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Unconsolidated separate financial statements and dividends: Evidence from Korea

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Abstract

The purpose of this study is to investigate whether Korean parent firms manage dividend payments by taking advantage of the Commercial Act of Korea and accounting discretion allowed under the Korean IFRS. While IFRS adoption has transformed primary financial statements from unconsolidated to consolidated financial statements, the Commercial Act of Korea continues to compute distributable profits based on unconsolidated separate financial statements. The discrepancy between the earnings for financial reporting and the distributable profits provides an opportunity for a parent firm to manage dividends upward through internal transactions without affecting consolidated earnings. Using the parent firms listed on the Korea Exchange (KRX) during the period from 2001 to 2018, we examine whether these parent firms engage in dividend management through internal transactions to meet the dividend expectations of their shareholders in the post-IFRS period. We find that the parent firms with small consolidated but large unconsolidated earnings ('SCLU' firms) pay more dividends than others in the post-IFRS period when they have significant transactions with related parties. The dividend-increasing behavior of the SCLU firms through related-party transactions is more pronounced when the ownership of foreign shareholders or the largest shareholder is high. Our results suggest that Korean firms may pay excessive dividends by managing distributable profits despite poor consolidated performance in order to meet shareholders' dividend demands.

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1. Introduction

Dividends are the distribution of a firm's earnings to its shareholders, and the amount of dividends should be determined in consideration of both the firm and its shareholders. During the period of high economic growth, Korean listed firms maintained a low dividend payout ratio because they wanted to retain their earnings to respond to investment opportunities under external financing constraints (Park, Lee, & Lee, 2003). Investors also preferred capital gains to dividends. However, in recent years, corporate dividends have been increasing as investors' demand for dividends increases due to economic and social changes, including prolonged low economic growth, internationalization and institutionalization of investors, and accelerated ageing of the population. In addition, temporary tax incentives were implemented from 2015 to 2017 to encourage corporate dividend payments.

The dividend payout ratio of Korean firms is notably below the global or G7 average, contributing significantly to the phenomenon known as the "Korea discount." Policymakers, media, and researchers have

consistently pointed out the low dividends of Korean firms, and institutional investors have engaged in shareholder engagement activities calling for an increase in dividends. In this context, an increase in dividend payments may be well-received in the capital market and viewed as an increase in shareholder return. Nevertheless, there is concurrent criticism asserting that the increased dividends of Korean firms predominantly benefit foreign investors and/or controlling shareholders.

In this study, we focus on Korea's institutional environment, in which firms' dividend capacities are calculated based on financial statements that are not the main financial statements for external reporting. Korea adopted the International Financial Reporting Standards ('K-IFRS') in 2011 and forced listed parent firms to issue consolidated (separate) financial statements as primary (supplementary) financial statements.[1] Even when a parent firm reports small or negative consolidated earnings due to the poor performances of its subsidiaries, it can report large positive separate earnings under the cost method permitted byIFRS. In addition, a parent firm may manage separate earnings upward through internal transactions with its own subsidiaries, as the cost method does not eliminate the impact of these transactions. Hwang and Kang (2017) find an increase in the proportion of firms with different signs of consolidated and unconsolidated earnings following the adoption of K-IFRS. Distributable profits, however, continue to be determined based on unconsolidated, separate financial statements in accordance with the Commercial Act even after the IFRS adoption.[2] We look into whether and how Korean-listed parent companies handle dividends through internal transactions to meet the needs of their shareholders after IFRS. This is because the difference between the earnings reported for financial reporting and those used for dividends may cause companies to act in ways that take advantage of the situation.

For empirical analyses, we use listed parent firms that have prepared consolidated financial statements for the period from 2001 to 2018. To capture those firms that manage separate earnings upward for dividend purposes, we identify parent firms reporting small or negative consolidated earnings but large unconsolidated earnings as 'SCLU' (small consolidated, large unconsolidated earnings) firms. Specifically, SCLU firms are those in the lowest quartile of firms ranked on the excess of consolidated earnings over unconsolidated earnings scaled by controlling interests.

We find that SCLU firms pay more dividends than others when the ratio of related-party transactions to sales ('RPT') is high in the post-IFRS period. This result is consistent with concerns raised in prior literature regarding the opportunistic use of separate earnings to pay out excessive dividends despite poor consolidated performance (Choi, Kwak, & Gong, 2013; Hwang & Kang, 2017). We also find that the dividend payout tendency observed above is more pronounced in firms with high ownership of foreign shareholders or the largest shareholder. These results provide supporting evidence that Korean parent firms may inflate unconsolidated earnings in their separate financial statements to meet the dividend needs of their shareholders.

This study contributes to the literature in two ways. First, we extend prior literature on separate financial statements by demonstrating the use of separate earnings for the purpose of dividend management under K-IFRS. While most of the parent firms' separate earnings do not reflect their subsidiaries' performance under the cost method, the individual earnings of the firms without subsidiaries but with unconsolidated associates encompass the profits of those associates under the equity method. This suggests an inconsistency in the calculation of distributable profits for each firm depending on the presence or absence of a subsidiary.

Second, we extend the literature on related-party transactions by adding another incentive to utilize them. Existing studies provide various motivations for related-party transactions, such as tunnelling, propping, earnings management, and tax avoidance.[3] When a parent firm chooses the cost method to account for its investments in subsidiaries, unrealized gains or losses from internal transactions remain uneliminated from separate earnings, which form the basis of distributable profits. Therefore, a parent firm can increase its distributable profits by increasing profits from related-party transactions.

The remainder of this study is organized as follows: Section II illustrates the financial reporting regime before and after the adoption of IFRS. Section III reviews prior literature and develops hypotheses. Section IV describes the research model and the sample selection process. Section V presents empirical findings, and Section VI concludes.

[1] International Accounting Standards ('IAS') 27 'Separate Financial Statements' does not mandate a firm to prepare separate financial statements. However, Korean-listed firms are required to issue separate financial statements under the Commercial Act (Article 447) and the Act on External Audit of Stock Companies (Article 6).

[2] The Commercial Act does not clearly define the type of financial statements that underlie the calculation of distributable profits. In practice, Korean firms use unconsolidated financial statements as the basis of their dividend decisions (Hwang & Kang, 2017).

[3] Prior literature provides two alternative views of related-party transactions: (1) Related-party transactions create *conflicts of interest*, and (2) Related-party transactions are *efficient transactions* that fulfill the underlying economic needs of a firm (Gordon, Henry, & Palia, 2004). In this study, we consider related-party transactions in the context of the conflict of interest between stakeholders involved in these transactions. Under the conflict of interest view, a firm tends to use these transactions to expropriate minority shareholders (Cheung, Jing, Lu, Rau, & Stouraitis, 2009; Cheung, Rau, & Stouraitis, 2006; Kang, Lee, Lee, & Park, 2014) or to prop up poorly performing firms (Cheung et al., 2009; Friedman, Johnson, & Mitton, 2003; Jian & Wong, 2010). Firms may also use internal transactions to manage reported earnings (Kim & Bae, 2013; Kim & Woo, 2008) or to lower tax burdens (Choi, Koh, & Cho, 2011; Jacob, 1996; Ko, 2000; Lo, Wong, & Firth, 2010).

2. Institutional Background

To improve accounting transparency, Korea mandated all listed firms to adopt the K-IFRS in 2011. Under K-IFRS, all parent firms must issue consolidated financial statements as primary financial statements. These firms are also required to prepare unconsolidated 'separate' financial statements as supplementary statements. Before the adoption of IFRS, Korean parent firms were obligated to disclose unconsolidated 'individual' financial statements as their primary statements, followed by supplementary consolidated financial statements. The types of financial statements of Korean firms before and after IFRS are summarized in Panel A of Table 1.

Table 1. Types of financial statements before and after the IFRS adoption.

Comparison of the types of financial statements (F/S) before and after the IFRS adoption.				
Financial statements	**Before the IFRS adoption**		**After the IFRS adoption**	
	(1) Firms with a subsidiary	**(2) Firms without a subsidiary**	**(3) Firms with a subsidiary**	**(4) Firms without a subsidiary**
Accounting standard				
Main F/S	Individual F/S	Individual F/S	Consolidated F/S	Individual F/S
Supplementary F/S	Consolidated F/S	N/A	Separate F/S	N/A
Commercial act				
F/S for calculating distributable profits	Individual F/S	Individual F/S	Separate F/S	Individual F/S

Note: This table compares the types of financial statements for financial reporting based on accounting standards and for calculating distributable profits according to the Commercial Act, in the pre- and post-IFRS period.

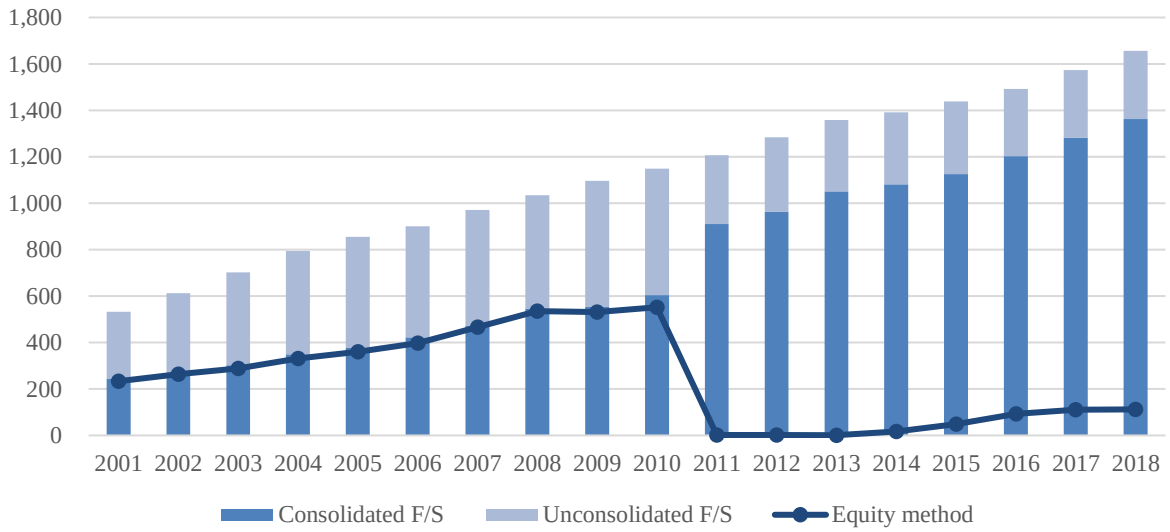

Figure 1. Annual distribution of the preparation of consolidated financial statements and the use of the equity method in unconsolidated financial statements.

Note: Figure 1 presents the annual distribution of consolidated (unconsolidated) financial statements prepared by parent (non-parent) firms with (without) a subsidiary. Figure 1 also presents the annual distribution of the parent firms using the equity method in their unconsolidated financial statements.

Individual and separate financial statements differ in their treatment of investments in subsidiaries, joint ventures, and associates ('investees'). Individual financial statements require firms to apply the equity method to these investments (IAS 28 paragraph 10). As a result, a parent firm's net income includes its share of the investees' net income, excluding gains or losses from transactions between the firm and its investees.[4] In contrast, separate financial statements under IFRS allow parent firms three choices for their investments: the cost method, the fair value method, and the equity method (IAS 27 paragraph 10). Most Korean listed firms have chosen the cost method, in which parent firms' earnings do not reflect their investees' earnings (Choi et al., 2013; Hwang & Kang, 2017).[5] Figure 1 shows that only a small number of firms employ the equity method in separate financial statements under IFRS.

[4]Paragraph 28 of IAS 28 "Investments in Associates and Joint Ventures" states that gains or losses resulting from 'upstream' and 'downstream' transactions between a firm and its investees are recognized in the firm's financial statements only to the extent of unrelated investors' interests in investees.
[5] Prior to 2016, IFRS required the use of cost or fair value for investments included in separate financial statements and did not permit the use of the equity method for those investments (IAS 27, BC9).

While IFRS adoption has changed primary financial statements from unconsolidated financial statements to consolidated ones, the Commercial Act of Korea continues to calculate distributable profits based on unconsolidated financial statements even after IFRS adoption. In other words, as shown in Column (3) of Panel A, parent companies make consolidated financial statements to show how well they are doing financially, but separate financial statements are used to figure out the maximum dividends under IFRS. This means that there is a difference between the earnings used for financial reporting and those used for dividends after IFRS.

3. Prior Literature and Hypotheses Development

The law restrict dividends, which are the distribution of earnings to shareholders, to retained earnings. Lintner (1956) suggests net earnings as the predominant driver of dividend changes in firms. Since reported earnings are significant constraints on dividends, managers are motivated to manage earnings to meet expected dividends (Watt & Zimmerman, 1986). Daniel, Denis, and Naveen (2008) show that dividend-paying firms are inclined to upwardly manage earnings when they anticipate pre-managed earnings falling below the expected dividends. Bennett and Bradbury (2007) find that there is an asymmetry in the dividend-cover earnings threshold and that this asymmetry dissipates with a legislative change that uncouples the connection between earnings and dividends.

After the introduction of K-IFRS, listed parent firms use unconsolidated earnings to calculate distributable profits while reporting consolidated earnings as their financial performance. In the post-IFRS period, the proportion of firms showing different signs of consolidated and unconsolidated earnings has increased (Hwang & Kang, 2017). We focus on Korean-listed parent firms reporting unconsolidated earnings that are much larger than consolidated earnings. In Hypothesis 1, we first analyze whether and how a discrepancy under K-IFRS between the main financial statements for reporting purposes and dividend purposes affects the dividend payout decisions of listed parent firms.

The accounting for investments in subsidiaries is different between consolidated and separate financial statements. Consolidated earnings include the financial performance of both the parent firm and its subsidiaries. In contrast, separate earnings under the cost method do not include the financial performance of the subsidiaries. As a result, even when the parent firm's consolidated earnings are small or negative due to the poor performances of subsidiaries, the cost method allows the parent firm to report large positive separate earnings, which increases distributable profits.

One of the key features of consolidated earnings is the elimination of intercompany transactions within a group. However, separate earnings under the cost method do not eliminate the effects of such transactions. For example, if parent firms generate profits through internal transactions with their subsidiaries, these profits do not affect consolidated earnings but increase separate earnings. This implies that parent firms can manage separate earnings upward by using internal transactions in order to meet dividend expectations without affecting consolidated earnings.

Based on the differences in accounting for both investments in subsidiaries and internal transactions between consolidated and separate financial statements, we predict that parent firms manage dividends upward through internal transactions under K-IFRS. This prediction leads to the following hypothesis:

H_1: Parent firms with unconsolidated earnings much larger than consolidated earnings (SCLU firms) pay more dividends than others when their internal transactions ratio (RPT) is high after the adoption of K-IFRS.

Ownership structure is one of the main factors affecting a firm's dividend policy and financial reporting quality. Many articles have pointed out that dividends from Korean-listed firms are primarily paid to foreign investors and the largest shareholders (Lee & Kim, 2018). According to the Korea Securities Depository, in December 2021, foreign investors received 14.134 trillion Korean Won ('KRW'), which accounted for 40.6% of the total dividends paid by listed firms. In addition, some firms where owners and their families hold significant stakes have been criticized for paying excessive dividends to meet the financial needs of their owners, even when the firms' business performance is poor. This study analyzes whether parent firms' dividend management through unconsolidated earnings differs according to the ownership structure in terms of the holdings of foreign investors and the largest shareholder.

In Hypothesis 2, we examine whether parent firms' dividend decisions are influenced by foreign ownership. In the Korean stock market, the majority of foreign investors are institutional investors who invest large-scale funds and can exercise influence on corporate decision-making (Park & Lee, 2006).[6]Porta, Lopez-De-Silanes, and Shleifer (1999) suggest that domestic controlling shareholders prefer policies that serve their interests, potentially disadvantaging minority shareholders, implying that foreign investors can play a vital role in determining dividend policies (Jeon et al., 2011).

The empirical evidence concerning the influence of foreign investors on dividend payments in Korea is mixed. According to Park et al. (2003),foreign investors' shareholding ratio has a positive relationship with dividend levels prior to the 1997 financial crisis but no significant relationship after the crisis. Sul and Kim

[6] Most foreign investors are financial institutions such as banks, securities and insurance companies, pension funds, or mutual funds (Jeon, Lee, & Moffett, 2011).

(2006) report that foreign shares are positively associated with dividends in firms with foreign ownership exceeding 5% for three consecutive years. They also find that firms with foreign majority shareholders distribute higher dividends compared to those with domestic majority shareholders. However, Park and Lee (2006) find a negative (positive) relationship between foreign ownership and dividend payout ratio in high-profit (low-profit) firms, suggesting that foreign shareholders induce firms' dividend decisions in a way that improves resource allocation efficiency.

Several studies report that foreign investors demand high dividend payments from firms even when their performance is poor. Yang (2012) shows that as the foreign ownership ratio increases, the stickiness of dividends is strengthened while the stickiness of committed costs is mitigated. These findings suggest that if foreign investors predict a firm's future prospects negatively, they may demand a reduction in committed costs by restraining capacity investments but demand an increase in dividends. Nam and Kim (2014) point out that dividend pressure from investors can be a greater burden on loss firms than on profit firms and show that the higher the ratio of foreign investors in loss firms, the higher the tendency to pay dividends.

Foreign investors may face greater information asymmetry problems than domestic investors (Kang & Stulz, 1997). If foreign investors demand high dividends to alleviate the information asymmetry problems, firms may decide to increase dividend payments to meet their demands. Dividend pressure can be a great burden, especially on loss firms, as investors prefer dividends to capital gains (Nam & Kim, 2014), which may strengthen the tendency to manage separate earnings upwards for dividend purposes.

Foreign investors, on the other hand, are one of the external elements of the corporate governance mechanism and can play a role in monitoring the opportunistic behaviors of managers (Stulz, 1999). Foreign investors with longer investment horizons may be more interested in the long-term performance of the firm than the short-term dividend returns based on managed profits. If foreign investors perform a monitoring role effectively, managers' incentive to manage separate earnings to increase dividend payments may be suppressed. These conflicting predictions lead to the following null hypothesis:

H_2: Dividend payout management through internal transactions of the parent firms with unconsolidated earnings much larger than consolidated earnings (SCLU firms) is not related to the ownership of foreign shareholders.

According to agency theory, dividends serve as a mechanism to mitigate agency costs derived from conflicts between managers and shareholders (Easterbrook, 1984; Jensen, 1986;Rozeff, 1982). High dividend payouts induce firms to raise external funds in capital markets, thereby facilitating more cost-effective monitoring of managers (Easterbrook, 1984) and constraining free cash flows available for managers' discretionary use (Jensen, 1986). With respect to the conflicts of interest between controlling and minority shareholders, controlling shareholders are inclined to prefer lower dividends, enabling them to extract private benefits of control at the expense of minority shareholders (Faccio, Lang, & Young, 2001). Alternatively, firms may opt for high dividends to alleviate investor concerns about expropriation, particularly in situations with a heightened conflict between controlling and minority shareholders (Faccio et al., 2001).

In Hypothesis 3, we examine whether the dividend policies of parent firms are influenced by controlling shareholders' ownership. With the exception of countries with dispersed ownership, such as the U.S. and U.K., most countries exhibit high ownership concentration, in which conflicts between controlling shareholders and outside investors is a main concern in corporate governance (Gugler & Yurtoglu, 2003; Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1998). The concentration of ownership and control in the hands of a small number of significant shareholders is distinctive to Korean business group. These controlling shareholders are typically the founders and their families and have considerable authority over critical corporate decisions (Baek, Kang, & Park, 2004). As these shareholders have the desire to retain their control, they may prefer dividends to capital gains as a means to realize a return (Schmid, Ampenberger, Kaserer, & Achleitner, 2012). Since dividends are paid on a pro-rata basis to all shareholders, controlling shareholders may have a greater incentive to receive dividends (Nam, 2017). On the other hand, under the agency framework, the relationship between controlling shareholders' ownership and dividends can be predicted in two directions (Porta, Lopez-De-Silanes, Shleifer, & Vishny, 2000). One perspective views dividends as an outcome of an agency problem and predicts that as controlling shareholders' ownership increases, their incentives to use corporate resources for personal interests decrease dividend payments. The other perspective views dividends as a substitute for legal protection for outside investors and expects firms with high ownership of controlling shareholders to increase dividend payments to alleviate investors' concerns about insider expropriation.

Previous studies present mixed findings on the association between the ownership of controlling shareholders and dividend payments. Gugler and Yurtoglu (2003) find a negative relationship between both the voting rights of the largest shareholder and deviations from the one-share-one-vote rule and the dividend payout ratio of German companies. This implies that a low dividend payout signals a potential risk of expropriation of minority shareholders by controlling shareholders. Using panel data from UK firms, Khan (2006) reports a negative but nonlinear relationship between dividends and ownership concentration. Truong and Heaney (2007) investigate 8,279 firms from 37 countries and show a convex relationship between the ownership of controlling shareholders and dividend payments.

Studies analyzing Korean firms find a positive relationship between the ownership of controlling shareholders and dividends (Hwang, Kim, Park, & Park, 2013; Ko & Joh, 2009; Nam, 2017; Park & Lee, 2006; Park, Park, & Hwang, 2005). Ko and Joh (2009) report that firms with controlling shareholders possessing

high levels of cash flow rights and control rights are more likely to distribute cash dividends to their shareholders. When managerial ownership surpasses a certain threshold, the entrenchment effect can exacerbate the agency problem (Morck, Shleifer, & Vishny, 1988). In light of significant ownership by controlling shareholders in Korean firms, the positive relationship between controlling shareholders' ownership and cash dividends indicates that firms with severe agency problems utilize cash dividends to alleviate agency conflicts between insiders and minority shareholders (Ko & Joh, 2009). Other studies suggest that the discrepancy between controlling shareholders' control rights and ownership rights is negatively related to dividend payments (Hwang et al., 2013; Park et al., 2005). Hwang et al. (2013) report a negative relationship between chaebol affiliation and dividend payouts, which implies that in chaebol firms with a greater disparity between control rights and ownership rights, controlling shareholders favor retaining corporate resources under their control.

Based on the previous studies that report a positive relationship between controlling shareholders' ownership and dividend payments in Korean firms, we examine whether parent firms with high ownership of controlling shareholders manage separate earnings upward for dividend purposes. For firms with a large shareholding by controlling shareholders, management may increase dividends to respond to dividend demands from controlling shareholders (Schmid et al., 2012), or to mitigate agency costs from conflicts between controlling and minority shareholders (Porta et al., 2000)or to build a reputation for not expropriating minority shareholders (Gomes, 2000).[7] According to Jung (2020), there are an increasing number of companies that pay excessive dividends in comparison to their financial performance, and the majority of these companies are ultimate parent companies in business groups that the largest shareholders and their families directly own. We expect that the upward management of separate earnings for dividend purposes is more pronounced for parent firms with higher ownership by the largest shareholder. This prediction leads to the following hypothesis:

H_5: The ownership of controlling shareholders has nothing to do with how dividends are managed by parent companies whose unconsolidated earnings are much higher than their consolidated earnings (SCLU firms).

4. Research Design

4.1. Sample Selection

For empirical analyses, we use parent firms listed on the Korea Exchange (KRX) for the period of 2001 through 2018. Financial data is sourced from the Total Solution 2000 ('TS2000') database.[8] Our initial sample encompasses all listed companies with a fiscal year-end of December, excluding financial institutions. We then delete observations with insufficient financial data necessary for measuring the variables for regression analyses. To investigate the dividend decisions of parent firms, we narrow down our sample to those preparing consolidated financial statements. Given our focus on analyzing whether and how parent firms manage separate earnings under the cost method, we exclude firms using the equity method in separate financial statements. We further delete observations with negative values of total equity or controlling interests, as these firms may have different incentives for business decisions. Lastly, we exclude observations in industries with fewer than ten firms each year to measure industry-adjusted dividends (Lai, Saffar, Zhu, & Liu, 2020). Following these criteria, our final sample consists of 9,527 firm-year observations, encompassing parent firms that prepare individual (separate) financial statements using the equity (cost) method in the pre-IFRS (and post-IFRS) periods. The sample selection procedure is summarized in Panel A of Table 2.

Panel B presents the annual distribution of sample firms. As we limit our sample to those preparing consolidated financial statements, the proportion of observations has increased sharply after the adoption of IFRS.[9]

Panel C reports the distribution of sample firms by the sign of consolidated and unconsolidated earnings. Before the adoption of K-IFRS in Column (2), the firms with consolidated losses and unconsolidated profits and the firms with consolidated profits and unconsolidated losses were 1.9% (48 firm-years) and 0.2% (5 firm-years), respectively. The proportion of these firms increases to 4.4% (305 firm-years) and 3.1% (214 firm-years), respectively, under K-IFRS in Column (3). Panel C shows that the difference between consolidated earnings and separate earnings applying the cost method after K-IFRS would be bigger than the difference between consolidated earnings and individual earnings when the equity method was used before K-IFRS.

[7]When minority shareholders discount the firm value due to the risk of expropriation, controlling shareholders with a substantial amount of shares suffer a reduction in their wealth, so managers are willing to a reputation for treating minority shareholders well (Gomes, 2000).
[8] The TS 2000 database provides detailed information on the financial statements and corporate ownership of all publicly traded firms in Korea.
[9] Korea has mandated all listed firms to adopt the K-IFRS since 2011. However, the number of sample firms increases the most in 2012 because we limit our sample to the firms with consolidated financial statements for two consecutive years to measure the regression variables.

Table 2. Sample selection and distribution.

Panel A: Sample selection

Criteria	**Firm-year**
Non-financial listed firms with December year-end for the period of 2001 through 2018	22,596
Less: Firms without financial data	(2,547)
Less: Firms without consolidated financial statements	(6,929)
Less: Firms using the equity method in separate financial statements after the IFRS adoption	(387)
Less: Firms with negative values of total equity or controlling interests	(1,157)
Less: Firms belong to industries with fewer than ten firms in any given year	(2,049)
Final sample	9,527

Panel B: Sample distribution by year.

Year	Firm	%
2001	82	0.86
2002	147	1.54
2003	177	1.86
2004	210	2.20
2005	234	2.46
2006	262	2.75
2007	296	3.11
2008	338	3.55
2009	380	3.99
2010	414	4.35
2011	446	4.68
2012	789	8.28
2013	865	9.08
2014	898	9.43
2015	921	9.67
2016	940	9.87
2017	1,024	10.75
2018	1,104	11.59
Total	9,527	100.00

Panel C: Sample distribution by the sign of earnings.

Consolidated earnings	Unconsolidated earnings					
	(1) Total		(2) Before the IFRS adoption		(3) After the IFRS adoption	
	Pos. (+)	Neg. (-)	Pos. (+)	Neg. (-)	Pos. (+)	Neg. (-)
Pos. (+)	6,833	219	2,015	5	4,818	214
Neg. (-)	353	2,122	48	448	305	1,674
Total	9,527		2,516		7,011	

Note: This table summarizes the selection procedure and distribution of sample firms. The final sample consists of Korean listed parent firms that prepare separate (individual) financial statements using the cost (equity) method in the post-IFRS (pre-IFRS) period.

4.2. Regression Model

To examine whether a parent firm manages dividend payments through internal transactions under K-IFRS, we perform multivariate regression analyses. We identify firms reporting small consolidated but large unconsolidated earnings as SCLU firms and compare their unconsolidated earnings to those of other firms. Specifically, SCLU firms are in the lowest quartile of firms ranked on the excess of consolidated earnings over unconsolidated earnings scaled by controlling interests. To test Hypothesis 1, we estimate the following Model (1):

$$\begin{aligned} DIV_t = {} & \beta_0 + \beta_1 SCLU_t + \beta_2 POST_t + \beta_3 SCLU_t \times POST_t + \beta_4 HRPT_t + \beta_5 SCLU_t \times HRPT_t \\ & + \beta_6 POST_t \times HRPT_t + \beta_7 SCLU_t \times POST_t \times HRPT_t + \beta_8 SIZE_t + \beta_9 LEV_t \\ & + \beta_{10} MTB_t + \beta_{11} ROA_t + \beta_{12} CFO_t + \beta_{13} VOL_t + \beta_{14} INDDIV_t + \beta_{15} TURN_t \\ & + \beta_{16} LAR_t + \beta_{17} FOR_t + YD + IND + \varepsilon_t \end{aligned} \quad (1)$$

Where, *DIV*= Cash dividend payout scaled by the market value of equity.

SCLU= An indicator variable equal to 1 if a firm is in the lowest quartile of the sample firms ranked on the excess of consolidated earnings over unconsolidated earnings scaled by controlling interests, and 0 otherwise.

POST= An indicator variable equal to 1 if a firm prepares financial statements in accordance with K-IFRS, and 0 otherwise.

HRPT= An indicator variable equal to 1 if the ratio of related-party transactions to sales (*RPT*) is in the top quartile of the sample in a given year, and 0 otherwise.

SIZE= The natural logarithm of the market value of equity.

LEV= The ratio of financial liabilities to total assets.

MTB= Sum of the market value of equity and total liabilities, divided by book value of total assets.

ROA= Earnings from continuing operation divided by total assets.

CFO= Operating cash flows scaled by total assets.

VOL= The standard deviation of *ROA* over the past three years.

INDDIV= The industry's median of *DIV*.

TURN= The ratio of common shares traded for one year to common shares outstanding at

the end of the year.
LAR= The percentage of common stocks held by the largest shareholder.
FOR= Ownership of foreign shareholders.
ΥD= Year dummies.
IND= Industry dummies.

The dependent variable *DIV* indicates a firm's dividend payments and is measured as cash dividends scaled by the market value of equity. *POST* is a dummy variable indicating the period during which a firm prepares financial statements in accordance with K-IFRS. *HRPT* indicates a firm in the top quartile of firms ranked on the ratio of related-party transactions to sales (*RPT*). The coefficients of *SCLU*POST* and *SCLU*POST*HRPT* represent the dividend payments of SCLU firms with low RPTs and those of SCLU firms with high RPTs under K-IFRS, respectively. If SCLU firms pay more dividends than others through RPTs in the post-IFRS period, the coefficient of *SCLU*POST*HRPT* is expected to be positive.

In Hypotheses 2 and 3, we predict that SCLU firms' management of dividends through internal transactions depends on the ownership level of either foreign investors or the largest shareholder, respectively. To test these hypotheses, we partition our pooled sample into two subsamples based on the ownership level of either foreign investors or the largest shareholder and estimate Model (1) separately for each subsample. We include a series of control variables drawn from prior studies. We first control for firm characteristics that may impact dividend decisions. Consistent with prior studies reporting that larger firms with higher profitability and fewer growth opportunities are more inclined to pay dividends (Denis & Osobov, 2008; Fama & French, 2001),we control for firm size (*SIZE*), growth opportunities (*MTB*), and profitability (*ROA*). To address a firm's agency costs and its ability to pay dividends (Faccio et al., 2001; Gugler & Yurtoglu, 2003;Nam, 2019), we include leverage (*LEV*) and operating cash flows (*CFO*). As risk lowers dividend payments (Hoberg & Prabhala, 2008), we include the volatility of profitability (*VOL*) to capture a firm's operating risk (Jeong, 2013; Park & Lee, 2006). We further control the market liquidity of stocks (*TURN*) because investors require more cash dividends if the liquidity of a firm's stock is low (Banerjee, Gatchev, & Spindt, 2007). To control for industry effects, we incorporate *INDDIV*, measured as the industry's median of dividend payments (Lai et al., 2020). We include foreign shareholders' ownership (*FOR*) and the largest shareholder's ownership (*LAR*) to control for the monitoring incentives and dividend preference of foreign investors (Baba, 2009; Jeon et al., 2011)and to control for agency conflicts and dividend pressure (Porta et al., 2000; Schmid et al., 2012), respectively. Finally, we control for year- and industry-fixed effects by including year dummies and 3-digit industry dummies in the regression model. To mitigate the influence of outliers on the results of the regression analyses, all continuous variables are winsorized at the 1% and 99% percentiles of the distribution. Taking into account the potential for residual dependence attributed to the firm effect, we calculate standard errors with clustering by the firm (Petersen, 2008).

Table 3. Descriptive statistics.

Variable	(1) Pooled sample					(2) Mean difference		
	Mean	Std. dev.	Min.	Median	Max.	SCLU firms	Other firms	Difference
DIV	0.012	0.015	-	0.008	0.070	0.010	0.013	-0.003***
SCLU	0.249	0.433	-	-	1.000	1.000	-	1.000***
POST	0.736	0.441	-	1.000	1.000	0.738	0.735	0.002
HRPT	0.250	0.433	-	-	1.000	0.270	0.243	0.028***
SIZE	18.873	1.514	16.084	18.604	23.595	18.731	18.920	-0.189***
LEV	0.212	0.169	-	0.198	0.649	0.255	0.198	0.057***
MTB	1.266	0.819	0.414	1.016	5.358	1.287	1.259	0.028
ROA	0.016	0.090	-0.426	0.027	0.192	0.004	0.019	-0.015***
CFO	0.045	0.076	-0.193	0.042	0.261	0.033	0.048	-0.015***
VOL	0.046	0.057	0.002	0.026	0.342	0.056	0.042	0.014***
INDDIV	0.009	0.008	-	0.008	0.055	0.008	0.009	-0.001***
TURN	3.472	4.710	0.093	1.874	29.192	3.850	3.346	0.504***
LAR	0.401	0.162	0.074	0.395	0.800	0.377	0.409	-0.032***
FOR	0.086	0.123	-	0.031	0.577	0.072	0.091	-0.019***

Note: This table provides the descriptive statistics of the sample. Column (1) presents summary statistics for the pooled sample and Column (2) compares the mean values of the variables between SCLU firms and other firms using t-statistics.DIV is cash dividend payout scaled by the market value of equity. SCLU is an indicator variable equal to 1 if a firm is in the lowest quartile of the sample firms ranked on the excess of consolidated earnings over unconsolidated earnings scaled by controlling interests, and 0 otherwise. POST is an indicator variable equal to 1 if a firm prepares financial statements in accordance with K-IFRS, and 0 otherwise. HRPT is an indicator variable equal to 1 if the ratio of related-party transactions to sales is in the top quartile of the sample in a given year, and 0 otherwise. SIZE is the natural logarithm of the market value of equity. LEV is the ratio of financial liabilities to total assets. MTB is sum of the market value of equity and total liabilities, divided by book value of total assets. ROA is earnings from continuing operation divided by total assets. CFO is operating cash flows scaled by total assets. VOL is the standard deviation of ROA over the past three years. INDDIV is the industry's median of DIV. TURN is the ratio of common shares traded for one year to common shares outstanding at the end of the year. LAR is the percentage of common stocks held by the largest shareholder. FOR is ownership of foreign shareholders.
***indicates statistical significance in two-tailed tests at the 1% level.

5. Empirical Results

5.1. Descriptive Statistics

Table 3 reports the descriptive statistics of the variables used in our regression analyses. Column (1) presents summary statistics of the variables for the pooled sample, and Column (2) compares the mean values of the variables between SCLU firms and others.

The dependent variable, dividend payments (*DIV*), has a mean value of 0.012 in the pooled sample, indicating that sample firms pay, on average, 1.2% of the market value of equity as dividends. The differences in the mean values of *DIV* between SCLU firms and other firms show that SCLU firms pay fewer dividends than others. The average values of *HRPT* for SCLU and other firms are 0.270 and 0.243, respectively, suggesting that 27.0% of SCLU firms and 24.3% of other firms belong to the top quartile group with a high proportion of RPTs.[10]The mean difference in *HRPT* between the two groups is significant, which implies that SCLU firms have more related-party transactions than others.

Control variables show the characteristics of SCLU firms compared to other firms. Specifically, SCLU firms have a smaller size (*SIZE*), higher leverage (*LEV*), lower profitability (*ROA*), fewer operating cash flows (*CFO*), and higher volatility of profitability (*VOL*) than others. The market liquidity of stocks (*TURN*) of SCLU firms is higher than that of others. The ownership of the largest shareholder (*LAR*) and foreign shareholders (*FOR*) is lower in SCLU firms than in others.

Table 4 presents the Pearson correlations among the regression variables.[11] The SCLU firm (*SCLU*) is negatively correlated with dividend payments (*DIV*), indicating that SCLU firms tend to pay fewer dividends than others. Since we aim to investigate the dividend payment decisions of SCLU firms with high RPTs after adopting IFRS, the correlations are limited in providing preliminary evidence for our hypotheses. Therefore, we use multivariate analyses to examine whether and how SCLU firms use separate financial statements for dividend decisions after the adoption of K-IFRS.

5.2. Regression Results

We first investigate whether SCLU firms tend to pay more dividends through internal transactions after the adoption of K-IFRS, as predicted in Hypothesis 1. The regression results are provided in Table 5. In Column (1), which does not include the extent of internal transactions by SCLU firms, the coefficients on *SCLU* and *SCLU*POST* are not significant, indicating that SCLU firms do not exhibit different dividend behaviors from other firms in both the pre- and post-IFRS periods. In Column (2), which considers how much SCLU firms do internal transactions with related parties, the coefficients on *SCLU* and *SCLU*POST* are still not significant. This means there isn't a big difference between SCLU firms and others in how likely they are to pay dividends before and after the IFRS adoption if RPT is low. The coefficient on *SCLU*POST*HRPT* is significantly positive at the 10% level, which indicates that SCLU firms tend to pay more dividends in the post-IFRS period if RPT is high, which is consistent with H1. These results suggest internal transactions as a mechanism to manage dividend payments upward under the cost method in the post-IFRS period.

Most of the control variables identified by prior studies as factors affecting dividend policy have statistically significant coefficients. Firms with low growth opportunities (*MTB*), high profitability (*ROA*), low leverage (*LEV*), high operating cash flows (*CFO*), and low operating risk (*VOL*) pay more dividends. The industry median dividends (*INDDIV*) have a significantly positive coefficient. The market value (*SIZE*) of a firm is negatively associated with dividend payments. The largest shareholder's ownership (*LAR*) and foreign investors' ownership (*FOR*) are positively related to dividend payments.

Next, we investigate whether SCLU firms' dividend decisions depend on the ownership structure. We first divide our sample into two subsamples based on the median of foreign ownership and examine the dividend payments of SCLU firms with different degrees of foreign ownership. In the high and low foreign ownership subsamples, the average value of foreign ownership is 16.28% and 1.04%, respectively, with large differences between the subsamples. Table 6 reports the regression results of the subsample analysis.

[10] The mean value of *RPT* for the pooled sample is 0.230, which indicates that internal transactions with other affiliates within the group account for 23.0% of sales on average. The mean values of *RPT* for SCLU firms and others are 0.248 and 0.224, respectively.
[11] The values of Variance Inflation Factor (VIF) do not exceed 10 for the regression model.

Table 4. Pearson correlations.

Variable		[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]	[9]	[10]	[11]	[12]	[13]
[1]	DIV													
[2]	SCLU	**-0.093**												
[3]	POST	**-0.276**	0.002											
[4]	HRPT	-0.004	**0.028**	0.004										
[5]	SIZE	**-0.024**	**-0.054**	**0.053**	**0.058**									
[6]	LEV	**-0.143**	**0.146**	**-0.083**	**-0.027**	**-0.128**								
[7]	MTB	**-0.287**	0.015	**0.186**	**-0.038**	**0.327**	**-0.096**							
[8]	ROA	**0.311**	**-0.072**	**-0.094**	-0.017	**0.268**	**-0.318**	-0.015						
[9]	CFO	**0.203**	**-0.088**	**-0.038**	**-0.035**	**0.198**	**-0.232**	**0.053**	**0.472**					
[10]	VOL	**-0.277**	**0.105**	0.011	0.015	**-0.166**	**0.126**	**0.181**	**-0.465**	**-0.229**				
[11]	INDDIV	**0.434**	**-0.040**	**-0.533**	-0.005	**0.034**	**0.066**	**-0.224**	**0.147**	**0.096**	**-0.145**			
[12]	TURN	**-0.231**	**0.046**	0.005	**-0.036**	**-0.210**	**0.062**	**0.151**	**-0.163**	**-0.107**	**0.162**	**-0.108**		
[13]	LAR	**0.228**	**-0.085**	**-0.050**	**0.032**	**-0.038**	**-0.079**	**-0.215**	**0.171**	**0.061**	**-0.211**	**0.152**	**-0.331**	
[14]	FOR	**0.140**	**-0.066**	**-0.093**	**0.023**	**0.574**	**-0.191**	**0.107**	**0.240**	**0.225**	**-0.159**	**0.147**	**-0.193**	**-0.091**

Note: This table reports the Pearson correlation coefficients among variables used in the regression analyses. The definitions of variables are provided in Table 3. The bolded correlation coefficients are significant at the 5 percent level.

Table 5. IFRS adoption, internal transactions, and dividends of SCLU firms.

Variable	Full sample			
	(1)		(2)	
	Coefficient	t-value	Coefficient	t-value
Intercept	0.043***	8.21	0.043***	8.15
SCLU	-0.001	-1.32	-0.000	-0.33
POST	-0.005***	-2.91	-0.005***	-2.86
SCLU*POST	-0.000	-0.12	-0.001	-1.02
HRPT			0.000	0.05
SCLU*HRPT			-0.003*	-1.73
POST*HRPT			-0.000	-0.08
SCLU*POST*HRPT			0.003*	1.91
SIZE	-0.001***	-5.06	-0.001***	-4.97
LEV	-0.008***	-5.05	-0.008***	-5.07
MTB	-0.003***	-10.07	-0.003***	-10.07
ROA	0.024***	10.96	0.024***	10.85
CFO	0.011***	5.10	0.011***	5.17
VOL	-0.025***	-7.99	-0.026***	-7.91
INDDIV	0.474***	8.89	0.473***	8.86
TURN	-0.000***	-10.95	-0.000***	-10.90
LAR	0.006***	3.30	0.006***	3.32
FOR	0.010***	3.49	0.010***	3.45
Year dummies	Included		Included	
Industry dummies	Included		Included	
F value	92.51		86.58	
Adjusted R^2	0.35		0.35	
N	9,527		9,527	

Note: This table reports the results of the Ordinary Least Squares (OLS) regression to examine dividend payments of SCLU firms with high RPTs after the adoption of IFRS. The definitions of variables are provided in Table 3. ***and* indicate statistical significance at the 1% and 10% levels, respectively.

In all columns, the coefficients on *SCLU* and *SCLU*POST* are not significant, indicating that dividend payments of SCLU firms are not significantly different from those of others before and after the adoption of IFRS, regardless of the degree of foreign ownership if RPT is low. The significance of the coefficients on *SCLU*POST*HRPT* is different across subsamples. The estimated coefficient on *SCLU*POST*HRPT* is significantly positive at the 5% level for firms with high ownership by foreign shareholders, while it is not significant for firms with low foreign shareholding. This result shows that under K-IFRS, SCLU firms with high foreign ownership manage dividend payments through internal transactions, suggesting that they can manage separate earnings to respond to the dividend demands of foreign shareholders.

Table 6. Influence of foreign ownership on SCLU firms' dividends.

Variable	Subsamples based on the ownership of foreign shareholders			
	(1) High		(2) Low	
	Coefficient	t-value	Coefficient	t-value
Intercept	0.050***	8.01	0.049***	4.90
SCLU	0.001	0.71	-0.001	-0.90
POST	-0.004*	-1.80	-0.005	-1.48
SCLU*POST	-0.002	-1.47	0.000	0.01
HRPT	0.002	1.00	-0.001	-0.81
SCLU*HRPT	-0.005***	-2.59	-0.000	-0.19
POST*HRPT	-0.002	-1.16	0.001	0.68
SCLU*POST*HRPT	0.005**	2.29	0.002	0.62
SIZE	-0.001***	-5.13	-0.002***	-4.00
LEV	-0.007***	-3.03	-0.008***	-3.86
MTB	-0.003***	-9.82	-0.001***	-3.10
ROA	0.031***	8.49	0.021***	8.44
CFO	0.007**	2.27	0.012***	4.26
VOL	-0.024***	-4.18	-0.026***	-6.79
INDDIV	0.425***	5.45	0.500***	6.86
TURN	-0.001***	-8.24	-0.000***	-8.36
LAR	0.006**	2.22	0.007***	3.31
FOR	0.005	1.56	0.092***	3.68

Variable	Subsamples based on the ownership of foreign shareholders			
	(1) High		(2) Low	
	Coefficient	t-value	Coefficient	t-value
Year dummies	Included		Included	
Industry dummies	Included		Included	
F value	41.44		45.56	
Adjusted R^2	0.34		0.36	
N	4,754		4,773	

Note: This table reports the results of the OLS regression to examine the influence of foreign ownership on dividend payments of SCLU firms with high RPTs after the adoption of IFRS. The two subsamples in columns (1) and (2) are partitioned by the level of foreign ownership. The definitions of variables are provided in Table 3. ***, **, and * indicate statistical significance at the 1%, 5%, and 10% levels, respectively.

Table 7 presents the results of the subsample analysis categorized by the ownership of the largest shareholder. In the high (low) controlling ownership subsample, the average ownership ratio of the largest shareholderis 53.23% (26.98%). The coefficient on *SCLU*POST*HRPT* is significantly positive only for firms with high ownership by the largest shareholders. This result suggests that upward dividend management through internal transactions under K-IFRS is more evident when the largest shareholder's ownership concentration is high.

Table 7. Influence of the largest shareholder's ownership on SCLU firms' dividends.

Variable	Subsamples based on the ownership of the largest shareholder			
	(1) High		(2) Low	
	Coefficient	t-value	Coefficient	t-value
Intercept	0.057***	6.34	0.034***	5.66
SCLU	-0.000	-0.16	-0.001	-0.81
POST	-0.004	-1.56	-0.006***	-2.83
SCLU*POST	-0.001	-0.67	-0.001	-0.45
HRPT	0.001	0.33	-0.001	-0.53
SCLU*HRPT	-0.005**	-1.97	-0.001	-0.46
POST*HRPT	-0.000	-0.19	0.000	0.20
SCLU*POST*HRPT	0.006**	2.30	0.001	0.46
SIZE	-0.001***	-3.42	-0.001***	-3.81
LEV	-0.006***	-2.69	-0.008***	-4.65
MTB	-0.004***	-6.90	-0.002***	-7.27
ROA	0.042***	8.80	0.016***	7.83
CFO	0.016***	4.28	0.006***	2.71
VOL	-0.032***	-5.15	-0.020***	-5.48
INDDIV	0.426***	5.94	0.505***	5.87
TURN	-0.001***	-8.36	-0.000***	-7.04
LAR	-0.001	-0.24	0.010***	3.06
FOR	0.005	1.14	0.015***	4.57
Year dummies	Included		Included	
Industry dummies	Included		Included	
F value	34.02		58.48	
Adjusted R^2	0.30		0.42	
N	4,761		4,766	

Note: This table reports the results of the OLS regression to examine the influence of the largest shareholder's ownership on dividend payments of SCLU firms with high RPTs after the adoption of IFRS. The two subsamples in columns (1) and (2) are classified using the degree of ownership of the largest shareholder. The definitions of variables are provided in Table 3. ***and** indicate statistical significance at the 1% and 5% levels, respectively.

Overall, Table 6 and Table 7 provide evidence that SCLU firms appear to manage dividends through internal transactions, especially when foreign shareholders' or the largest shareholder's ownership is high. Since SCLU firms are those with poor consolidated performance, our findings suggest that firms may opportunistically use separate earnings with the cost method to pay excessive dividends despite poor business performance.

5.3. Additional Analyses

Prior literature shows that firms belonging to Korean business groups (*chaebols*) generally exhibit lower average dividend payouts compared to others. The owners of chaebol firms, with significantly higher control rights than ownership rights, are likely to have weak incentives to return corporate earnings to outside shareholders but strong incentives to divert corporate resources for their own interests (Hwang et al., 2013).

To investigate whether and how the disjunction between control rights and ownership rights affects the dividend decisions of parent firms, we categorize the sample into two groups depending on their chaebol affiliation.

Table 8. Influence of chaebol affiliation on SCLU firms' dividends.

Variable	Subsamples based on chaebol affiliation			
	(1) Chaebol		(2) Non-chaebol	
	Coefficient	t-value	Coefficient	t-value
Intercept	0.054***	5.53	0.039***	5.19
SCLU	0.001	0.67	-0.001	-0.45
POST	-0.003	-1.32	-0.004*	-1.65
SCLU*POST	-0.000	-0.63	-0.001	-0.75
HRPT	0.000	0.10	0.001	0.59
SCLU*HRPT	-0.000	-0.24	-0.004*	-1.71
POST*HRPT	0.001	0.51	-0.001	-0.82
SCLU*POST*HRPT	0.001	0.37	0.004**	1.96
SIZE	-0.002***	-3.66	-0.001***	-2.78
LEV	-0.000	-0.08	-0.010***	-5.74
MTB	-0.004***	-5.79	-0.002***	-7.74
ROA	0.056***	6.27	0.021***	9.23
CFO	0.008	1.50	0.011***	4.85
VOL	-0.039***	-3.66	-0.025***	-7.24
INDDIV	0.606***	5.32	0.426***	7.04
TURN	-0.000	-1.56	-0.000***	-10.59
LAR	-0.001	-0.18	0.007***	3.56
FOR	0.009*	1.76	0.009***	2.87
Year dummies	Included		Included	
Industry dummies	Included		Included	
F value	18.43		74.82	
Adjusted R^2	0.39		0.36	
N	1,612		7,915	

Note: This table reports the results of the OLS regression to examine the influence of chaebol affiliation on dividend payments of SCLU firms with high RPTs after the adoption of IFRS. The two subsamples in columns (1) and (2) are partitioned based on chaebol affiliation. The definitions of variables are provided in Table 3. ***, **, and * indicate statistical significance at the 1%, 5%, and 10% levels, respectively.

In Table 8, the coefficient on *SCLU*POST*HRPT* is not significant for chaebol firms but is significantly positive at the 5% level for non-chaebol firms. The insignificant coefficient for chaebol firms is consistent with the finding from prior literature that chaebol firms pay fewer dividends than other firms and suggests that chaebol firms have weak incentives to increase dividend payouts through internal transactions.

To clarify the impact of ownership structure and internal transactions on dividends, we partition sample firms into four groups based on the ownership of the largest shareholder or foreign shareholders and the ratio of internal transactions and repeat the main analysis for each group. In Panel A of Table 9, the coefficient on *SCLU*POST* is significantly positive only when both the percentage of shares held by the largest shareholder and the internal transaction ratio are high. In Panel B, the coefficient on *SCLU*POST* is significantly positive only when both foreign ownership and the internal transaction ratio are high. These results show that SCLU companies are more likely to raise dividends through internal transactions when the biggest shareholder or foreign shareholders own a lot of shares. This shows that our main results are robust even when we use different model specifications.

Table 9. Alternative model specifications.

Panel A: Subsamples based on the ownership of the largest shareholder and internal transaction ratio								
Variable	Ownership of the largest shareholder * internal transaction ratio							
	(1) High*High		(2) High*Low		(3) Low*High		(4) Low*Low	
	Coefficient	t-value	Coefficient	t-value	Coefficient	t-value	Coefficient	t-value
Intercept	0.048***	3.88	0.056***	5.48	0.045***	5.25	0.032***	4.47
SCLU	-0.006***	-2.93	-0.000	-0.16	-0.002	-0.87	-0.001	-0.82
POST	-0.009***	-2.79	-0.002	-0.59	-0.005	-1.45	-0.008***	-2.59
SCLU*POST	0.006***	2.76	-0.001	-0.63	0.000	0.20	-0.000	-0.41
Controls	Included		Included		Included		Included	
Year dummies	Included		Included		Included		Included	
Industry dummies	Included		Included		Included		Included	
F value	10.26		28.81		14.99		49.89	

Panel A: Subsamples based on the ownership of the largest shareholder and internal transaction ratio								
Variable	Ownership of the largest shareholder * internal transaction ratio							
	(1) High*High		(2) High*Low		(3) Low*High		(4) Low*Low	
	Coefficient	t-value	Coefficient	t-value	Coefficient	t-value	Coefficient	t-value
Adjusted R^2	0.28		0.31		0.40		0.43	
N	1,265		3,496		1,112		3,654	
Panel B: Subsamples based on ownership of foreign shareholders and internal transaction ratio								
Variable	Ownership of foreign shareholders * internal transaction ratio							
	(1) High*High		(2) High*Low		(3) Low*High		(4) Low*Low	
	Coefficient	t-value	Coefficient	t-value	Coefficient	t-value	Coefficient	t-value
Intercept	0.046***	4.84	0.050***	7.22	0.063***	4.99	0.044***	3.57
SCLU	-0.004***	-2.61	0.001	0.62	-0.002	-0.66	-0.001	-0.88
POST	-0.006*	-1.71	-0.002	-0.89	-0.004	-1.27	-0.005	-1.50
SCLU*POST	0.004*	1.75	-0.002	-1.44	0.002	0.65	0.000	0.11
Controls	Included		Included		Included		Included	
Year dummies	Included		Included		Included		Included	
Industry dummies	Included		Included		Included		Included	
F value	13.14		32.96		11.16		40.52	
Adjusted R^2	0.35		0.34		0.34		0.38	
N	1,281		3,473		1,096		3,677	

Note: This table reports the results of the OLS regression to examine dividend payments of SCLU firms after the adoption of IFRS. In Panels A and B, four subsamples are partitioned by the ownership of the largest shareholder or foreign shareholders and internal transaction ratio. The definitions of variables are provided in Table 3. ***, and * indicate statistical significance at the 1% and 10% levels, respectively.

6. Conclusion

Despite the transition of the main financial statements from unconsolidated to consolidated financial statements with the introduction of IFRS, unconsolidated financial statements are still used significantly in Korea. This study focuses on the implications of unconsolidated financial statements for dividend decisions. We find that firms reporting unconsolidated earnings much larger than consolidated earnings (SCLU firms) pay more dividends than others in the post-IFRS period when related-party transactions are high. We also find that dividend-increasing management of SCLU firms is more pronounced when the ownership of foreign shareholders or the largest shareholder is high. These results suggest that firms manage dividends upward through internal transactions, taking advantage of the cost method under K-IFRS.

Our results suggest that firms strategically manage distributable profits using internal transactions. Although distributable profits are important information to shareholders, most companies do not disclose distributable profits. Our findings support the concerns about the opportunistic use of unconsolidated separate earnings to pay out excessive dividends despite poor consolidated performance. We hope that our results provide policy implications for regulators and market participants to enhance transparency in dividend decisions.

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