



# Faculty of Business Administration

**SEMINAR SERIES No.11/1011**

*Finance*

## **“The Retention Consequences of Caps on Executive Compensation during Financial Crises”**

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### **Abstract**

We estimate a structural model of CEO compensation and turnover during financial crises and public bailouts, using it to analyze one of the main provisions of the American Recovery and Reinvestment Act of 2009 (ARRA), namely a cap on executive compensation imposed on firms accepting bailouts. Using Compustat and ExecuComp data, we estimate the model's pre-policy regime and then simulate the effect of the policy on the design of executive compensation contracts, CEO turnover, the probability a firm accepts a bailout, and the probability of bankruptcy. The analysis characterizes the distortion in compensation contracts that results from the policy, i.e. the piece rate is suboptimal and is either too high or too low depending upon the executive's risk preferences and the variance in the performance measure on which the variable pay is based. While the theoretical model allows base pay and the piece rate to be either substitutes or complements, the data reveal them to be substitutes.

**Date:** March 16, 2011 (Wednesday)

**Time:** 15:00 -16:30

**Venue:** J317

**ALL ARE WELCOME!**

## **A Short Biography of Prof. Scott Fung**

Prof. Fung holds a DBA degree from Graduate School of Management, Boston University. Before joining California State University, he was an assistant professor at Hong Kong Polytechnic University. Prof. Fung's research interests cover various areas in corporate finance, options and futures, market microstructure, and real estate. His research papers have been published on excellent academic journals such as *Journal of Portfolio Management*, *Journal of Real Estate Finance and Economics*, and so on.