**	.264**	.102	-.468**
		Sig. (2-tailed)	.304	.477	.	.000	.000	.000	.003	.264	.000
		N	121	121	121	121	121	121	121	121	121
	SMEAN(ROE)	Correlation Coefficient	.178	.104	.851**	1.000	.558**	.380**	.298**	.099	-.440**
		Sig. (2-tailed)	.051	.258	.000	.	.000	.000	.001	.279	.000
		N	121	121	121	121	121	121	121	121	121
	SMEAN(EPS)	Correlation Coefficient	-.060	.159	.613**	.558**	1.000	.360**	.206*	.356**	-.546**
		Sig. (2-tailed)	.513	.082	.000	.000	.	.000	.024	.000	.000
		N	121	121	121	121	121	121	121	121	121
	SMEAN(OCFTA)	Correlation Coefficient	.004	.294**	.429**	.380**	.360**	1.000	.186*	.282**	-.179*
		Sig. (2-tailed)	.965	.001	.000	.000	.000	.	.041	.002	.049
		N	121	121	121	121	121	121	121	121	121
	SMEAN(TQ)	Correlation Coefficient	.125	.094	.264**	.298**	.206*	.186*	1.000	.420**	.263**
		Sig. (2-tailed)	.171	.307	.003	.001	.024	.041	.	.000	.004
		N	121	121	121	121	121	121	121	121	121
	SMEAN(TRS)	Correlation Coefficient	.022	.030	.102	.099	.356**	.282**	.420**	1.000	.039
		Sig. (2-tailed)	.814	.743	.264	.279	.000	.002	.000	.	.675
		N	121	121	121	121	121	121	121	121	121
	SMEAN(PE)	Correlation Coefficient	-.076	-.028	-.468**	-.440**	-.546**	-.179*	.263**	.039	1.000
		Sig. (2-tailed)	.408	.758	.000	.000	.000	.049	.004	.675	.
		N	121	121	121	121	121	121	121	121	121

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

5.5 Regression Model

Regression is a statistical technique to explain the relationship between variables in a mathematical order. It establishes the relationship of dependent variable and one or more independent variables. Usually, this regression model is used for prediction and estimation purposes. According to Alan (2000), the regression analysis typically assesses the statistical significance of the estimated relationship, that is, the degree of confidence that the true relationship is close to the estimated relationship. This study used a multiple regression analysis. The multiple regression models are used to determine the relationship between directors share option grant with firm performance. Statistical Package for Social Science (SPSS) version 19.0 was used to analyze the data and descriptive, correlation and regression analyses were carried out. The regression models are as follows:

$$FP = \beta 1\ [STOC / DRComp] + \beta 2\ [STGC / DRComp] + \varepsilon$$

FP : Firm performance
β1 and β2 : Variable coefficients
STOC : Stock option ratio
STGC : Stock grant ratio
DRComp : Director Compensation
ε : Error variable

The correlation coefficients, R-Square and adjusted R-Square are displayed in Table 5. A value of R-Square closest to one indicates that the model fits the data well. The R-Square of 0.417 indicates that share option ratio and share option grant can only explain about 41.7% of the total variation of ROA. However, the ANOVA results display the multiple regression model is significant ($F=7.048$, p-value = $0.000 < 0.05$). Hence, hypotheses H3 and H4 are accepted since the relationship between the independent variables of share option ratio and share option grant and firms performance. However, among measures of firm performance, only OCFTA is significant. This indicates that OCFTA has an impact

on the share grants received by the directors. This implies that when the directors are granted with shares of the company's, OCFTA will increases. Hence, directors employed by these firms will have greater responsibilities and commitment in monitoring the companies' affairs. In return, the directors would expect a higher compensation especially on the equity based. This result is consistent with findings of Lambert and Larcker 1987; Morck et al. 1988; Hanlon et al. 2003, Jensen and Murphy (1990), Wickham et al. (2001) which found that both compensation and firm performances are positively related. Besides it is proven by Jorn et al. (2010) that one of three core objectives throughout the implementation of the CG is achieved; to build upon the principles-agent relationship between the shareholders and manager as described CG as the set to mechanism to align the interest of both party. As examined from the result, the shareholders wealth is increases since the OCFTA of the companies increase as well as the directors gain the benefits from the share grants rewarded to them.

Table 5: Regression Model 1 Coefficient Results

All Years	Beta	t	Sig.
(Constant)			
Share Option Ratio	.052	.3.74	.710
Share Option Grant	.440	3.172	.003
	Model		
Model Summary			
R-Squared	0.417		
Adjusted R-Squared	0.286		
F-Statistics	7.048		
p-value	0.002		

6.0 Conclusion

Presently, companies have adopted share options and share grants compensation to directors, in an effort to align their interests with those of the firm's shareholders. Specifically, share-based compensation is intended to encourage directors to monitor executives more closely (Bryan, Gold and Sheldon, 2000), thus reducing secondary agency costs, and improving firm performance It has also attempted to rationalize and document the differential impact of share grants versus share options, and to link components of director share compensation to company performance under different contexts.

The paper analyzed the relationship between two different director share-based compensation components (i.e. share grants and share options) and two separate measures of firm performance (accounting and market based measures). Based on the analysis, the results indicate that firm performance has a significant relationship with the director remuneration explicitly on share grants. Moreover, the result strongly supports NACD Blue Ribbon Commission Report on Director Compensation (2003) which recommends a significant portion of compensation is in the form of equity because by granting share option it will reflect directors' contribution towards the company as well as enhance their self-esteem. In addition, it provides evidence to convince on Davis et al. (1997) who claimed that a steward protects and maximize shareholders wealth through firm performance, because by doing so the steward's utility functions are maximized.

The current study's result also shows that there is significant difference in share grants between the two groups; companies listed and non-listed under MCG Index. It can be inferred that the highest mean rank in the test of difference belongs to the company listed in the MCG Index. It indicates the ability of the companies in well complied with the MCCG requirements as lead to their well performing. Therefore, with a good compliance with the MCCG requirement, it will bring better performance to the company. Consequently, by rewarding excellence and tremendous rewarding packages to the directors, it will motivate and inspire them to strive for a better company performance.

This study is limited in several ways. The current study focuses on only 30 companies which are listed and non-listed in MCG Index respectively for two years period of financial performance and does not look at the trend of how the companies have compensated the share option grants to the directors. Therefore the findings may differ if the current study expands the sample and duration of the investigation

Another obstacle in conducting this study is the use of per-share option value as used by Cordeiro (2007). Most of the previous studies in the US used Black-Scholes option pricing model to obtain the per-share option value (Boumosleh, 2009). Conversely the present study absorbs the share option value explicitly from the financial report. The findings will be more accurate and exact if the study uses the Black-Scholes option pricing model since the per-share option value is more specific and precise. However, the Black-Scholes option pricing model software is not available at the campus and not affordable for personal subscription.

Currently in Malaysia, MCCG enforces the companies to establish the remuneration committees in accessing the appropriateness of rewarding directors' compensation packages. Thus, the study highlights the needs for remuneration committees to have awareness on offering the directors with a higher proportion of stock grants as a part of their compensation packages. Subsequently, the companies should take an initiative to develop the ESOS and option committee. This committee is formed primarily to establish and administer the option and ESOS of the company. This is to ensure the adoption of the ESOS and option are running smoothly since there are growth practices in Malaysia.

Different research designs in the future study may help the researcher to capture the effects of compensation practices to the company performance. Future research on directors' share options and share grants could perhaps may incorporate more over a longer period. The future study should compare the firm performances before and after the adoption of the specific compensation plans. Besides, researcher may also consider extension that includes other context such as firm diversification and the industry structure.

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