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The Impact of Implementation Good Corporate Governance to Firm Value (Evidence from Indonesia Public Banking Sector)

Adrie Putra*
Faculty of Economy, University of Esa Unggul
Adrie.putra@esaunggul.ac.id

Royhisar Martahan Simanungkalit
Faculty of Economic, University of Esa Unggul
Royhisarmartahan@gmail.com

ABSTRACT

This paper sets out the issue of good corporate governance that exists in the Indonesian banking sector, which in recent years Indonesia ranks 11 out of 11 countries in ASIA in the application of good governance based on the data of the Asian Corporate Governance Association (ACGA) during 2007, 2010, and 2012. The focus of this paper is to look at the impact of the implementation of good corporate governance to financial performance of direct and indirect enterprise value. This study used path analysis, with secondary data sourced from existing financial statements on Indonesia Stock Exchange (IDX) for 5 consecutive years during 2008 to 2012. It is expected that this research can provide empirical evidence and significant impact to the banking industry, as well as academia and regulators to enhance shareholder value.

Keywords : good corporate governance, earning management,financial report, firm performance, firm value.

I. INTRODUCTION

Bank as a financial services and financial intermediary who accept deposits and channel deposit into in credit, either directly or indirectly to the way, capital market loan through where it can be said that the bank is an institution that between customer who have a surplus capital market with customers who need capital market. Thus it can be said that the bank is an institution that should be trusted by the people in the way that was owned by the customer assets.

Some evidence can be given as an example of such a case that hit the global investment bank Lehman Brothers, who perform 'cosmetic accounting' that caused collapse of the bank, Baring Brother which is the oldest bank in the UK which should eventually go bankrupt because of a loss of 827 million pounds as a result of trading , to the case of local banks that hit several banks in Indonesia starting from the case of Bank Century Bank Duta and losers clearing, which causes a deficit in the bank, Burglary case Citibank customer funds by the bank internally, until the case of Bank Indonesia Liquidity assistance (BLBI), which is a scheme BLBI aid (loans) provided by Bank Indonesia to banks experiencing liquidity problems at the time of the 1998 monetary crisis in Indonesia. This scheme is based Indonesian agreement with the IMF in addressing the crisis. In December 1998, the Bank has disbursed 147.7 trillion rupiah BLBI to 48 banks.

From this case, come into a series questions to the community as a stakeholder and specifically the investors, such as why that can happen? Do bank still can be called as an

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institution that can be trusted by the society and businesses? Why manipulation to investors continue to occur again? Why manipulation is often too late to be detected? And some of the questions which refers to the transparent and accountable performance of the company.

From that several question, this research is expected to provide benefits for science, especially in term of accountancy, financial accounting and behavior accounting, or is also expected to be able to contribute empirical evidence to banks practitioners and public about the impact of good corporate governance in banking industry that can have consequences for the decision makers.

II. THEORITICAL BACKGROUND

Implementation of good corporate governance in the banking sector especially in Indonesia refers to the rules made by Bank of Indonesia as central bank or regulator of all banks in Indonesia. Along with the demands for good corporate governance on the banking sector, Bank of Indonesia in 2006 initiated the regulations specifically governing the implementation of corporate governance provisions in the Commercial Banks. This study is based on Bank of Indonesia Regulation Number 8/4/PBI/2006 dated January 30, 2006 on the Implementation of Good Corporate Governance for Commercial Banks is again perfected through PBI. 8/14/PBI/2006 dated October 5, 2006 on the amendment of PBI. 8/4/PBI/2006 on Implementation of Good Corporate Governance for listed commercial banks stated that the implementation of GCG is mandatory. GCG implementation in this study based from the financial statements will be undertaken by the banks based on the principle of which 5 pillars of Transparency, Accountability, Responsibility, Independency and Fairness (TARIF).

Many previous studies on corporate governance and corporate values such as those made by Jensen and Meckling (1976) which states "nexus of contracts" between principal and agent, or research conducted by Scott (2002) the contract between the owners of fund with the company manager. Where between the agent and the principal wants to maximize the utility of each with the information held. On the one hand, agents have more information (full information) compared with the principal, giving rise to the asymmetry information ". This Asymmetry information caused a conflict of interest. Klapper and Love (2002), who argued that the GCG inefficiency and poor implementation of laws relating to the increased risk of investing in emerging market.

The financial statements are often manipulated by the agent for the benefit of the agent itself. Accrual method is often choice by the agent because it is more rational and fair view in reflecting the company's financial condition and overall in real terms, using the accrual basis, the agent can freely choose the method of accounting to be applied at the company as long as what was done does not deviate from the standard or regulation.

There are some patterns that motivate agents to engage the act of earning management; taking bath, income minimization, income maximization and income smoothing. An empirical evidence can be presented in the agent motivation in doing earning management in order to get bonus plan (Healy, 1985; McNichlos and Wilson, 1988; Jones 1991; Holthousen, Larcker, and Sloan, 1995), another motivation is contracting motivations where enterprises seek to delay or postpone debt due date (Sweeny, 1994; De Angelo, De Angelo and Skinner, 1994; Bowen, DuCharme, Shores 1995).

Banking performance measurement based on Bank of Indonesia Regulation / 6/10/PBI/2004 on banks performance measurement system, which includes an assessment of the

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factors CAMEL (Capital, Asset quality, Management, Earnings and Liquidity). Other studies reveal that the banking performance based on CAMEL significantly influence the firm value as seen from increase in stock price (Abdullah, Fariz and Suryanto 2004). From the literature mentioned above, the hypotheses in this study are as follows:

H_1 : Good Corporate Governance significantly affect to Firm Performance.
H_2 : Earning Management significantly affect to Firm Performance
H_3 : Financial Report Disclosure significantly affect to Firm Performance
H_4 : Good Corporate Governance have significantly affect to Price to Book Value.
H_5 : Earning Management significantly affect to Price Book Value.
H_6 : Financial Report Disclosure significantly affect to Price Book Value.
H_7 : Firm Performance significantly affect to Price Book Value
H_8 : Good Corporate Governance significantly affect to Earning Management
H_9 : Earning Management significantly affect to Financial Report Disclosure
H_{10} : Good Corporate Governance significantly affect to Financial Report Disclosure

III. RESEARCH FRAMEWORK AND METHODLOGY

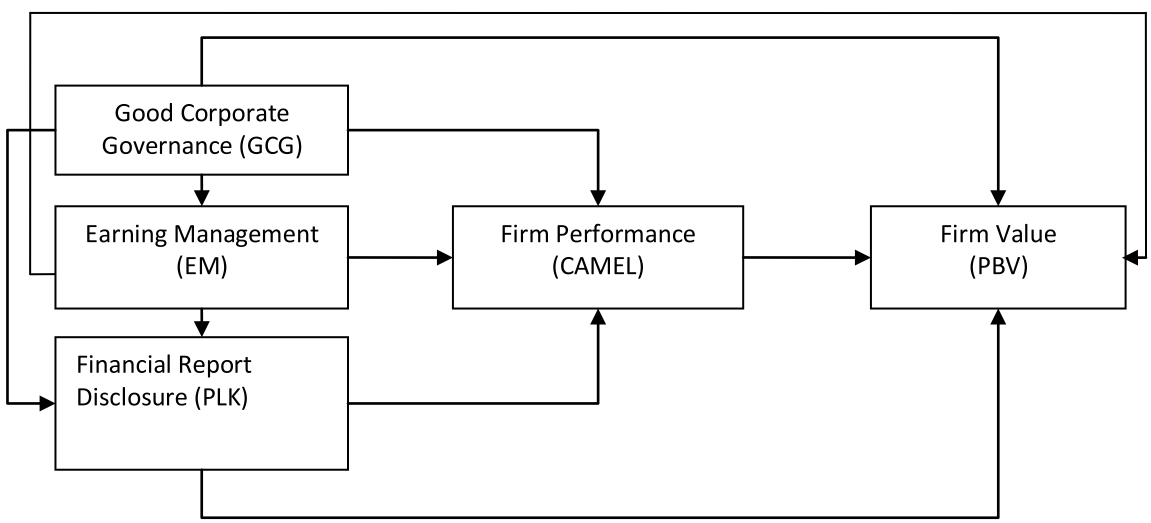

Fig. 1: Research Framework

Samples in this study were 30 commercial banks listed on the Indonesia Stock Exchange (IDX) during the years 2008 to 2012; the analysis technique used in this study is path analysis. Reason using path analysis is based on considerations, path analysis has the ability to combine multidimensional simultaneously and efficiently. Using path analysis is a Structural Equation Model (SEM), with Partial Least Square (PLS) technique. Model in this study can be formulated as follows:

$$PBV= f\ (GCG, CAMEL, PLK, EM) + \varepsilon$$

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IV. RESULT AND DISCUSSION

From the results in Table 1, it can be used by researchers to prove the hypothesis. Acceptance of the hypothesis used measure of the significance level of *T-value* table compare to *T-statistic*. If the value of *T-statistic* is higher than the value of *T-table* means that the hypothesis is accepted. For the 95 percent confidence level (alpha 5 percent) the value of the *T-table* for two-tailed hypothesis was > 1.96 and for a one-tailed hypothesis > 1.64 Hartono (2008). Based on the table above, it can be concluded that the hypothesis H_2, H_5 and H_8 are acceptable

Table 1. Coefficient test track

	Original Sample (O)	Sample Mean (M)	Standard Dev. (STDEV)	Standard Errors (STERR)	T Statistics (I/O STERR)
GCG -> CAMEL	-0.0576	-0.0606	0.1031	0.1031	0.5590
EM ->CAMEL	-0.1182	-0.1173	0.0522	0.0522	2.2640 *
PLK -> CAMEL	0.1001	0.1006	0.1060	0.1060	0.9442
GCG -> PBV	0.0394	0.0248	0.0832	0.0832	0.4734
EM -> PBV	-0.1896	-0.2209	0.0926	0.0926	2.0485 *
PLK -> PBV	-0.0754	-0.0401	0.1101	0.1101	0.6850
CAMEL -> PBV	-0.1921	-0.1633	0.1469	0.1469	1.3070
GCG -> EM	-0.3022	-0.3029	0.0445	0.0445	6.7963 *
EM -> PLK	-0.0634	-0.0648	0.0947	0.0947	0.6692
GCG -> PLK	0.0271	0.0353	0.0886	0.0886	0.3055

Source: proceed

Implementation of good governance or good corporate governance, it is must be disclosed by any bank listed on the Indonesia Stock Exchange. The central bank, Bank Indonesia in terms of the provisions states that GCG is mandatory for all banks operating in Indonesia. But in this study provides evidence that in contrast to a previous study conducted by Jensen Meckling where corporate governance has a significant influence on the performance of the company which is not evident in this study. The results provide an overview of this unique for Bank Indonesia as a regulator that GCG implementation is mandatory in regulation, but the monitoring should be reviewed furthers the mechanisms of its implementation.

This study confirms a previous study conducted by Ball and Brown was performed in 1968, in which researchers provide evidence that earning behavior management will be a direct impact on company performance. The practice of earnings management is driven by multiple motives that drive the agent to do so. In the above table also shows that the practice of earnings management is performed by an agent with a lower corporate profits, it can be seen from the negative value of which is in Table 1 motif is due to earnings management practice management (agents) have the freedom of choice in determining the method accounting records used in the company on the basis of accrual-based method. This method can be freely used by accountants as an agent of the company to meet the motivations of the other agents.

Disclosure of financial statements as an indicator of management (agents) in this study did not have a significant effect on corporate performance. There are several things that cause this is not significant. In the banking sector in Indonesia, where the central bank in this case is a bank of

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Indonesia, has an extremely dominant preventive role, this can be seen on the instrument the instrument is in CAMEL. The instruments were seen regarding the capital adequacy of Adequacy Capital Ratio (CAR), the minimum value is 8%. Bank Indonesia as the supervisor of banks in Indonesia indicate this strictly, the bank which has a CAR of less than 8%, in two consecutive years will be suspended in operation. This affects the performance of banks that are on average quite high.

Proof of implementation of good corporate governance in this study is also not proven. Direct implementation of good corporate governance has no significant effect on firm value, but when looking at the relationship between good corporate governance and earnings management, then it becomes logical, in which implementation of good corporate governance is a rule that will have a direct impact on the practice of earnings management behavior but not directly on the value of the company.

The value of the company is essentially influenced by the demand and supply of the company's stock price. Demand and supply is a market mechanism that cannot be controlled only by the application of good corporate governance. Implementation of Good Corporate Governance is directly able to be aligning information for the principal where principal basically have less information about the company than the agency as managers.

The direct effect of earnings management practices also have a significant effect on firm value with a negative direction, where the increase of earnings management practices will result in decreasing the value of the company. This decrease can be seen from Table 1 in the table, it can be seen that the value of the original sample showed a negative sign is equal to -0.1896.

Earnings management practices influence indirectly affect the value of the company. It is the impact of the earnings management practices that degrade the performance of the company. The company's performance is what gives a negative impact on the value of the company. In other words the practice of earnings management is detected on the actions taken by management as an agent of the company, the impact to the desire (demand) investors to invest in corporate banking. The practice of earnings management can be detected by looking at the performance of the company as indicated by the distribution of a portion of the company's performance in the form of dividend as a signal to investors and also to prospective investors.

Disclosure of financial statements should be reliable information for stakeholders. The financial report is a window for investors and prospective investors to invest their funds in the target company. Disclosure of financial statements that show the average-rate fair disclosure at this stage does not have an impact on the value of the company directly. Financial statements disclosure is a reflection of the performance of the agent. It is also proved that the characteristics of investors and prospective investors that there is on the market in Indonesia is investors who are "naïve" in which financial information is a reflection of the performance of the agent is not a major concern.

The results of this study showed that there was no significant relationship between the performance of the company (CAMEL) where the average performance of banking demonstrate good performance or the level of healthy / good, the value of the company that is Price to Book Value (PBV) it shows that the market value stock above book value, although not yet be said that the price of the stock on the banking industry over valued.

Insignificant performance in the banking industry, more due to the characteristics of the investor or prospective investor in this sector which most of them is the institution investor. The institutional investors have the characteristic that the information obtained from the performance derived from the company's financial statements, is not enough to convince and encourage

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investors in an effort to increase the demand for shares in the banking industry. This led to the hypothesis of the influence of performance on firm value is not proven.

Good Corporate Governance is a bridge to both stakeholders in a company, the principal and the agent. Implementation of Good Corporate Governance, in this study showed positive results with the implementation of Good Governance Corporate high enough, it is quite capable of reducing earnings management practices. Earnings management practices in this study decreased with increasing adoption of good corporate governance. Implementation of Good Corporate Governance is quite effective as a tool for principal "surveillance" effective. Regulation of the central bank is also petrified of a decline in earnings management practices by agents.

Implementation of Good Corporate Governance reflects that indirectly impact on increasing the value of the company. This is proof that the "conflict of interest" that exists in the Agency theory is true. With the implementation of good corporate governance is based on 5 pillars of applicable which transparency, accountability, responsibility, independency and Fairness (TARIF) this can be overcome well.

The practice of income smoothing is an option for the agent to determine the desired goal or target. Agents sometimes do things like income smoothing, income minimization, income maximization, and taking bath (Scott 2009). This will affect the financial statements are reflected in the final report prepared by the accountant. Basically, an accountant must be independent in the report, because the report made by the accountant should contain principles relevant and reliable, but it is sometimes violated, caused by the accountant are part of the agent, who has the same interests with other agents. Thus it seems that the financial statements prepared by the company still contain information that is biased because the interests of the agent contained therein. The dominance of the agent is also seen in a given financial reporting tends to stage fair disclosure, it demonstrates the desire of the agent to express its performance in the financial statements is not yet fully visible, still there is information that is not disclosed. This led to the practice of earnings management has no significant effect on the disclosure of financial statements.

The principle of transparency as one of the pillars that exist in the implementation of good corporate governance, not proven. This is due to the flexible regulation, which allowed the disclosure of financial statements in three stages which; adequate disclosure, fair disclosure and full disclosure. Agent is allowed to disclose financial statements on stage adequate disclosure. In the disclosure of adequate disclosure, not all of the information disclosed. Adequate disclosure gives leeway to the agent to provide standard financial reports such as balance sheet, profit and loss and cash flow, without providing any supporting notes of the financial statements. This is the cause of the implementation of good corporate governance does not significantly influence the Financial Statements.

V. CONCLUSIONS

In this research found evidence that the implementation of Good Corporate Governance which is important in the value of a company. The implementation for Good Corporate Governance is the key to increase the company's value even it is not directly, but with implementation of Good Corporate Governance is proven to be able to reduce earning management practices by accountant.

This study also proves that earnings management practices that can be derived by the implementation of good corporate governance directly. Implementation of Good Corporate

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Governance is viewed from the 5 pillars; Transparency, Accountability, Responsibility, and Fairness Independency, considered quite effective. Implementation of good corporate governance is in accordance with the applicable regulations.

Implementations of Good Governance Corporate also indirectly have a positive impact on the performance of the banking company, especially in terms of transparency, which that is one of the pillars implementation of good corporate governance. Transparency is considered important for the implementation of good corporate governance specially in banking sector which is a service industry, where service industries emphasizes "trust" which is the “oxygen” of the services industry and this can be accommodated by transparency.

Bank Indonesia as banking regulator in Indonesia, considered to be quite effective in implementing regulations which are made. The application for Good Corporate Governance as a bridge between the parties concerned where often has been conflict of interest in the company that is principal and agents, it can also be muffled.

It is expected that in the future the data in this study can be extended in order to provide an overview over the banking industry. With the broader picture is expected to provide a greater contribution to science with more sophisticated findings. For the banks this study is expected to provide a reference from another perspective in evaluating company performance, while for investors hoped this research can also add useful information for decision making and last for academics expected to add perspective and another point in assessing the performance of companies, especially in terms of the functions of auditors and dividends, which in some previous studies these two variables is a significant variable effect on firm value.

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