Managerial Incentives and R&D Investments: Are Protected Managers Risk-Takers?

Li-Yueh Chen, Sheng-Yung Yang, Yu-Fen Chen
E-mail: yfchen@mail.dyu.edu.tw

ABSTRACT

Literature regarding the impact of managerial incentives on firm's research and development (R&D) investments suggests that due to the riskiness of R&D activities, firms need to provide managerial incentives to encourage managerial discretion on corporate long-term investments of R&D. This paper focuses on the listed firms of Taiwan Securities Exchange and Taipei Exchange in the emerging market of Taiwan to investigate whether managerial discretion on R&D investments is associated with the incentive scheme of CEO compensations. Furthermore, this paper examines the moderating role of protection from the directors' and officers' (D&O) liability insurance. The results indicate that the listed firms in Taiwan simultaneously determine corporate R&D investments and CEO compensations. They reward their CEOs in compliance with their efforts on R&D investments and CEO compensation motivates CEOs to align their interests with firms' long-term investments on R&D. A further analysis supports that D&O liability insurance in Taiwan positively moderates the relationship between R&D investments and CEO compensation. It encourages CEOs to allocate resources on R&D activities and make CEO incentive contracts efficacious on corporate long-term investments.

Keywords: managerial incentive; CEO compensation; R&D investment; directors' and officers' (D&O) liability insurance.

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