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MARKET INTEGRATION IN ASEAN:
SUSTAINABLE GROWTH AND CROSS - CULTURAL ISSUES

Ho Chi Minh City, Vietnam 18th - 20th March 2016

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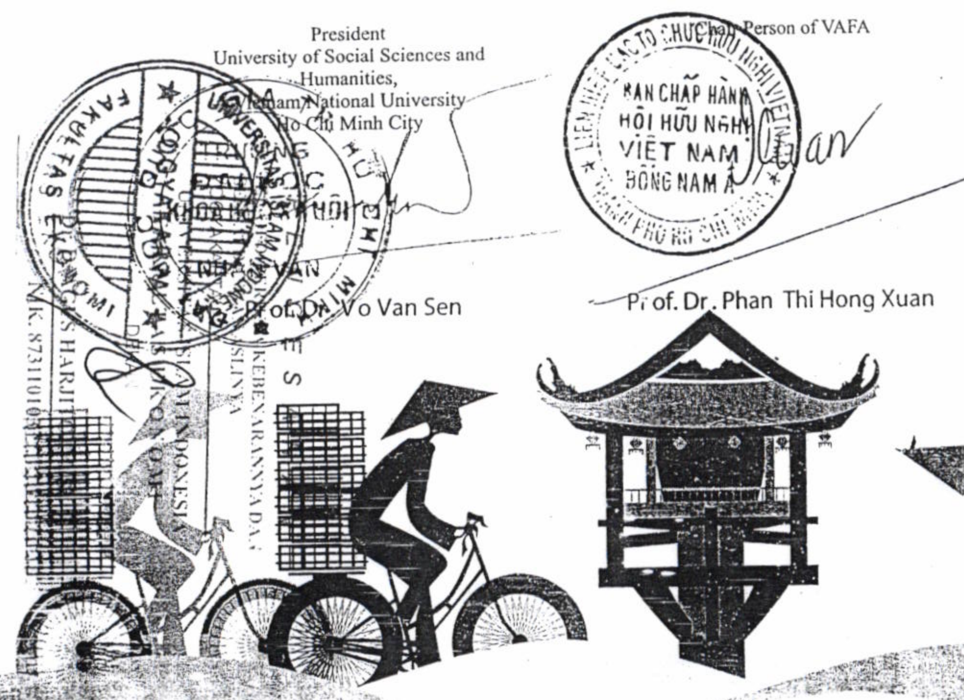

13th INSYMA

international annual symposium on management

MARKET INTEGRATION IN ASEAN: SUSTAINABLE GROWTH AND CROSS - CULTURAL ISSUES

Ho Chi Minh City, Vietnam 18th - 20th March 2016

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PENGESAHAN
TELAH DIPERIKSA KEBENARANNYA DAN SESUAI DENGAN ASLINYA
YOGYAKARTA
UNIVERSITAS ISLAM INDONESIA
FAKULTAS EKONOMI
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Proceeding

The 13th UBAYA International Annual Symposium on Management

MARKET INTEGRATION IN ASEAN: SUSTAINABLE GROWTH AND CROSS CULTURAL ISSUES

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Published by:

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  Phone: +62-31-2981139; Fax : +62-31-2981239
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ISBN (Indonesia): 978-602-73852-0-7
ISBN (Vietnam): 978-604-73-4020-0

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ISBN (Indonesia): 978-602-73852-0-7

THE EFFECT OF CORPORATE GOVERNANCE MECHANISM ON THE FINANCIAL PERFORMANCE OF MANUFACTURING COMPANIES WITH AGENCY COST AS THE INTERVENING VARIABLE

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ABSTRACT

The aim of this research is to analyze the effect of *Corporate Governance* mechanism consisting of the size of boards of Commissions, board of directors, independent Commissions, institutional ownership, managerial ownership, and audit committee on the financial performance of manufacturing companies from 2012 to 2014. This research also used the *agency cost* as the intervening variable. The population used in this research was the manufacturing companies registered in BEI (Indonesia Bursary Effect). The sampling was conducted using *purposive sampling* method from 30 manufacturing companies in each year. This research used the secondary data in the form of annual report of 30 manufacturing companies as registered in BEI (Indonesia Bursary Effect) from 2012 to 2014. The testing on hypothesis used the descriptive analysis, classical assumption test, and doubled linear regression. The results of the research showed that the size of the board of Commissions, independent Commissions, and audit committee had a significant effect on financial performance (ROE). The size of board of Commissions and independent Commissions had a significant effect on *agency cost*. The research result also showed that agency cost was not proven as the intervening variable between the mechanisms of *corporate governance* towards the financial performance (ROE).

Keywords: *corporate governance*, financial performance, *agency cost*
JEL Classification: G34

INTRODUCTION

Company refers to a corporation with certain vision and mission regularly and continually conducting its business activity to reach the company objective. The main purpose of company is to maximize the prosperity of shareholders. A good work performance of company is able to increase the value of the company represented with the price of stocks of company from time to time. There are a number of business persons

ISBN: 978-602-73852-0-7

using one of their companies to be a *go public* company, which is managed by separating between the function of ownership and function of management. Such separation might emerge an agency relation. In this case, the company will give an authority to the manager to make any decisions to realize the company objective. However, it does not guarantee that a manager will act based upon the main purpose of company. This cannot be separated from the personal interest motivation of the manager in company (Khoiruddin, 2011).

The conflict of interest might occur when there is a different interest between the managers and the owner, thus making a manager tend to make a decision that benefits to him/herself. This then can cause an *agency conflict*. To cope with this conflict, it can be done by controlling and monitoring the company management. This attempt later on also \can emerge a cost called as *agency cost*. Hence, *good corporate governance* is highly required to minimize the *agency conflict* and to maintain the sustainability of company.

A research conducted by Lindawati (2010) on the manufacturing companies that are registered in BEI (Indonesian Bursary Effect) showed that an institutional ownership and the size of the board of directors had an effect on the financial performance of company through *agency cost*. Meanwhile, a research by Faisal (2005) showed a different result stating that the relation between the institutional ownership and agency cost negative. Lindawati (2010) also stated that there was no any significant effect of managerial ownership measured using ROE. However, the result of this research is different from the research conducted by Ika and Wahyu 2013) in which their research showed that the managerial ownership and concentration of company ownership had a positive effect on ROA and ROE.

THEORETICAL REVIEW

Agency Theory explains that the relation of agency emerges when an individual or more (principle) hires or hire other people (agent) to give a service and then delegates the authority of decision making to the agent (Jensen and Meckling, 1976). This is in line with the *Agency Theory* emphasizing on the importance of the company owner (shareholder) to mandate the management of company to the professionals (agents). Manager as the agent has an obligation to maximize the prosperity of the shareholders. However, on the other side, the manager also has an interest to maximize his or her own prosperity. Sutedi (2012:14) stated that an authority of the one in charge of management to maximize the profit of company could lead to the process of maximizing the interest of his or her own management interest using the burden and cost that must be borne by the company owner. The difference of interest between management and the company owner can make the management to do some actions that are not beneficial for the company for a long term. Such difference of interest is called as *agency conflict*.

Lindawati (2010) stated that *corporate governance* is one of key elements in enhancing the economic efficiency including the relation among the management of company, board of directors, shareholders, and other stakeholders. *Corporate Governance* is a structure managing the pattern of the harmonious relation about the board of

ISBN: 978-602-73852-0-7

Commissions, directors, shareholders and other stakeholders. Such structure must be addressed and controlled well to achieve a balance of rights and obligations of all related parties in company. The owner (principle) can do a control to make the manager (*agent*) can do his or her tasks in accordance with the regulations defined. By implementing the controlling mechanism will emerge the cost called as the *agency cost*.

The variable studied here was the mechanism of internal monitoring covering the size of the board of directors, board of Commissions and independent Commissions. The mechanism of monitoring the ownership consisted of the managerial ownership and institutional ownership. Meanwhile, the mechanism of monitoring of the disclosure included the disclosure conducted by the audit committee. In measuring the financial performance of the company, it could be done by using *Return on Equity* (ROE) – measuring the company competence in obtaining the net profit based upon certain capital. It also could be done using ROE – measuring the ratio of net profit after the tax to its own capital stock as a measurement to measure to what extent the level of return in the form of percentage from the share given in the related business. Meanwhile, the *agency cost* can overall be measured using the means of asset turnover of company reduced by the annual asset turnover, which is the sale divided into the mean of total asset. .

PREVIOUS RESEARCH

Research conducted by Lindawati (2010) entitled "*Pengaruh Mekanisme Corporate Governance terhadap Kinerja Keuangan Perusahaan*" (The Effect of Corporate Governance Mechanism on the Financial Performance of the Company) was to test the effect of corporate governance on the financial performance of the manufacturing companies registered in BEI (Indonesian Bursary Effects) in the period of 2007 to 2009 through *agency cost* as the intervening variable. There were 41 companies used as the sample. The *corporate governonce* mechanism used in this research was the size of Board of Directors, the managerial ownership and the institutional ownership The financial performance of the company was represented using *Return on Equity* (ROE) and *agency cost* as the intervening variable. The analysis result showed that a number of corporate mechanism – institutional ownership and board directors had a significant effect on the financial performance through *agency cost*. What is similar with this research is that the writer studied about the effect of corporate governance mechanism on the financial performance of the company using *agency cost* as the intervening variable. In contrast, the differences were in the corporate governance mechanism in which the writer added a number of variables to be analyzed including the size of the board of Commissions, auditing committees and independent Commissions.

The research by Ridho and Aditya (2013) entitled "*Pengaruh Mekanisme Corporate Governance dan Struktur Kepemilikan terhadap Kinerja Keuangan Perusahaan*" (The Effect of Corporate Governance Mechanism and the structure of the ownership on the financial performance of the manufacturing companies registered in BEI (Indonesia Bursary Effect in the period of 2009 to 2011. The mechanism of *corporate governance* used by the researcher was the size of board of Commissions, independent Commissions,

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size of the auditing committees, institutional ownership and the managerial ownership. The research used ROA as the measuring tools to test such variables. The research conducted by Ridho and Aditya (2013) showed that the size of board of directors and the institutional ownership had an effect on ROA. However, the result of this analysis showed that the independent Commissions and the size of the auditing committees had a negative effect on financial performance of the company. What is similar with this research is when the writer studied the effect of *corporate governance* mechanism on the financial performance of the company. In addition, the writer also used a number of similar variables in the *corporate governance* mechanism including Board of Directors, size of Board of Commissions, Auditing Committee, Independent Committee, Institutional Ownership and Managerial Ownership. However, Ridho and Aditya differently only used ROA in doing an analysis on financial performance; while, the writer used ROE to measure the financial performance. In addition, the writer also used *agency cost* as the intervening variable.

The research by Ika and Wahyu (2013) entitled "Pengaruh *Corporate Governance* terhadap Kinerja Keuangan Perusahaan" (*The Effect of Corporate Governance* on the Financial Performance of Company") tested about the effect of *corporate governance* on the financial performance of the companies registered in BEI in the period of 2009 to 2011. The *corporate governance* mechanism used by the researcher to do an analysis included the independency of board of Commissions, size of board of Commissions, managerial ownership, concentration of ownership and leverages. The researcher used ROE, ROA, PER and Tobins'Q to do an analysis on the relation of *corporate governance* mechanism towards the financial performance of company. The research result showed that the size of board and concentration of ownership had a significantly positive effect on ROA. What is similar in this research is that the writer studied the effect of *corporate governance* mechanism on the financial performance of company represented using ROE; while, differently, the research by Ika and Wahyu added the variable of *leverage* in the *corporate governance* mechanism. Besides, in doing the analysis on financial performance, the writer used *agency cost* as the intervening variable.

HYPOTHESIS DEVELOPMENT

Commissions Board and Financial Performance

Based upon the general guidelines of *Good Corporate Governance* of Indonesia issued by Komite Nasional Kebijakan *Governance* (2006), it is stated that the Board of Commissions as the company organ collectively acts to and is responsible for monitoring and advising the directors and ascertaining that the company has performed a good company management. Chtourou et al. (2001) stated that the higher the number of boards, the better the mechanism of monitoring the company management. The size of the board of Commissions has a critical role in monitoring and controlling the company management. A better performance of board of Commissions in monitoring the company management could minimize the agency cost in which later on it can influence the financial performance of company. Based on the explanation above, the hypotheses proposed are as follows:

H1: : The size of the Board of Commissions has a significant effect on the Financial Performance represented using ROE.

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H1b: The size of the Board of Commissions has a significant effect on the Financial Performance (ROE) through *agency cost.*

Board of Directors and Financial Performance

The size and the composition of the Board of Directors can influence the level of effectiveness in doing the monitoring activity. The bigger size and the composition of the board of directors will bring a positive effect on the work performance and the value of the company if the composition of the board of directors is more dominated by the board of directors coming from the outside of the company; while, the performance and value of the company will be at lower level if the size and the composition of the board of directors come from the inside company (Bambang, 2013). Pfeffer and Salancik (1978) cited from Ridho and Aditya (2013) explained that the higher the needs for a more effective external relation, the higher the needs for the more number of boards. Hence, the board of directors play a role in the work performance of the company and can reduce the conflict of agency occurred in the company and can reduce the agency cost. Based on the explanation above, then the hypotheses proposed are as follows:

H2a: The size of the Board of Directors has a significant effect on the Financial Performance represented using ROE.

H2b: The size of the Board of Directors has a significant effect on the Financial Performance (ROE) through *agency cost.*

Independent Commissions and Financial Performance

The existence of the Board of Independent Commissions in a company can bring an effect on the integrity of a financial report made by the management. If the company has the independent Commissions, then the financial report presented by the management tends to be more integrated as in a company there is a division directly monitoring and protecting the rights of the external parties of the company management (Bambang, 2013). Ridho and Aditya (2013) stated that the larger independent Commissions can give a power to the board of Commissions to press the management in enhancing the quality of disclosure. A better monitoring can enhance the financial performance. Based on the explanation above, then the hypotheses proposed are as follows:

H3a: The Independent Commissions has a significant effect on the Financial Performance represented using ROE

H3b: The Independent Commissions has a significant effect on the Financial Performance (ROE) through *agency cost.*

Institutional Ownership and Financial Performance

The institutional ownership is the shareholding by the financial institution such as insurance companies, bank, pension fund, investment banking (Siregar and Utama, 2005; in Bambang, 2013). The share percentage of the institution is obtained from the accumulation of the share percentage of other domestic or foreign companies and the share owned by the domestic or foreign companies. The more institutional ownership not only could reduce the

conflict between the shareholders and the managers but also could minimize the agency cost. Based on the explanation above, then the hypotheses proposed include:

H4a: The Institutional ownership has a significant effect on the financial performance represented using ROE.

H4b: The institutional ownership has a significant effect on the Financial Performance (ROE) through *agency cost.*

Managerial Ownership and Financial Performance

The managerial ownership refers to the number of shareholding by the management from all of the managed capital stocks of company. Jensen and Meckling (1976) stated that *agency cost* will be lower in a company with a high managerial ownership. A company with the large number of managerial ownership tends to have a lower level of agency conflict and agency cost. A lower level of agency conflict can be reflected from the high level of active circle and lower burden for the operation towards the company sale. Based on the explanation above, then the hypotheses proposed include:

H5a: The Managerial Ownership has a significant effect on the Financial Performance represented with ROE

H5b: The Managerial Ownership has a significant effect on the Financial Performance (ROE) through *agency cost.*

Audit Committee and Financial Performance

The Audit committee as stated by the Komite Nasional Kebijakan *Governance* (2006) acts to help the Board of Commissions to ascertain that the financial report has been reasonably presented in accordance with the general accounting principles, structure of controlling the internal company has been well implemented, the implementation of the internal and external audit has been conducted in accordance with the audit standard applied and to follow up the findings from the audit conducted by the management. According Ridho and Aditya (2013), the size of audit committee can enhance the effectiveness of audit committee that, later on, can prevent any bad managerial actions. Given such preventive action, the performance of the company could be improved. Based on the explanation above, the hypotheses proposed include as follows:

H6a: The Audit Committee has a significant effect on the Financial Performance represented using ROE.

H6b: The Audit Committee has a significant effect on the Financial Performance (ROE) through *agency cost.*

RESEARCH METHOD

Population and Research Sample

The population used in this research was the manufacturing companies registered in BEI (Indonesian Stock Exchange). The sampling method was conducted using *purposive sampling* method in which a sample was taken using consideration. The criteria of the sampling in this research were that the company in a row has been registered in BEI from 202 to 2014.

The Variable and Definition of Variable

This research involved independent variable, dependent variable and intervening variable.

1. Dependent Variable
   Dependent Variable in this research refers to the financial performance of the manufacturing companies. In this research, it refers to the financial performance of the manufacturing company. The financial performance is represented using ROE, which in a company can be calculated from the profit after the tax has been divided with total equity.
2. Independent Variable
   In this research, Independent Variable refers to the mechanism of corporate governance represented using the size of board of Commissions, size of the board of directors, independent Commissions, institutional ownership, managerial ownership and audit committee. The institutional ownership is measured using the ratio scale through the number of shares owned by the institutional investors in comparison to the total share of company. Meanwhile, the Managerial Ownership can be measured using the ratio scale through the percentage of the number of shares owned by the management for all of share capital circulated. The size of the Board of Commissions is measured based upon the total members of board of Commissions consisting of Commissions and independent Commissions. The size of the Board of Director is from the number of the members of the existing directors in the company. The Independent Commissions were measured using the ratio scale through the percentage of the members of the board of Commissions coming from the outside of the company from the total of the size of Commissions board members. The Audit Committee was measured using the ratio scale through the percentage of the member of audit committee coming from the outside audit committee towards all of the members of audit committees.
3. *Intervening* Variable
   Intervening Variable in this research included *agency cost* which is measured using the rate of the asset turnover of company overall and reduced with the asset turnover in each year. The *Asset turnover* can be counted from the sale divided with the total asset.

DATA ANALYSIS METHOD

The technique of data analysis used to test the hypotheses formulated in this research refers to the descriptive-statistical analysis, path analysis, and test of classical assumption, doubled regression analysis, t-test and f-test with the help of *SPSS for Windows*.

The test of hypothesis in this research used the doubled regression. The equations of doubled regression formulated are as follows:

ROE = a+ **b1 BOC + b2 BOD + b3 ID + b4 IO + b5 MO + b6 AC +e**

AGC = a+ **b1 BOC + b2 BOD + b3 ID + b4 IO + b5 MO + b6 AC +e**

RESULTS AND DISCUSSION

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The regression equation in this research, after being tested for the normality with the plot, showed that the data had a normal distribution. The regression equation in this research also has been tested with the classical assumption in which the results showed that there was no any multicollinearity, heteroscedasticity and autocorrelation in the regression model. This research used the doubled regression analysis and the equation of the doubled regression results on the significances as follows:

Table 1
Corporate Governance on ROE and Agency Cost

	ROE.	AGC.
(Constant)	0,000	0,418
BOC	0,050	0,025
BOD	0,107	0,227
ID	0,000	0,013
IO	0,064	0,993
MO	0,701	0,092
AC	0,007	0,735

The effect of board of Commissions on the financial performance (ROE) and AGC

The result of the test on the regression showed that the size of the board of Commissions had a significant effect on the financial performance represented using ROE. Thus, H1a was accepted. This can be seen from the level of significance at 0,050 (sig. <0, 05). The result of the finding supports the theory stating that the size of the board of Commissions determines the level of effective supervision in monitoring the work performance of the management. Chtourou et al. (2001) stated that the more increasing number of the boards can make the mechanism of the monitoring the company management better. BOC also had an effect on the *agency cost*. Hence, H1b was accepted. The result of this finding is in line with a theory of Arifin (2002) stating that a mechanism to minimize the agency matters is the mechanism of control using monitoring that can be done with the establishment of Board of Commissions. The board of Commissions dominated by the outside members of the Commissions can make the monitoring process of the board of Commissions to the manager more effective. An effective monitoring towards the manager conducted by the board of Commissions will minimize any potential fraud act of the manager in managing the company; thus it minimizes *agency cost*.

The effect of Board of directors on the financial performance (ROE) and AGC

The test result on the regression showed that the size of board of directors (BOD) had no any significant effect on the financial performance represented using ROE. Hence, H2a is unaccepted. This can be seen from the significance level for BOD towards ROE and ROA, each of which was at 0,107 (sig. >0.05). The result of the finding did not support the

theory stating that the increase of the size and diversity from the Board of Directors has an effect on the financial performance of company as it can give benefits for the company in the form of the creation of the network of the outsider of the company and can guarantee the availability of the resources (Pearce & Zahra, 1992 in Faisal, 2005). The result of the findings stated that the size of Board of Directors had no any significant effect on the financial performance represented with ROE. This is because there were a number of companies in which the composition of their board of director is dominated by the board of directors coming from the internal company. Such condition can make the performance and the value of the company cannot improve optimally. The result of the analysis showed that the size of the board of directors had no any significant effect on the *agency cost*; thus H2b was unaccepted. In this research, the average of the number of board of director was quite more. The too many compositions of the board directors and unbalanced with the composition of the board of Commissions can make the monitoring to the manager ineffective for the lack of synergy between the board of Commissions and board of directors.

The effect of the independent Commissions on the ROE and AGC

The result of the regression test showed that the independent Commissions (ID) had a significant effect on the financial performance represented with ROE. Then, H3a was accepted. This can be seen from the significant level for ID towards ROE at 0,000 (sig. <0, 05). This result of the finding is supported by a theory stating that the larger the independent Commissions can give the power to the board of Commissions to press the management to improve the quality of the disclosure (Haniffa and Cooke, 2002; in Ridho and Aditya, 2013). In this case, the independent Commissions is the members of the board of the Commissions that are not affiliated with the directors, member of other board of Commissions and controlling shareholders, and free from any business relation that can affect their competence to act independently merely conducted for the interest of the company. The result of the regression analysis showed that the independent Commissions had a significant effect on the *agency cost*. Thus, H3b was accepted. The Independent Commissions that had no any business or kinship relation with the Commissions and the directors will be more objective in doing monitoring and the assessment towards any actions of the managers. The Independent Commissions that can act independently can maximize their competence in monitoring the manager; then, it can minimize any frauds conducted by the manager towards the company for their own interest.

The effect of the institutional ownership on ROE and AGC

The result of the regression test showed that institutional ownership (OI) had no any significant effect on the financial performance represented with ROE. Hence, H4a was unaccepted. This can be seen from the significant level for IO towards ROE at 0.064 (sig. >0.05). This is not in line with the theory, as stated by Jensen and Meckling (1976), stating that the institutional ownership is one of tools that can be used to reduce any *agency conflict*. The result of the finding also showed that ID had no any significant effect on

agency cost; hence H4b was unaccèpted. The result of the findings supported a research conducted by Bambang (2013) stating that the more the number of the institutional ownership, the more decreased the banking performance. The large institutional ownership is the majority of the owner and tends to ignore the interest of the minority share. In this case, the higher control from the external parties can make the policy taken tends to follow the policy from the external institution.

The effect of managerial ownership on the financial performance (ROE) and AGC

The result of the regression test showed that the managerial ownership (MO) had no any significant effect on the financial performance represented with ROE. Thus, H5a was unaccepted. This can be seen from the significant level for MO to ROE and ROA with 0.701 on each (sig. >0.05). The result of the test also showed that MO had no any significant effect on *agency cost*. Thus, H5b was also rejected. This is not in line with the theory of Jensen and Meckling (1976) that stated that the managerial shareholding can help to unite the interest between the shareholders and manager. The more increase the proportion of the managerial shareholding, the better the performance of the company. However, the result of this testing is in line with the research conducted by Ridho and Aditya (2013) that stated that the managerial ownership has the share in little amount (minority) that can make other shareholders attempt to monitor and influence the managerial decision making thus the process of the decision making inflexible and slow. Based on the descriptive analysis, the average value of the managerial ownership in the manufacturing company is categorized little. The managerial ownership at the low level can make the manager less maximal in doing his or her duties to maximize the wealth of the shareholders that is by improving the company performance using ROA and attempts to shift the resource of the company for their own interest (Jensen & Meckling, 1976).

The effect of the audit committee on the financial performance (ROE and ROA)

The result of the regression test showed that the Audit Committee (AC) had a significant effect on the financial performance represented using ROE. Thus, H6a is accepted. This can be seen from the significance level for AC towards ROE at 0,007 (sig<0,05). The result of this research was not in line with a research conducted by Ridho and Aditya (2013) stating that the company merely does the formality in obeying the rules about the minimum number of the audit committee in a company. The formality in obeying the regulations about the number of audit committee causes the effectiveness of audit committees in doing their task not optimal. However, the result of this research was in line with the research conducted by Sam'ani (2008) in Ridho and Aditya (2013) stating that the audit committee has a critical and strategic role in maintaining the credibility of the process of drafting the financial report of company such as maintain the running of the sufficient company system and the implementation of GCG. Given the effective function of audit committee, then the function of monitoring towards the company management will be better and can prevent any agency conflict and can improve the financial performance.

ISBN: 978-602-73352-0-7

The result of the test also showed that the audit committee had no any significant effect on *agency cost.* Hence, H6b was not accepted. There are a number of companies that do the election of the member of audit committee only based upon the position of the kinship. This then has caused the performance of the audit committee is not optimal as in such position; the audit committee is in the difficult position to act independently and objectively. The performance of the audit committee that is not optimal can give any freedom for the managerial parties to make the financial report not transparent, thus, the information given can be inaccurate. This then can emerge the asymmetric information – an unbalanced information as the distribution of the information is not equal between the management (managers) and the owners (shareholders). In this case, the manager does not provide information comprehensively to the shareholders related to the achievement. As a result, the shareholders will not obtain complete information. This can emerge the agency issue; thus the company will burden more *agency cost* to do monitoring.

Table 2

Test result of the hypothesis with the intervening variable of *agency cost*

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	20.862	2.433		8.576	.000		
	AGC	-.094	.040	-.240	-2.318	.023	1.000	1.000

a. Dependent Variable: ROE

Based on the regression analysis as presented in Table 3, it can be seen that the value of significance of *agency cost* is at 0,023 (0,023<0,05). This then shows that the agency cost has a significant effect on the financial performance of manufacturing company represented using ROE.

The conditions that the mechanism of *governance* has an effect on the financial performance (ROE) through *agency cost* as the intervening variable:

1. Mechanism of *Corporate Governance* refers to the Board of Commissions (BOC), size of Board of Directors (BOD), Independent Commissions (ID), institutional ownership (IO), Managerial Ownership (MO) and Audit Committee (AC) that have no any significant effect on the financial performance (ROE).
2. Mechanism of *Corporate Governance* refers to the size of the Board of Commissions (BOC), size of Board of Directors (BOD), Independent Commissions (ID), Institutional ownership (IO), Managerial Ownership (MO) and Audit Committee (AC) that have a significant effect on the financial performance represented with *Agency Cost.*
3. *Agency cost* has a significant effect on the financial performance (ROE)

ISBN: 978-602-73852-0-7

Based on the conditions above, *agency cost* in this case was not proven as the intervening variable between the mechanism of corporate governance and the financial performance of (ROE) of manufacturing companies.

CONCLUSION AND RECOMMENDATION

Based on the test and discussion of the effect of corporate governance mechanism on the financial performance of manufacturing companies represented through ROE and *agency cost* as the intervening variable, then it can be concluded that *Agency cost* is not proven to be the intervening variable between the mechanism of *corporate governance* on the Return of Equity (ROE) of manufacturing companies. There was a significant effect of mechanism of *corporate governance* on the Return of Equity (ROE) of manufacturing companies. There was a significant effect of agency cost on the Return of Equity (ROE) but the size of Board of Commissions (BOC), Board Commissions (BOC) had no any significant effect on the performance through agency cost.

Board of Commissions also had a significant effect on the Return of Equity (ROE) and the agency cost. Similarly, the Independent Commissions (ID) statistically has a significant effect on ROE and *agency cost*. However, ID had no any significant effect on the financial performance (ROE) through *agency cost*. The institutional ownership statistically also had no any significant effect on ROE through *agency cost*. However, the managerial ownership statistically had no any significant effect on ROE and *agency cost*.

A significant effect was also found from the audit committee on ROE as the proxy of the financial performance of the company. Statistically the audit committee had no significant effect on ROE through *agency cost*. In a company, the audit committee is led by one independent commissary. A large company will have a high business complexity, in his case the audit committees will find difficult to do their tasks and responsibilities; thus, it is possible to make the performance of committee not maximal.

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ISBN: 978-602-73852-0-7