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Delegation and Managerial Misreporting: The Role of Incentive Compensation Scheme and Trust in Superior

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Abstract

This study investigates determinants of managers' misreporting behaviour. Misreporting in this study is defined as managers' action of withholding or misrepresenting information to their superior for their own benefit. Specifically, this study examines the relationship between delegation of decision rights and incentive compensation scheme on manager's misreporting behaviour. Furthermore, this study examines the mediating role of incentive compensation scheme on the relationship of delegation of decision rights on manager's misreporting behaviour. In addition, this study explores the potential informal control of trust in superior in deterring delegated managers engaging in misreporting behaviour. The results from a survey of 145 managers who reside in U.S. show that delegation of decision rights affect manager's misreporting behaviour directly and indirectly through incentive compensation scheme. Moreover, the results show that trust in superior negatively moderates the relationship between delegation of decision rights and manager's misreporting behaviour, indicating that high trust in superior can be used as informal control to deter managerial misreporting behaviour.

Keywords: Delegation of Decision Rights; Incentive Compensation Scheme; Manager's Misreporting Behaviour; Trust in Superior

1. Introduction

It is difficult for top management in modern organisation to make operation decision on a daily basis. Organisations to some extent need to delegate their decision making to their lower-level managers to make the decision making up-to-date and can tackle problems on a daily basis (Garrison et al., 2017). Delegation can be defined as transferring the authority to undertake specific decision-making activities to an individual

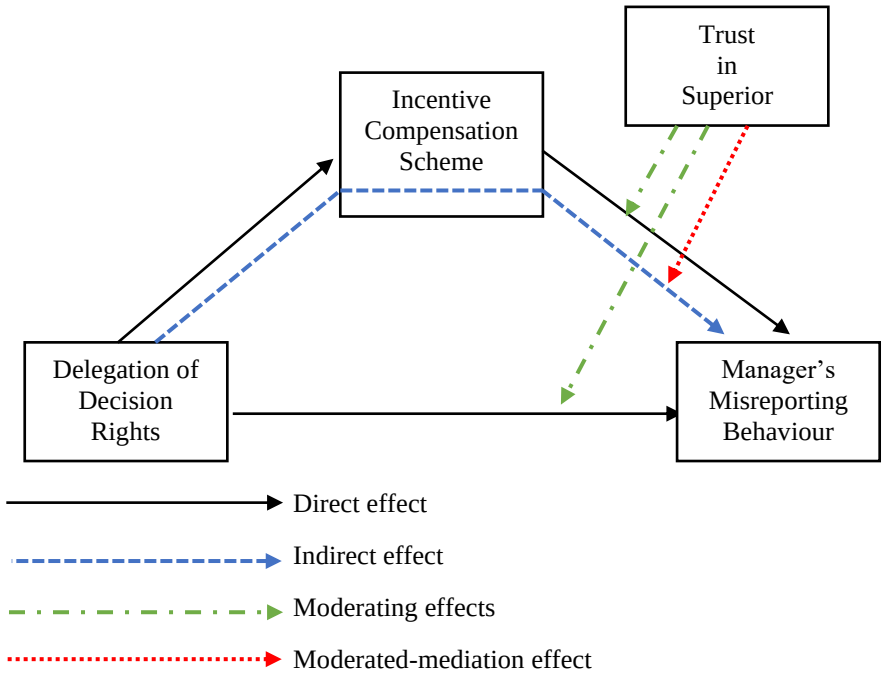
(Chong & Wang, 2019; Nagar, 2002). Numerous studies have documented the positive effect of delegation of decision rights such as increase in organisation's efficiency (Jensen & Meckling, 1995), improving organisational performance (Abernethy, Bouwens & van Lent, 2004), and reducing information gathering cost (Bushman, Indjejikian & Smith, 1995; Melumad & Reichelstein, 1987). Despite the positive effect, delegation of decision rights has a potential negative effect. This negative effect can occur when delegated managers abuse their authority and engaging in opportunistic behaviour. Principals in dealing with the potential negative effect of delegation attempt to design an incentive compensation scheme to realign the behaviour of self-interest agents. Nagar (2002, p.379) poses a question of 'how to design incentive compensation to ensure that these employees do not misuse their discretion?'. Indeed, organisations need to enhance their understanding of how to design a control system that can prevent fraud and/or misreporting (Church, Hannan & Kuang, 2014; Maas & Van Rinsum, 2013; Murphy & Dacin, 2011). This study focuses on internal managerial reporting which involves information to facilitate manager's decision making.

Classical agency theory posits that principal can use incentive contract to align agent's interest with organisation's interest. Indeed, incentive compensation can discourage manager's opportunistic behaviour, stimulate behaviours that optimise shareholders' value and increase individual's and organisation's performance (Chong & Eggleton, 2007; Gomez-Mejia, Tosi & Hinkin, 1987; Jensen & Murphy, 1990). Moreover, Cardinaels and Yin (2015, p.990) note that 'incentives may reduce information misrepresentation when agents value both pro-social behavior (i.e., honesty) and pecuniary gains'. In general, most people are intrinsically honest and assume that there is a cost that must be covered that associated with lying. Despite the positive effect of incentive compensation scheme, there are numerous studies that documented the positive relationship between incentive compensation scheme and manager's opportunistic behaviour (e.g., Bruner et al., 2008; Healy, 1985; Ittner, Larcker & Randall, 2003; Cardinaels & Jia, 2016). For example, Healy (1985) suggest that incentive compensation scheme induce managers to engage in earnings management. In addition, Cardinaels and Jia (2016) indicate that the use of incentive compensation scheme leads to increase in misreporting. Taken together, these evidence suggest that the relationship between incentive compensation scheme and manager's misreporting behaviour is unclear.

In addition to the investigation of the relationship between the extent of delegation of decision rights and incentive compensation scheme on manager's misreporting behaviour, this study investigates the role of trust in superior as a potential informal control. Trust in superior refer to subordinates' belief that their superior is a benevolent person and will not take advantage of them (Chong & Ferdiansah, 2011). De Cremer et al. (2001) suggest that trust mitigates the conflict of interest amongst people in the organisation. Indeed, when people trust each other, they are willing to help and work together to achieve common goal (Zand, 1997). Thus, it is expected that trust in superior could moderate the relationship between the extent of delegation of decision rights and incentive compensation scheme on manager's misreporting behaviour.

A theoretical model is developed for this study (see Figure 1). It is posited that the extent of delegation of decision rights is associated with manager's misreporting behaviour. Furthermore, it is predicted that the extent of delegation of decision rights is associated with incentive compensation scheme and that incentive compensation scheme is associated with manager's misreporting behaviour. Moreover, this study predicts that incentive compensation scheme mediates the relationship between delegation of decision rights and manager's misreporting behaviour. In addition, this study predicts that trust in superior to moderate the relationships between (i) the extent of delegation of decision rights and manager's misreporting behaviour and (ii) incentive compensation scheme and manager's misreporting behaviour. Finally, this study predicts that trust in superior conditionally affect the direct and indirect effect of the extent of delegation of decision rights on manager's misreporting behaviour through incentive compensation scheme.

Figure 1. Theoretical Model



One hundred and forty-five middle level managers employed in various US manufacturing firms completed an online survey. The results suggest that the extent of subordinate's trust in superior functions as a moderator, weakening the positive relationship between the extent of delegation of decision rights and manager's misreporting behaviour. Specifically, the interaction between the extent of delegation of decision rights and the extent of subordinate's trust in superior results in negative and significant association with manager's misreporting behaviour.

This study has several contributions. First, the findings of this study provide evidence of indirect effect of the extent of delegation of decision rights on manager's misreporting behaviour through incentive compensation scheme. Specifically, incentive compensation scheme acts as mediating factor in the relationship between delegation of decision rights and manager's misreporting behaviour, supporting the previous literature on the positive relationship between the extent of delegation of decision rights and incentive compensation scheme on manager's misreporting behaviour (Chong & Wang, 2019).

Second, the results suggest that the positive relationship between the extent of delegation of decision rights and manager's misreporting

behaviour is stronger when subordinate's trust in superior is low, indicating that a high trust in superior can deter managers engaging in misreporting behaviour when managers are delegated with higher decision rights. Organisation can cultivate trust in superior and use it as an informal control against manager's opportunistic behaviour such as misreporting.

The remainder of the paper is organised as follows. Section 2 develops the study's hypotheses. Section 3 describes the research method, and section 4 presents the results. Section 5 discusses the findings, the implications and limitations of the study, and the future research opportunities.

2. Theory and Hypotheses Development

2.1. Delegation of Decision Rights and Manager's Misreporting Behaviour

One of the ways for principal to benefit from relevant information possessed by his/her agents is by delegating the authority to make a decision to his/her agents (Melumad & Reichelstein, 1987). Delegation is defined by Leana (1987, p.228) as 'a process whereby the manager transfers decision-making authority to subordinate.' Even though managers may benefit from delegating authority to subordinate, it also has a downside. Agency theory posits that delegation of authority could induce conflict of interest between managers and subordinates. Delegated subordinates are assumed to act in the best interest of the organisation (i.e., principal) but in reality act to maximize their own self-interest (Jensen & Meckling, 1976). The subordinates are incentivised by the opportunity from having authority to obtain what they believe as a fair compensation for the risk and added effort that the managers expect them to bear (Alchian & Woodward, 1988). This claim is supported by anecdotal and empirical evidence. For example, Ittner et al. (2003) find that managers who are motivated by reward may maximize their reward by engaging in opportunistic behaviour where they increase their short-term financial results at the expense of the firm's long-run performance. Locke and Schweiger (1979) suggest that delegation emphasizes subordinate's autonomy in making decision. Thus, it is fair to assume that delegation of decision right provides the opportunity for subordinate to engage in opportunistic and unethical behaviours.

This study investigates the effect of delegation of decision rights on managerial misreporting behavior under the agency framework. Misreporting can be defined as managers' action to withhold or misrepresent information (Chong & Wang, 2019; Keil & Robey, 2001). The literature shows that managers who misreport can gain additional resources or obtain compensation based on their performance (e.g., Brüggen & Luft, 2011; Mass & Van Rinsum, 2013). In the context of this study, delegated managers could profit themselves by abusing their authority and engaging in unethical behavior. Chong and Eggleton (2007) indicate that delegated managers may be reluctant to share their private information truthfully to their superiors. Thus, delegating the decision rights to managers can be problematic since managers can misreport their performance targets to get bonus, gain more resources or exert less effort. Thus, this study predicts that delegation of decision rights is positively

associated with managers' misreporting behavior. The formal hypothesis is as follow:

H1: the extent of delegation of decision rights is positively associated with the extent of manager's misreporting behavior.

2.2. Delegation of Decision Rights and Incentive Compensation Scheme

Incentive compensation scheme is normally used by an organisation to align delegated agent's interest towards organisation interest. Incentive compensation scheme can be defined as a bonus and/or a profit sharing used by an organisation as part of the payment packages (Balkin & Gomez-Mejia, 1990). Theoretical studies in accounting research have formalized the nature of relationship between delegation and incentive compensation scheme (Baiman & Rajan 1995; Bushman et al., 1995; Melumad, Mookherjee & Reichelstein, 1992; Melumad & Reichelstein, 1987). Furthermore, empirical accounting studies have documented the relationship between delegation of decision rights and incentive compensation scheme (e.g., Chong & Wang, 2019; Evans, Kim & Nagarajan, 2006; Foss & Laursen, 2005; Gong & Ferreira, 2014; Nagar, 2002; O'Connor, Deng & Luo, 2006; Prendergast, 2000). These studies find that incentive compensation scheme is necessary to align agents' interest with the organisation's interest when the agents are given an authority to make decisions. Thus, this study predicts that delegation of decision rights is positively associated with incentive compensation scheme. Stated formally, the hypothesis is as follow:

H2: The extent of delegation of decision rights is positively associated with incentive compensation scheme.

2.3. Incentive Compensation Scheme and Misreporting

Prior studies find mix evidence on the relationship between incentive compensation scheme and misreporting. Some studies find a negative association between incentive compensation scheme and misreporting (e.g., Evans et al., 2001; Gong & Ferreira, 2014; Nagar, 2002; Tayler & Bloomfield, 2011). On the other hand, other studies find that incentive compensation scheme has a positive association with misreporting. Previous studies suggest that when managers' compensations link with their performance measure, they are more likely to encounter

dysfunctional behaviour such as propensity to create slack (e.g., Dunk, 1993, Hobson, Mellon & Stevens, 2011; Lau & Eggleton, 2003; Merchant, 1990) and misreporting (e.g., Chong & Wang, 2019; Church, Hannan & Kuang, 2012; Hannan, Rankin & Towry, 2006; Mayhey & Murphy, 2014; Murphy, 2012). In addition, Jensen (2003) contends that pay-for-performance triggers managers to 'play with the numbers' and destroy the value of their organisation.

In spite of the conclusive findings, this study focuses on the negative consequences of incentive compensation scheme. Using agency theory framework, this study posits that when managers' compensation tied with their ability to achieve their target, they are more likely to withhold or even falsify their private information to their superior in order to get their compensation (Jensen, 2003). Consequently, incentive compensation scheme would induce managers to engage in misreporting behaviour. Thus, the formal hypothesis is stated as follow:

> H3: Incentive compensation scheme is positively associated with manager's misreporting behaviour.

2.4. The Mediating Role of Incentive Compensation Scheme on the Relationship between Delegation of Decision Rights and Manager's Misreporting Behaviour

As discussed in section 2.2, it is posited that delegation of decision rights is positively associated with incentive compensation scheme, and as discussed in section 2.3, incentive compensation scheme is expected to be positively associated with manager's misreporting behaviour. Taken together, it is expected that incentive compensation scheme mediates the relationship between delegation of decision rights and manager's misreporting behaviour where delegating decision authority increases the use of incentive compensation scheme which in turn, increases manager's misreporting behaviour. Thus, the following hypothesis is proposed.

> H4: The relationship between delegation of decision rights and manager's misreporting behaviour is mediated by incentive compensation scheme.

2.5. The Concept of Trust in Superior

Trust is defined as "the willingness of a party to be vulnerable to the action of another party based on the expectation that the other will

perform a particular action important to the trustor, irrespective of the ability to monitor or control that other party" (Mayer, Davis & Schoorman, 1995, p.712). Similarly, Chong and Ferdiansah (2011) state that trust in superior is a condition where subordinates have faith that their superior will not take advantage of them. Furthermore, Fulk et al. (1985) suggest that trust in superior means that subordinates can openly discuss their job-related problems without being fear of negative reaction from their superior. It has been found that trust foster healthy teamwork, enhances communication, cooperation, and positive attitudes as well as facilitates organizational citizenship behaviour (OCB) (e.g., De Jong, Dirks & Gillespie, 2016; Dirks & Ferrin, 2001; Podsakoff et al., 1990).

De Cremer et al. (2001) suggest that when people trust each other, it reduces conflict of interest among them. Furthermore, the trust literature had shown that the relationship building around trust condition is more effective and pleasant (e.g. Dirks, 1999; Kramer, 1999). In the context of this study, a delegated manager would pursue his/her personal interest under the agency theory framework. However, if the delegated manager has a trust in his/her principal (e.g. the superior), the delegated manager would be reluctant to make action that could harm the trustor. The reason behind this is because if someone trust others he/she will took into account the trustor's interest into his/her action. Furthermore, a delegated manager does not want to be seen as trust violators by someone he/she trust (i.e. his/her superior) by doing opportunistic behaviour such as misreporting (Cressey, 1950, 1953). Thus, it is posited that a manager who trust his/her superior would refrain herself/himself from conducting misreport.

2.6. The Moderating Role of Trust in Superior on the Relationship of Delegation of Decision Rights and Manager's Misreporting Behaviour

As discussed in section 2.1, delegation of decision rights is predicted to be positively associated with manager's misreporting behavior. Furthermore, this study posits that the relationship between delegation of decision rights and manager's misreporting behavior is moderated by trust in superior. As discussed in section 2.5, trust in superior is defined as 'subordinates' belief that superior is reliable and will not take advantage of them' (Chong & Ferdiansah, 2011, p.57). Indeed, when subordinates trust their superior they feel protected and do not hesitate to disclose their private information to their superior (Read, 1962). In addition, Zand (1997) suggest that when people trust someone they will

be willing to help and work together with people that they trust to achieve common goal.

Studies in management and accounting suggest that when subordinates trust their superior they feel less stress about their job (Lau & Buckland, 2001; Lau & Tan, 2006) and more committed to their organisation (Chong & Law, 2016; Locke, Latham & Erez, 1988; Maiga & Jacobs, 2007). Furthermore, De Cremer et al. (2001) indicate that trust can mitigate the conflict of interest that happen in the organisation. When member of the organisation trust each other, they will work toward common goal believing that others will not take advantage of them and will also act for the sake of the organisation (De Cremer et al., 2001; Dirks, 1999). Thus, when delegated managers have a high trust in their superior, presumably they will refrain themself to do action (e.g., misreporting) that is harmful to their organisation. Thus, the following hypothesis is proposed:

> H5: The relationship between the extent of delegation of decision rights and manager's misreporting behaviour is moderated by the extent of subordinate's trust in superior such that the positive relationship between delegation of decision rights and manager's misreporting behaviour is weak (strong) when the extent of subordinate's trust in superior is high (low).

2.6. The Moderating Role of Trust in Superior on the Relationship of Incentive Compensation Scheme and Manager's Misreporting Behaviour

Hypothesis 3 predicts that incentive compensation scheme is positively associated with manager's misreporting behaviour. Findings from prior literature suggest that incentive compensation scheme provides a reason that motivate managers engaging in misreporting (e.g., Chong & Wang, 2019; Church et al., 2012; Hannan et al., 2006; Mayhew & Murphy, 2014; Murphy, 2012). This study contends that the extent of subordinate's trust in superior can moderates this relationship.

As previously discussed, when subordinates trust their superior they will commit to their organisation and willing to help and work together with people that they trust. (Chong & Law, 2016; Locke et al., 1988; Maiga & Jacobs, 2007; Zand, 1997). Zand (1997) suggests that two people that trust each other will help each other and work cooperatively, such as sharing information, to provide constructive solution for their problem. Thus, when subordinates have high trust in their superior it is

unlikely that they will engage in opportunistic behaviour such as misreporting. this is because the subordinates do not want to be seen as a trust violator (Cressey, 1950, 1953). Hence, the formal hypothesis is stated as follow:

> H6: The relationship between incentive compensation scheme and manager's misreporting behaviour is moderated by the extent of subordinate's trust in superior, such that the positive association between incentive compensation scheme and manager's misreporting behaviour is weak (strong) when the extent of subordinate's trust in superior is high (low).

2.7. Moderating Role of Trust in Superior on the Indirect Effect of the Delegation of Decision Right on Manager's Misreporting Behavior Through Incentive Compensation Scheme

As discussed in section 2.4, it is expected that the relationship between delegation of decision rights and manager's misreporting behaviour is mediated by incentive compensation scheme (i.e., H4). It is also predicted that the extent of subordinate's trust in superior moderates the relationship between incentive compensation scheme and manager's misreporting behaviour (i.e., H6). Thus, combining H4 and H6 will leads to a moderated-mediation hypothesis (Hayes, 2017). This model is also known as conditional indirect model (Hayes & Preacher, 2013; Preacher, Rucker, & Hayes, 2007). It is predicted that the indirect effect of the delegation of decision rights on manager's misreporting behaviour will be moderated by trust in superior. Thus, the formal hypothesis as follows:

> H7: The indirect relationship between the extent of delegation of decision rights and manager's misreporting behaviour is moderated by trust in superior, such that the indirect effect of the delegation of decision rights on manager's misreporting behaviour through incentive compensation scheme is stronger (weaker) when the extent of subordinate's trust in superior is low than when trust in superior is high.

3. Research Method

3.1. Data Collection and Sample

An international research online provider was used to collect data for this study. the use of online-based services to recruit participants had been increasing from 200 to 2012 (see Brandon et al., 2014). It is

suggested that people tend to respond to an online survey than a paper-based survey and there is no difference in term of the data quality between online and paper-based survey methods (Croteau, Dyer & Miguel, 2010; Deutskens, de Ruyter & Wetzels, 2006). An invitation letter with a survey attached was sent by Qualtrics to its relevant online panel members. The invitation letter informed that participants' involvement in this survey were voluntary. Nevertheless, a small monetary incentive was offered by Qualtrics for those participants who completed the survey.

Some criteria for sample inclusion are established to ensure participants' suitability for this study. First, participants are middle-level managers to ensure that participants have and experience some level of delegation of decision right. Second, the participants must work in manufacturing companies with at least one hundred employees. This criterion is to control companies' characteristics and ensures that the companies are big enough to implement a formal accounting system. Furthermore, this criterion is to provide some control over company size in my sample.

A Pre-test was set for the survey instrument and was sent to 16 participants. Based on the response from 16 participants, minor modifications were made to the demographic questions of the instrument. The instrument then distributed to 1,929 online panel members in the U.S. the participants were given 13 days to complete the survey. The initial screening of the survey resulted in 1,500 unqualified samples being dropped (77.76% drop-out rate).

Furthermore, there were 274 incomplete surveys excluded from the sample. Consequently, 155 completed responses were collected from the remaining participants. Further examination of participants' identification (I.D.) and their internet protocol (I.P.) address suggested that there were no multiple responses from the same participants. Outlier analysis was conducted based on age, number of employees, tenure, and experience using the Statistic Package for Social Science (SPSS). The results of the outlier analysis suggest that there is one participant based on age, five participants based on the number of employees, two participants based on tenure, and two participants based on experience were indicated as outliers. Hence, these ten participants were excluded from the sample resulting in a final sample of 145. Table 1 presents the demographic information of our sample.

Table 1. Demographic Information, Type of Industries/Sectors, and Functional Areas

Panel A: Demographic Information of Participants and Organizations				
	Mean	***Standard Deviation***	***Minimum***	***Maximum***
Tenure (Exp.1)	7.77	4.68	1	22
Experience (Exp.2)	10.16	6.05	1	29
Number of Employees in Organization	1,994.30	3,795.31	100	28,000
Age	43.18	11.33	22	73
Gender			***Number***	***Percentage***
Female			36	24.83
Male			109	75.17
Panel B: Type of Industries/Sectors				
	Number		***Percentage***	
Automotive	10.00		6.90	
Building and Construction	33.00		22.76	
Food and Beverage	13.00		8.97	
Furniture, Cabinets, and Joinery	5.00		3.45	
Pharmaceutical and Health Technologies	9.00		6.21	
Textiles, Clothing, and Footwear	8.00		5.52	
Electronic and Computing	33.00		22.76	
Other*	34.00		23.45	

Panel C: Type of Functionals Areas (Departments) in the Organizations		
	Number	***Percentage***
Accounting and Finance	11.00	7.59
Research and Development	13.00	8.97
Design of Product and Process	5.00	3.45
Production	42.00	28.97
Marketing	7.00	4.83
Sales	8.00	5.52
Distribution	2.00	1.38
Customer Services	7.00	4.83
Human Resources	10.00	6.90
Information Technology	34.00	23.45
Other**	6.00	4.14

* Eleven participants work in the process manufacturer industry, eight participants work in Information and Technology industry, and the other work at metal, heavy equipment, magazines, plastic, roadworks products, chemical, packaging, and aerospace products.

** One participant does not specify which department s/he works, while the other participants work at/as general manager, operation, engineering, quality control, manufacturing, and purchasing departments.

Table 1 shows that my participants have an average age of 43.18 years old and consist of 36 female (24.83%) and 109 male (75.17%). On average, the participants have working experience of 10.16 years and average tenure of 7.77 years.

3.2. Variable Measurement

To enhance the validity and reliability of the variable used in this study, this study relies on established variable instruments that had been used by previous studies. Following suggestion from Nunnally (1978),

this study uses explanatory factorial analysis and Cronbach's alpha to measure the construct validity and the reliability of the instruments. A factorial analysis is conducted for each instrument to determine whether the instruments are unidimensional as an indication of good internal validity. Moreover, the consistency of each instrument is assessed using Cronbach's alpha which will indicate the reliability of each instrument (Cronbach, 1951). In addition, as suggested by Fornell and Larcker (1981), this study employs composite reliability as an additional examination for internal reliability of the instruments. Furthermore, average variance extracted (AVE) is used to further probe the internal validity of the instruments (Xu et al., 2012). As shown in Table 2, the composite reliability ranges from 0.90 (misreporting) to 0.93 (delegation of decision rights) indicating that all instruments have satisfactory internal reliability. Xu et al. (2012, p.213) note that 'to ensure the construct validity, the items within one construct should demonstrate a relatively high correlation (convergent validity) whereas the items from different constructs should be characterized by low correlation (discriminant validity).

Table 2 shows that all instruments have AVE scores above 0.50 which indicate a strong convergent validity within each instrument (Chin, 1998; Hair et al., 1998)[1]. Moreover, as an additional examination of discriminant validity, the square roots of AVE of each instrument are computed and compared with the correlation among the latent variables (Chin, 1998; Fornell & Larcker, 1981). The results from Table 3 show that the square roots of the AVE statistics for each instrument are greater than its correlation with other instruments in the model, suggesting strong discriminant validity among the instruments. The next section discusses the measurement of each variable.

[1] We compute average variance extracted (AVE) manually using the following formula (Malhotra & Dash, 2016):

$$AVE = \frac{\sum_i^n L_i^2}{n}$$

Where:
L = factor loading
n = number of indicators

Table 2. Descriptive Statistics, Factor Loading, Cronbach's Alpha, Composite Reliability, and AVE

		Mean	*Standard Deviation*	*Factor Loading*	*Cronbach's Alpha*	*Composite Reliability*	*AVE*
	Delegation of Decision Right (DDR)	5.28	1.41		0.91	0.92	0.64
DDR1	The hiring and firing of personnel			0.77			
DDR2	Staff promotion			0.76			
DDR3	Setting the operating hours			0.79			
DDR4	Setting the budget			0.88			
DDR5	Spending items in the budget			0.84			
DDR6	Spending items outside the budget			0.86			
DDR7	Development of new products, projects, and/or services			0.70			
	Incentive Compensation Scheme (ICSi)	5.30	1.13		0.88	0.91	0.76
ICSi1	Pay incentives such as a bonus or profit-sharing are an important part of the compensation package in my organization			0.70			
ICSi2	Pay incentives are designed to provide a significant amount of an employee's total earnings in my organization			0.76			
ICSi3	We have a strong commitment to distribution rewards based upon contributions to the organization			0.78			
ICSi4	In this organization, a portion of an employee's earnings is contingent upon divisional profitability being achieved			0.76			

ICSi5	We designed our compensation system so that a substantial portion of our compensation cost is variable pay in the form of incentives, bonuses, or related rewards			0.85			
ICSi6	Divisional profitability is used as a criterion for pay decisions and aggregate incentive programs (e.g. gainsharing, profit sharing) for employees			0.76			
ICSi7	Bonuses are often provided; the frequency of bonuses is viewed at least as important as their magnitude			0.77			
	Trust in Superior (TSPV)	4.03	0.85		0.90	0.93	0.71
TSPV1	I am confident that my supervisor will always care about my personal needs at work			0.82			
TSPV2	If I shared my problems with my supervisor, I know (s)he would respond with care			0.86			
TSPV3	I am confident that I could share my work difficulties with my supervisor			0.83			
TSPV4	I am sure I could openly communicate my feelings to my supervisor			0.84			
TSPV5	I feel secure with my supervisor because of his/her sincerity			0.87			
	Misreporting (MR)	3.93	1.62		0.87	0.90	0.81
MR2	Of the total amount of information (e.g., financial and nonfinancial information) you receive, how much of it must be actively changed in some way before share or pass on to your supervisor?			0.69			

MR3	There are significant forces that cause me to modify information in some of my communication to my superior	0.72
MR4	which you feel most accurately describe your own behavior when you are at work: - How frequently do you find it necessary to alter the content of your progress reports to fit the expectations of your superior?	0.88
MR5	which you feel most accurately describe your own behavior when you are at work: - About how often during a typical work week do you withhold information from your superior that might be useful to him/her?	0.88
MR6	which you feel most accurately describe your own behavior when you are at work: - How frequently do you find it necessary to omit particular facts from the information you share/pass on to your superior?	0.86

Table 3 The Pearson Correlation Matrix and Square Roots of the AVEs (N=145)

	MR	***DDR***	***ICSi***	***TSPV***	***Gender***	***Age***	***Tenure (Exp.1)***	***Experience (Exp.2)***
MR	(0.89)							
DDR	0.55**	(0.80)						
ICSi	0.51**	0.69**	(0.88)					
TSPV	0.18*	0.37**	0.39**	(0.85)				
Gender	0.19*	0.21*	0.05	0.06	N/A			
Age	-0.37**	-0.21*	-.289**	-0.08	0.09	N/A		
Tenure (exp.1)	-0.26**	-0.11	-0.14	-0.08	0.04	0.63**	N/A	
Experience (exp.2)	-0.10	0.03	0.05	0.09	0.04	0.46**	0.68**	N/A

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

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

3.2.1 Delegation of Decision Right

The delegation of decision right's instrument was adopted from Chong and Wang (2019), Nagar (2002), and O'Connor et al., (2006). The delegation was measured using a seven-item, seven-point Likert type anchored from 1 "not at all" to 7 "a very large extent". The result of factor analysis showed that the delegation of decision right construct had a total variance explained of 64.31% indicating a unidimensional nature of the construct. Furthermore, the Cronbach alpha coefficient (Cronbach, 1951) was 0.91 indicating very high internal reliability for the scale (Nunnally, 1978).

3.2.2 Incentive Compensation Scheme

The incentive compensation scheme instrument was adopted from Balkin & Gomez-Mejia (1990) and Gomez-Mejia et al. (1987). The incentive compensation scheme instrument was measured using a seven-item, seven-point Likert type anchored from 1 "strongly disagree" to 7 "strongly agree". Factor analysis showed the unidimensional nature of

the construct. The factor analysis yielded a total variance explained of 58.78%. In addition, the Cronbach alpha coefficient was 0.88 indicating a strong internal reliability for the scale (Nunnally, 1978).

3.2.3 Trust in Superior

The trust in superior instrument was adapted from Read (1962). The trust in superior instrument was measured using a four-item, seven-point Likert type anchored from 1"to a very little extent" to 7"to a very large extent". The instrument had a unidimensional nature as shown by the total variance explained of 71.44%. Furthermore, the Cronbach's alpha coefficient was 0.90 indicating a strong internal validity of the construct.

3.2.4 Misreporting

The misreporting instrument consisted of six items, a seven-point Likert-scale. The instrument was derived from Roberts and O'Reilly (1974), Fulk and Mani (1986), and Smith et al., (2009). The initial factor analysis showed that the total variance of the construct was 55.21%, with five of the items (MR2 to MR6) loaded above 0.50. MR1 item had a low factor loading score (0.23), hence the MR1 item was excluded from the construct. The second factor analysis (MR2-MR6) results showed the total variance of 65.51% and all five items loaded above 0.50 on a single factor. The Cronbach's alpha coefficients was 0.86 suggesting a strong internal validity of the misreporting scale.

3.2.5 Control Variables

The following four control variables was included in the study: age, gender, tenure, and current working experience. Tenure was measured as the participants work in their current employer. The current working experience was measured as the participants' time in their current position.

4. Results

PROCESS version 3.5 is used in this study to analyse the data. It is a tool embedded in Statistical Package for the Social Science (SPSS), which initially develop by Hayes (2017)[2]. PROCESS not only allows to test the simple direct association hypotheses (i.e., H1, H2, and H3), it also enables to test simple mediation hypothesis (i.e., H4) and simple

[2] Before conducting analysis, all independent variables were mean-centered to ensure the direct interpretation of the regression coefficient of the main effect can be done in term of the original variables (Dawson, 2014)

mediation hypotheses (i.e., H5 and H6) as well as moderated-mediation hypothesis (i.e., H7).

In this study, common method bias could exist due to the use of the same participants that provide all responses to a set of survey items (Podsakoff et al., 2003). To ensure that the data do not suffer from common-method bias problem, Harman's one-factor test is employed using procedures suggested by Podsakoff and Organ (1986). A principal component analysis is conducted using SPSS by entering all the model's principal constructs. The principal component analysis yields four-factor solution using the eigenvalue greater than one criterion. the factor analysis of the four factors accounts for 66.76% of the variances. The first factor accounts only for 39.48%. Since there is no single factor that dominantly explains the variances, it can be concluded that the data does not suffer from common-method bias (Podsakoff & Organ, 1986; Widener, 2007)

4.1. Hypotheses testing

Hypothesis 1 states that delegation of decision rights has a positive and significant association with misreporting. Table 4 Panel A shows that the coefficient of the relationship of delegation of decision rights and misreporting is positive and significant (0.275, t-value=2.334, $p<0.05$) indicating that H1 is supported.

Table 4. Results for Moderated Mediation[a]

Panel A: Regression Results

	Coefficients	***Standard error***	***t-Value***	***p-Value***	***L.L. 95% CI***	***U.L. 95% CI***
Incentive Compensation Scheme (ICSi)						
DDR	0.528	0.050	10.575	0.013	0.430	0.628
Control Variables						
Gender	-0.180	0.158	-1.142	0.255	-.0495	0.132
Age	-0.018	0.008	-2.363	0.019	-0.034	-0.003
Tenure (Exp.1)	-0.011	0.017	-0.622	0.535	-0.045	.023

Experience (Exp.2)	0.039	0.019	1.985	0.049	0.000	0.077
$R^2 = 0.523$, $p < .001$						
Misreporting (MR)						
DDR	0.275	0.118	2.334	0.021	0.042	0.509
ICSi	0.493	0.152	3.235	0.002	0.191	0.794
TSPV	-0.217	0.145	-1.494	0.138	-0.504	0.070
DDR x TSPV	-0.286	0.100	-2.852	0.005	-0.484	-0.088
ICSi x TSPV	0.181	0.116	1.557	0.122	-0.049	0.412
Control Variables						
Gender	0.459	0.251	1.829	0.069	-0.037	0.956
Age	-0.029	0.013	-2.395	0.018	-0.055	-0.005
Tenure (Exp.1)	-0.032	0.028	-1.151	0.252	-0.088	0.023
Experience (Exp.2)	0.007	0.032	0.204	0.838	-0.056	0.069
$R^2 = 0.444$, $p < .001$						

Panel B: Conditional Direct Effect of Delegation of Decision Rights on Misreporting at Three Levels of Trust in Superior

	Direct Effect	***Bootstrap S.E.***	***t-Value***	***p-Value***	***L.L. 95% CI***	***UL 95% CI***
-1 SD (-0.851)	0.518	0.124	4.199	0.000	0.274	0.763
Mean (0.000)	0.275	0.118	2.334	0.021	0.042	0.509
+1 SD (0.851)	0.032	0.165	0.196	0.845	-0.293	0.358

Panel C: Conditional indirect effect of delegation of decision rights on misreporting through incentive compensation scheme at three levels of trust in superior

	Indirect effect	*Bootstrap SE*	*L.L. 95% CI*	*U.L. 95% CI*
-1 SD (-0.851)	0.179	0.087	0.044	0.385
Mean (0.000)	0.261	0.097	0.088	0.462
+1 SD (0.851)	0.342	0.143	0.048	0.616

Panel D: Index of moderated mediation

	Index	*Bootstrap SE*	*L.L. 95% CI*	*U.L. 95% CI*
TSPV	0.096	0.080	-0.104	0.219

Notes: L.L.: lower limit; CI: confidence interval; U.L.: upper level; SD: standard deviation; S.E.: standard error; DDR: delegation of decision rights; DP: displacement of responsibility; W.B.: whistleblowing mechanism.

All the independent variables are mean-centered when the analyses conducted

[a]Bootstrap sample size = 5,000

Hypothesis 2 posits that delegation of decision rights has a positive and significant association with incentive compensation schemes. The results in Table 4 Panel A show that the coefficient of the relationship between delegation of decision rights and incentive compensation schemes is positive and significant (0.528, t-value=10.574, $p<0.05$). Hence, the result provides support for the positive association between delegation of decision right and incentive compensation schemes.

Hypothesis 3 predicts that incentive compensation schemes have a positive and significant association with misreporting. The results in Table 4 Panel A show that the coefficient of the relationship between incentive compensation schemes and misreporting is positive and significant (0.4983, t-value=3.235, $p<0.01$). Thus, H3 is supported.

Hypothesis 4 contends that the relationship between delegation of decision rights and misreporting is mediated by incentive compensation

schemes. Sobel test and bootstrapping approach are used to test whether hypothesis 4 supported[3]. Table 5 Panel A and Panel B show the Sobel test and the bootstrapping approach results respectively.

Table 5. Results of Simple Mediation Effect[a]

Panel A: Sobel Test of Indirect Effect				
	Indirect Effect	***SE***	***Z***	***p-Value***
Path: DDR - ICSi - MR	0.197	0.078	2.514	0.012
Panel B: Bootstrapping Approach of indirect effect				
	Indirect Effect	***SE***	***L.L. 95%CI***	***U.L. 95%CI***
Path: DDR - ICSi - MR	0.197	0.089	0.037	0.392

Notes: DDR: delegation of decision rights; ICSi: Incentive compensation scheme; MR: misreporting; L.L.: lower limit; CI: confidence interval; U.L.: upper limit; SE: standard error

[a]Bootstrap sample size = 5,000

The results in Panel A of Table 5 show that the coefficient of the indirect effect of incentive compensation scheme on the relationship between delegation of decision right and misreporting is positive and significant (indirect effect = 0.197, z = 2.514, $p<0.05$) suggesting H4 is supported. Moreover, the results of bootstrapping approach in Panel B of Table 5 show that the mediating role of incentive compensation scheme on the relationship between delegation of decision right and misreporting is statistically significant since the bootstrap confidence level does not straddle zero ((indirect effect = 0.197, 95% CI = 0.037 to 0.392). taken together, the results provide support for the mediating role of incentive compensation scheme on the relationship between delegation of decision right and misreporting.

Hypothesis 5 posits that trust in superior moderates the relationship between delegation of decision right and misreporting, such that the

[3] Preacher and Hayes (2008, p. 886) suggest that "bootstrapping provides the most powerful and reasonable method of obtaining confidence limits for specific indirect effect under most condition."

interaction between trust in superior interaction and delegation of decision rights negatively affect misreporting. the results shown in Table 4 Panel A indicate that the moderation effect of trust in superior on the relationship between delegation of decision right and misreporting is negative and significant (DDR x TSPv = -0.286, p =0.005, 95% CI = -0.484 to -0.088). Thus, H5 is supported.

Hypothesis 6 predicts that trust in superior will interact with incentive compensation scheme and negatively affect misreporting. the results in Panel A Table 4 show that the interaction between incentive compensation scheme and trust in superior is positive but not significant (0.181; p = 0.122; 95% CI = -0.049 to 0.412). Thus, Hypothesis 6 is not supported.

Hypothesis 7 predicts that the delegation of decision rights' indirect effect on misreporting through incentive compensation scheme is moderated by trust in superior. To test the moderated-mediation effect, Hayes's (2017) PROCESS Model 15 is employed on a bootstrap sample of 5000. The PROCESS analysis does not yield a statistically significant index of moderated mediation on a 95% confidence level (see Table 4. Panel D). Hence, hypothesis 7 is not supported.

5. Discussion and Conclusion

This study examines the relationship between the extent of delegation of decision rights and manager's misreporting behaviour by considering the mediating role of incentive compensation scheme. This study finds that the extent of delegation of decision rights is positively associated with manager's misreporting behaviour, consistent with previous study (Chong & Wang, 2019). The results further reveal that incentive compensation scheme plays a mediating role on the relationship between the extent of delegation of decision rights and manager's misreporting behaviour.

This study also examines the moderating effect of trust in superior as a form of informal control to deter misreporting behaviour. The results demonstrate that the extent of subordinate's trust in superior plays moderating role in the relationship between the extent of delegation of decision rights and manager's misreporting behaviour. Specifically, the results of this study reveal that high trust in superior negate the positive direct effect of delegation of decision rights on manager's misreporting behaviour which indicates that delegated managers are less likely to

misreport when they trust their superior. This result implies that trust in superior can be used by organisation as informal control to mitigate the problems that may arise from delegating decision rights to lower-level manager (i.e., misreporting behaviour). Organisation should try to cultivate subordinates' trust in superior by fostering an environment that conducive for building trust among members of the organization.

This study has several limitations. The sample of this study is drawn from middle-level managers in the manufacturing sector. Therefore, the generalization of the findings of this study should be restricted to similar types of organizations. Future research may explore other non-manufacturing sectors such as the financial services sector, public and non-profit organizations. Second, the use of survey scales is likely led to the higher mean value (i.e., high leniency error) and a restricted range (i.e., low variability error) in the observed scale (see Prien & Liske, 1962; Thornton, 1968). Third, the survey method can suffer from social-desirability bias if respondents provide answers that they believe are socially acceptable (Parker & Kyj, 2006; Randall & Fernandes, 1991). Future research should incorporate a social-desirability bias scale to address this issue (see Reynolds, 1982; Rudmin, 1999). Finally, my study relies on a cross-sectional survey method. Hence, the results do not confirm causal relationships. Thus, future studies can vary the findings of this study and rely on a different method, such as a longitudinal methodology to test the directions of causal relationships proposed in this study.

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