Malaysian Accounting Review, Vol. 10 No. 1, 17-42, 2011

CORPORATE GOVERNANCE AND PERFORMANCE: EVIDENCE FROM AN EMERGING MARKET

Siti Nuryanah
Universitas Indonesia, Indonesia

Sardar M. N. Islam
Victoria University, Australia

Abstract

This study investigated the relationships between the internal corporate governance mechanisms and firm performance in Indonesia. Recognising weak external mechanisms of Indonesian corporate governance, this study focused on the internal mechanisms, hence offering considerable insights for the understanding of the relationships between internal corporate governance mechanisms and performance in Indonesia. The main proposition of this study was that the traditional findings on the relationships between internal corporate governance mechanisms and company performance relevant to developed countries were not appropriate for emerging markets like Indonesia where the business environment is different as, for example, the capital market is still under-developed, and the regulatory framework is weak. Using a panel data during 2002-2004, the findings show that all internal mechanisms except size of both board and audit committee, and management ownership are significant in explaining company performance. Specifically, some results on the audit committee are different to the literature of best practice of audit committee. The findings, therefore, support our proposition that the role of some specific aspects of internal corporate governance mechanisms affecting company performance does not exist in Indonesia.

Keywords: *Corporate governance, internal mechanisms, Indonesian Code of Corporate Governance, JSX*[1]*, company performance.*

Introduction

It has been a decade since the economic crisis hit Asia causing a prolonged financial crisis suffered by some Asian countries including Indonesia. Many studies indicate that fundamental fragility of the economy and poor corporate

ISSN 1675-4077

governance were the main factors of the crisis (Johnson, Boone, Breach and Friedman, 2000; Barton, Felton and Song, 2000; Claessens and Fan, 2002). Indonesia began its economic recovery programs by strengthening the corporate governance systems. This was also one of the points in the IMF package of economy recovery planning for Indonesia (IMF, 1997). Indeed, good corporate governance not only improved the economy of the country (OECD, 2004) but also increased the performance of individual companies (McKinsey, 2002; Gompers, Ishii and Metrick, 2003). Therefore, it is important, to assess the implementation of the corporate governance practices ensuring that they achieved the recovery and improved the business practices of listed companies in Indonesia. Based on the authors' observation, there are only few official evaluations undertaken by the regulators or the government except for the corporate governance country assessment completed by the World Bank in 2004. In fact, such exercises are crucial to determine the efficiency and effectiveness of the corporate governance practices. Studies on the implementation of corporate governance in Indonesia indicate that the corporate governance practices are still not effective (JSX, 2003; CGFRC, 2004).

The main motivation for this study was to examine the effectiveness of the corporate governance practice in Indonesia by examining the relationship between internal corporate governance mechanisms and company performance. In emerging markets like Indonesia when the external governance is less effective and the legal protection for investors is weak, internal governance mechanisms, such as, board governance become more important to mitigate conflict of interests amongst stakeholders (Young, Peng, Ahlstrom, Bruton and Jiang, 2008). This study presents empirical evidence which differs from earlier regional studies, such as, Darmawati et al. (2004), because rather than examining the broad issues of corporate governance, this study focused on the internal mechanisms of Indonesian corporate governance so that a precise implication could be drawn. For this purpose, the study investigated Indonesian publicly listed companies on Jakarta Stock Exchange (JSX).

The results of relationships between internal corporate governance mechanisms and performance show that the independence of both board and audit committee is an important attribute that can affect a company's performance. Similarly, both outsider ownership (institutional and individual ownership) and leverage also impact company performance. The study failed to detect any relationship between size of both board and audit committee, and company performance. The results suggest that management ownership does not affect company performance. Finally, the result shows that a company having an audit committee chaired by an independent member and one of its members having accounting/financial qualification has a negative impact on performance. This is in contrast with the recommendation of best practice for good corporate governance (JSX, 2000; NYSE, 2008; ASX, 2007, 2010; Nasdaq, 2006, 2008).

The structure of this paper is as follows. The next section reviews the literature relating to corporate governance and firm performance, and then builds the hypotheses for the study. Section 3 discusses the research methodology and econometrics modelling of the study. Section 4 shows details of the results, and then Section 5 discusses the implications of the study. The final chapter is the conclusion.

Literature Review and Hypotheses Development on Corporate Governance and Company Performance

Corporate Governance and the Practice in Indonesian Corporations

Corporate governance as a concept gained its momentum due to the previous corporate collapses, such as, Enron and WorldCom, and the 1998 Asian financial crisis, even though it had been discussed previously in the agency theory of Jensen and Meckling (1976, p. 2) and long before in Adam Smith's era (Farinha, 2003). Based on the agency theory, the objective of corporate governance is to minimise conflict of interests not only between the management and the owners but also between all internal and external stakeholders thereby creating and improving shareholders' wealth (Farrar, 2005).

Effective corporate governance results in the use of resources of a company efficiently, thereby underpinning growth (OECD, 2004, p. 11). In addition, according to the comment on major governance reforms initiated by three major U.S. stock exchanges, Brown and Caylor (2008, p. 2) argue that "ceteris paribus, greater controls over managerial actions should reduce principal-agency problems, enhancing firm performance". Good corporate governance practice is also positive to the market as found by Gompers et al. (2003) that firms with good corporate governance practice "had higher firm value, higher profits, higher sales growth, lower capital expenditures, and made fewer corporate acquisitions". Furthermore, the global investor survey of McKinsey (2002, p. 2) confirms that "a majority of investors are prepared to pay a premium for companies exhibiting high governance standards". There is compelling evidence in current literature, which find a positive relationship between good corporate governance practice and company performance (Black, Jang and Kim, 2006; Brown and Caylor, 2004; Beiner, Drobetz, Schmid and Zimmermann, 2004; Gompers et al., 2003). These favourable results generally show that good corporate governance practice implemented by a company benefits the company in terms of accounting profit and market return.

Despite the fact that good corporate governance increases the company's value, Iskander and Chamlou (2000) argue that the successfulness of corporate governance practice, which leads to company's value improvement, can be influenced by both external and internal factors. These factors are known as internal and external corporate governance instruments by other corporate governance scholars. The internal factors are related to board governance issues, such as, size of the boards, composition of the boards, leadership of the boards, compensation for the boards, size of the company, financial conditions, leverage, product uniqueness and ownership structure (Adams and Mehran 2003; Gillan and Starks, 2003; Hermalin and Weisbach, 2003; Barnhart and Rosenstein, 1998).

On the other hand, the external factors refer to external corporate governance mechanisms as firstly, legal systems are matter for good corporate governance (Klapper and Love, 2004). In the environment where shareholder protection and judicial efficiency is weak, improving the quality of corporate governance is important as it could increase the company's performance and valuation (Klapper and Love, 2004). Similar to this, is market for corporate control that impacts the pressure on managers, and causes changes to other (internal) governance mechanisms (Bushman and Smith, 2001). As mentioned by Bushman and Smith (2001, p. 296): “the adoption of anti-takeover legislation reduces pressure on top managers, and causes firms to substitute more intensive incentives elsewhere”. They also argue that “well-functioning capital markets facilitate corporate takeovers that replace underperforming manager” (p. 296).

Regarding the external mechanisms, Capulong, Edwards, Webb and Zhuang (2000) found that Indonesia has an under-developed capital market, and weak legal and regulatory framework. Therefore, in the emerging markets like Indonesia, since the external governance is less effective and the legal protection is weak, internal governance mechanisms, such as, board governance are important to mitigate conflict of interests amongst stakeholders (Young et al., 2008). Coincidentally, looking back at the corporate governance practice in Indonesia, since 1999 following the financial crisis, the Indonesian regulatory has issued code of corporate governance that is mainly applicable for board governance[2]. One of the provisions in the codes, which is issued by Jakarta Stock Exchange (JSX), requires every publicly listed companies to have a board governance structure that consists of: 1) at least 30% of independent commissioners, 2) an audit committee, with at least three people and that, one of them must be an independent commissioner who also acts as a chairman of the committee, and at least one of the members must be accounting and/or financial literate, and 3) a corporate secretary.

An Indonesian regional study of Darmawati, Khomsiyah and Rahayu (2004) could not find a relationship between corporate governance practice and market performance. This finding confirms the findings of other studies on the implementation of corporate governance in Indonesia, which indicate that the Indonesian corporate governance practices are still not effective (JSX, 2003; CGFRC, 2004). Based on this literature and overview of external mechanisms Indonesian corporate governance, the study proposed that the standard relationships between internal mechanisms of corporate governance and company performance found in other studies in developed countries did not exist in an emerging market like Indonesia. The following paragraph presents literature on the internal mechanisms of corporate governance and the practice in Indonesia.

Internal Corporate Governance Mechanisms: Literature and Practice in Indonesia

Board Governance

Board practices have been prominently discussed in the literature since it is the apex of a corporate system; the effectiveness of corporate governance practice is a function of the board. The board has a vital role to play in a company, as its function is to manage and direct the management (Farrar, 2005). It also plays a monitoring role since the separation between ownership and control within the company (Jensen and Meckling, 1976). In the emerging markets, the board becomes important tools complementing for the inefficient external corporate governance mechanisms to alleviate conflict of interests amongst parties (Young et al., 2008). According to Van den Berghe and Levrau (2004), there are three main characteristics for a good board, which are related to composition, size and leadership structure.

The composition of a board is important; Nonetheless, there are many perspectives on whether a company should have more insiders than the outsiders or vice versa. In fact, there are at least six different perspectives, from which the board roles are derived, which cause board composition between companies or amongst countries to be different. The perspectives are: resource dependent theory, agency theory, stakeholder theory, stewardship theory, institutional theory, and management hegemony theory (Van den Berghe and Levrau, 2004; Hung, 1998). Based on these six theories, six roles of governing boards can be identified: a linking role (from resource dependency theory), a coordinating role (from stakeholder theory), a control role (from agency theory), a strategic role (from stewardship theory), a maintenance role (from institutional theory), and a support role (from managerial hegemony theory) (Hung, 1998). These board perspectives vary the board composition since, for example, the agency theory is a countervailing perspective to the stewardship theory; while the agency theory recommends the majority of non-executive directors on the board and the stewardship theory supports a bigger composition of executive directors (Van den Berghe and Levrau, 2004).

Despite the diverse perspectives on board composition, it is clear that there is a requirement for independent directors and non-executive directors as all corporate governance practices around the world suggest that an independent member should be included on the board. Independent directors minimise the agency cost as they make the monitoring role and the strategic planning role of the board more effective (Berle and Means, 1933). Considered as an important attribute of a good board, Indonesia in its corporate governance practice suggests that every listed company have at least 30% of its board independent members [3].

While there is consensus that independent member(s) improves the quality of the board, empirical studies have had difficulty in finding supporting evidence. This can be seen for example in the empirical study by Lawrence and Stapledon (1999). Examining the impact of independent directors on corporate performance and executive remuneration, they could not find that these types of directors affect firm value (both in terms of accounting and share-price measurement). Abdullah (2004) could not find either the relationship between independent boards and firm performance. Abdullah (2004) is suggests study failed to find a relationship between the variables due to using financial ratios as a proxy for firm performance. While the company's growth measurement reflected long-term performance of the firm, the financial ratios might only measure short-term firm performance. Abdullah's study implies that a time lag should be considered when investigating the relationship between board independence and the company performance.

Whether independent directors are important for boards seem still debatable since it is difficult to find conclusive evidence. A study of Barnhart and Rosenstein (1998), on examining the sensitivity of simultaneous equations, found support for a curvilinear relation between insider ownership and the company performance, but weak evidence for a curvilinear relation between performance and the proportion of outside directors. A long horizon study by Bhagat and Black (2002) also confirms no evidence that companies with bigger numbers of independent directors can perform better than other companies. Furthermore, their study suggests that the strategy taken by low-profitability companies to hire more independent directors in order to increase performance, does not work. Finally, DeAndreas, Azofra and Lopez (2005), combining regression analysis with simultaneous equations, also confirmed the unclear relationship between the proportion of outside directors (a proxy for board independence) and firm value.

For the purpose of this study, since the Indonesian code of corporate governance compeled every listed company to have independent commissioners, the relationship between independency of board and company performance was tested by the following hypothesis:

H_1 : There is a positive relationship between the proportions of independent commissioners and company performance.

In addition to board composition, the second important characteristic for good board is size of the board. The board size might influence the dynamics in board functions. For example, a large and diverse board of directors may increase board performance in terms of knowledge and skills. On the other hand, this type of board potentially may face group dynamics problems, which in turn make the board less effective (Van den Berghe and Levrau, 2004). Hermalin and Weisbach (2003), argued that the relationship between board size and a company performance showed consistent results of a negative relationship. Supporting this, the study of DeAndreas et al. (2005) found out that in OECD countries the association between the board size and firm value to be negative. This negative relationship was persistent after testing for robustness by controlling the variables board composition, internal functioning, country effect, industry effect, and market performance measurements.

The statement of Hermalin and Weisbach (2003) above is contradicted by other studies as a meta-analysis of Kiel and Nicholson (2003) found a positive correlation between board size and a market-based company's performance, but not for accounting based performance measurement. The study of Beiner et al. (2004), modelling the interrelationships between the influencing aspects and mechanisms, such as, leverage and ownership structure, could not find a significant association between board size and firm valuation. Similarly, Kula (2005) found no significant results of the effect of the structure variables, i.e., size, the proportion of independent directors and the board committees' structure, on firm performance. Using a banking sample, Adams and Mehran (2005) could not find either a relationship between board size and firm value. Finally, in an emerging market study, Jaafar and El Shawa (2009) found that board size significantly influenced firm performance, while Suntraruk (2009) found that board size was not significant.

For this study, the relationship between size of board and company performance was tested by hypothesis as follows:

H_2 : There is a significant relationship between the board of commissioners' size and company performance.

Turning to the third effective board factor, a board leadership structure is derived from two opposition theories, namely, agency and stewardship theory. According to Van den Berghe and Levrau (2004), agency theory recommends separation of the roles of CEO and chairperson on the board, hence reducing the domination of management on the board. In contrast, the stewardship theory advocates a unitary structure where a CEO also serves as the chairperson, to increase the trust and the motivation of the board. Similar to the other elements of good boards, vexing results are found in the board leadership structure. The current study of Suntraruk (2009) in the emerging market finds that CEO duality is insignificant to company performance. Previously, the study of Dalton et al. (1998) and Abdullah (2004) could not find a relationship between the leadership structure and firm performance. On the other hand, the study of Kula (2005) found a positive impact of separation between the chairperson and general manager on a company's performance. Compared to Abdullah (2004), Kula used multiple indicators of firm performance such as indicators of dividends, profits, sales volume and market share.

Regarding the leadership of a board, the hypothesis that was tested in this study is as follows:

H_3 : A company with a board led by an independent commissioner has a better performance than a company which does not have this attribute.

Having characteristics of a good board, board also establishes committees in order to fulfil their responsibilities. The following section discusses the audit committee as part of the internal instruments of corporate governance which assists the board in performing their duties.

Audit Committee

Amongst the types of board committees, the audit committees are set up to assist the oversight function of the board of directors in order to increase financial disclosure. Indeed, financial disclosure becomes important related to the phenomena of corporate collapse (Clarke, Dean and Oliver, 2003; Australia, 2002). In Asia, following the Asian crisis, the effectiveness of the audit committee was being questioned; thus, there is a great concern of the effectiveness of audit committees (Allen, 2000). In fact, the phenomena of corporate collapse around the world have led to legislation or regulation reforms in both the accounting field and the stock exchange (Clarke et al., 2003; Australia 2002; Allen, 2000). In the 20th century, following the biggest American corporate scandal of Enron and WorldCom, the Sarbanes-Oxley Act has become the *magna carta* of corporate disclosure and internal control, especially in relation to the duties of an audit committee issue (Findlaw, 2005; EIRIS, 2005).

Recommendations were suggested by the Blue Ribbon Committee (BRC) in order to improve the effectiveness of a corporate audit committee (BRC, 1999, pp. 10-15). It recommends three important points that should be strengthened: independence, effectiveness and accountability. To increase the audit committee's independence, BRC defines the meaning and the circumstances so that independence can be assured. Then, to increase the audit committee's effectiveness, important points are related to financial literacy, which involves needs for a formal written charter and its review and assessment, and the disclosure of a formal written charter adoption in the company's proxy statement. For accountability, BRC recommends some mechanisms of relationship amongst the audit committee, the outside auditors and the management. Regarding the mechanisms between the audit committee and the external auditor, BRC suggests that two things which influence the objectivity and the independence of the auditor must be specified. These are the ultimate accountability of the outside auditor to both the board of directors and the audit committee, and the relationship between the auditor and the company. Then, to increase accountability, the letter from the audit committee must be disclosed. The letter requires the following information : a) a review activity of the management to the audited financial statements and b) a discussion between the external auditor and the audit committee about the auditor's judgement whether the preparation of financial statements follow general accepted accounting practice (accounting standards).

In addition to the recommendations, BRC also addresses "guiding principles for Audit Committee Best Practices" (BRC, 1999, pp. 37-44). The guiding principles relate to the issue of the independence, diligence and knowledge of the audit committee member. Indeed, these principles can improve the key role of the audit committee in the context of a 'three-legged-stool' relationship; the relationship among board of directors (including the audit committee), financial management (including the internal auditors), and external auditors.

DeZoort, Hermanson, Archambeault and Reed (2002) consider four determinants of audit committee effectiveness (ACE), namely, composition, authority, resources and diligence. Regarding the composition of audit committee, members should be independent, financially literate, and have integrity and objectivity. Meanwhile, the characteristic of diligence is defined as the willingness of committee members working as a team in the context of a 'three-legged-stool' relationship. Then, related to the resource component, DeZoort et al. (2002) emphasis that three to six members are considered suitable. Finally, all criteria will be interdependent, as for example they will ensure fulfilment of the audit committee's authority or responsibilities.

Addressing the financial fraud scandals, DeZoort et al. (2002) also states that the function of audit committees needs to be improved in relation to their independence, composition, expertise, disclosure of activities, discussion of financial reporting quality and materiality assessment. Indeed, shown by literature, independence has a favourable impact on the audit function. Abbott et al. (2000) found that firms composed of independent directors in their audit committees and where the audit committees met at least twice a year, were less likely to be associated with and engage in both fraudulent and misleading reporting. Next, the study of Xie, Davidson III and DaDalt (2003) showed that there was a small possibility that earnings management occured when the audit committee consisted of more independent rather than outside directors. In addition, Mangena and Pike (2005) found that companies were more likely to disclose less interim information when the audit committee was less independent since, as suggested by Khrisnan (2005), an independent audit committee decreases the incidence of internal control problems.

Regarding other criteria for an effective audit committee, the literature shows that experience, knowledge and ability also add value to audit committee effectiveness. In particular, these criteria enhance the interim disclosure (Mangena and Pike, 2005). In addition to increase effectiveness, DeZoort and Salterio (2001) found that in the case of auditor-management disputes, the independent members of audit committee and the members' auditing knowledge were positively associated with support for the auditor. Therefore, financial disclosure became more reliable. In the case of aggressive accounting activities, the literature suggests that an audit committee having more expertise and knowledge in financial literacy is more effective in constraining the earnings management (Bedard et al., 2004; Xie et al., 2003).

Literature also shows that the appointment of directors with financial expertise to the audit committee is also significantly and positively rated by the market (DeFond, Hann and Hu, 2005; Davidson III, Xie and Xu, 2004). DeFond et al. (2005) emphasise that the reaction, measured by cumulative abnormal returns (CARs), is only positive when the appointed outside director is independent and when the appointing companies have relatively strong corporate governance records before the appointing process. Regarding financial expertise, Davidson et al. (2004) found that auditing experience was more important than corporate financial management and financial statement analysis experience.

Related to audit committee, Indonesian corporate governance code follows international best practice as follows: 1) size: committee consists of at least three persons; 2) independency: at least one of the members is an independent commissioner; 3) leadership structure: the chairperson is an independent commissioner; 4) competency: at least one of members holds financial or accounting qualifications.

For the study, this paper examined the compliance to audit committee attributes 3 and 4 above using dummy variables[4]. Therefore, given that the audit committee structure had some bearing on company performance, the hypotheses were:

H_4 : There is a positive relationship between proportions of independent commissioners in audit committee and company performance.

H_5 : A company, which its audit committee is led by an independent commissioner and at least one of the members has accounting/ financial literacy, has better performance than a company which does not have any these characteristics.

H_6 : There is a positive relationship between size of audit committee and company performance.

Leverage

In addition to board, leverage is another internal instrument of corporate governance that increases company performance (Bodie, Kane and Marcus, 2005). The debt composition reflected by leverage also increases the monitoring activities by outsiders. Nonetheless, mentioned by Sarkar and Sarkar (2008), debt has double-edge sword effects, that on one hand, it is a potential device to discipline management that having commitment to pay debt (both principal and interests) minimises the free cash flow problem. Hence, it mitigates conflict between agent and principal (Jensen, 1986). On the other hand, from the corporate finance point of view, while debt offers tax advantages, too much debt causes a company to face a bankruptcy risk. In addition to this, in the developing markets when common type of conflict is between minority and majority shareholders, rather than playing as an effective corporate governance instrument disciplining management, debt is misapplied by the majority shareholders to expropriate the minority shareholders (Sarkar and Sarkar, 2008; Bunkanwanicha, Gupta and Rokhim, 2003). Accordingly, literature of the disciplining role of leverage is mixed (Sarkar and Sarkar, 2008). Therefore, hypothesis that was tested in this study was stated generally as:

H_7 : There is a relationship between leverage and company performance.

Ownership

Literature suggests that majority of shareholders, blockholders and institutional ownership could play positive roles in disciplining managers. Ownership of institution which does not have business relationship with the company increases the monitoring activities (Cornett, Marcus, Saunders and Tehranian, 2003). Large institutional shareholders give better monitoring which then increases output and firm value (Huddart, 1993; Admati, Pfleiderer and Zechner, 1994). This type of ownership will give independent monitoring activities which then ensure management to perform in the best interest of the shareholders. Therefore, the hypotheses tested in this study was:

H_8 : There is a positive relationship between unrelated parties' ownership and company performance.

H_9 : There is a positive relationship between block outsider ownership and company performance.

Literature suggests that some aspects of management ownership will increase the management's sense of belonging to the company which motivates the managers to run the company optimally (Fahlenbrach and Stulz, 2007; Gillan and Starks, 2003; Morck, Shleifer and Vishny, 1988; Stulz, 1988). Therefore, the hypothesis tested in this study was:

H_{10}: There is a positive relationship between management ownership and company performance.

Regarding the ownership from parent entity or related parties, Pinkowitz, Stulz and Williamson (2003) found that when protection for investors was weak, this type of shareholders could abuse their power to suppress the rights of the minority shareholders and to transfer cash from the company for their own benefit through tunnelling. Related to this, the hypothesis tested was:

H_{11}: There is a negative relationship between related parties' ownership and company performance.

Control Variables

In addition to board governance as the independent variable, this study considered size of company as a controlling variable. The size of company can be measured by the value of assets (LnAssets) and sales (LnSales). It is assumed that the bigger the company size, the bigger capital resources are available (Demstez and Lehn, 1985). Hence, greater resources mean a greater opportunity for the company to have a strong company performance. Similarly, larger sales figure indicates a growth opportunity for the company to achieve higher company performance.

Compared to some studies which included variables of company profitability, such as, ROE or ROA as one of the explanatory variables, this study did not include these variables as control variables since this study focused on the relationship between corporate governance instruments and a company's market-based performance measurements, such as, Tobin's Q. In addition, similar to some studies, such as, Barnhart and Rosenstein (1998), Himmelberg, Hubbard and Palia (1999), and Bhagat and Sinjai (2008), this study considered ROA or ROE which is an accounting based performance that has a similar function as Tobin's Q (a company's market-based performance) as a dependent variable of the study; "they are alternative measures of performance".

Having discussed literature of internal instruments of corporate governance and the practice in Indonesian corporations, the model of the study is shown in Figure 1. Depicted in the figure are the unique business environments of Indonesia as a basis of corporate operates, known also as the external mechanisms of corporate governance. In the existing external governance mechanisms, Figure 1 presented how internal governance mechanisms influence company performance.

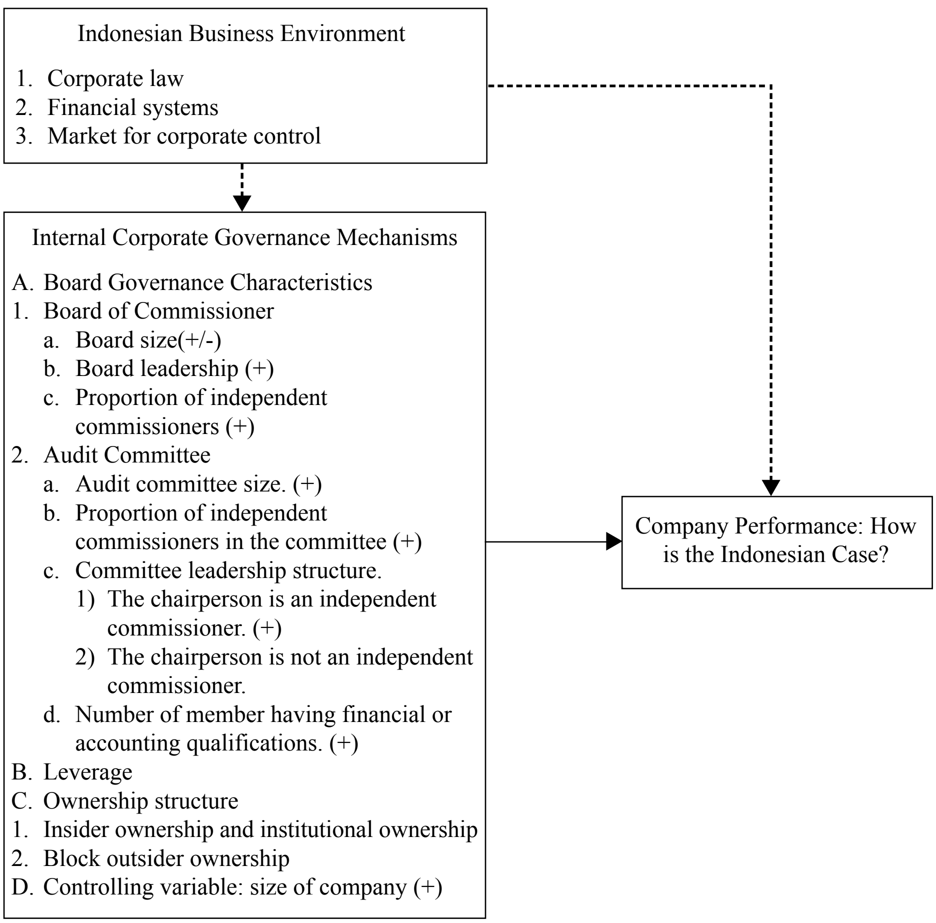

Figure 1: Corporate Governance and Company Performance: Evidence from Indonesia

Research Methodology

The data of this study was secondary and the sample was Indonesian listed companies. The period of the study was 2002-2004 and the starting period: 2002 was chosen since it was the effective period of the implementation of good corporate governance practice on the JSX listed companies (even though the practice has been introduced since 2000). The sample of the study was selected based on its availability on the JSX website; hence, only companies which were listed during 2002-2004 and published their annual reports on the JSX website were selected. This paper also excluded bank and financial companies due to two specific reasons. Firstly, there are other regulations imposed on these companies, i.e. regulations issued by the Indonesian central bank is specifically concerned with the prudential risk issues of banks. Secondly, these companies' performances are measured with specific financial indicators, i.e. net performing loan (NPL) and capital adequacy ratio (CAR). Finally, from 315 listed companies, only 46 companies were selected for this study. Therefore, within three years (2002-2004), 138 observations were examined.

Following former studies, such as, Darmawati et al. (2004), and Kiel and Nicholson (2003), this board governance effectiveness was examined using Tobin's Q. This Tobin's Q is the measure of a company's market-based performance. A high Tobin's Q with a value greater than 1, suggests a high market value for the company's asset and growth. The calculation of Tobin's Q is as follows (Bhagat and Black, 2002, adopted from Chung and Pruitt, 1994).

$$\text{Tobin's Q} = \frac{\text{Market Value of Asset}}{\text{Book Value of Asset}} = \frac{\text{MVCS} + \text{BVPS} + \text{BVLTD}}{\text{BVTA}}$$

where:

MVCS : Market value of common stock
BVPS : Book value of preferred stock
BVLTD: Book value of long term debt
BVTA : Book value of total asset

To investigate the relationship between corporate governance and a company performance, multiple regressions followed by a test of the endogenous problem (Durbin wu-husman test) were conducted. A statistical model for multiple regressions is as follows.

$$\text{Tobin's Q} = \alpha_0 + \alpha_1\,\text{BSize} + \alpha_2\,\text{BLdr} + \alpha_3\,\text{BIdp} + \alpha_4\,\text{ACIdp} + \alpha_5\,\text{ACothers} + \alpha_6\,\text{ACSize} + \alpha_7\,\text{Big} + \alpha_8\,\text{Lev} + \alpha_9\,\text{Mgt} + \alpha_{10}\,\text{InsNot} + \alpha_{11}\,\text{InsRltd} + \alpha_{12}\,\text{Block} + e_i$$

where:

Tobin's Q : Company performance
BSize : Board of commissioners' size (Ln)
BLdr : Board of commissioners is led by an independent commissioner
BIdp : Composition of independent commissioners in board of commissioners

ACIdp	: Composition of independent commissioners in audit committee
ACothers	: Other qualities of audit committee comply with Indonesian corporate governance regulation; the audit committee is led by an independent commissioner and consists of members having financial/accounting literacy
ACSize	: Size of audit committee (Ln)
Big	: Size of company (LnAsset)
Lev	: Leverage
Mgt	: Insider ownership
InsNot	: Institutional ownership, unrelated parties
InsRltd	: Institutional ownership, related parties
Block	: Outsider ownership (individual) with ownership more than 5%

Results of the Study

Tables 1 and 2 describe corporate governance practice in Indonesia. Firstly, the mean of Tobin's Q increased from 0.465 to 0.831 within the three years. Similarly, the minimum of Tobin's Q value increased to 0.143 from just 0.031 in 2002. The increasing trend of Tobin's Q suggests better economic conditions in Indonesia. This is also supported by a decreasing trend in the leverage of Indonesian companies. The statistics show that the mean value of leverage decreased from 0.981 in 2002 to 0.273 at the end of 2004 while the maximum leverage also decreased dramatically to 3.163 from 27.208 in 2002.

Turning to the concentration of ownership, individual outsider ownership and insider ownership had changed over the three years. Over these periods, the ownership of Indonesian companies was concentrated in institutions that had no business relationship with the company. The percentage of ownership of this type of institution remained at the level of 30% on average, while the ownership of institution that had business relationship with the company remained at 0.3% over the last two years. Similarly, the ownership of manager or commissioners in the company stayed at level 0.2% over three periods. The descriptive statistics also portray board governance of the listed companies. The figure shows how varied the board of commissioners of companies in JSX. Firstly, over three periods of observations, while there was a company that had only four members on the board of commissioners, there was also a company that had 13 commissioners on its board. Nonetheless, the average member of a board remained constant at four members between 2002 and 2003. The second variable showing high variation in the governance of the JSX listed companies was the composition of independent commissioners. There was another company that still did not have an independent commissioner in its board, while there was another company in which its board consisted of 60% of independent commissioners. Nonetheless, the composition of independent commissioners on average was not more than 40% and not less than 30%, just meeting the minimum requirement of the composition of independent commissioners of 30%.

The descriptive statistics also show that the audit committee size was three members on average. In contrast, with the figure of board of commissioners, there was no significant gap in audit committee size as the minimum/maximum number of committee members

Table 1: Descriptive Statistics

Observation	2002	2003	2004	Observation	2002	2003	2004
Mean Q	0.465	0.651	0.831	Mean MGT	0.022	0.024	0.023
Med Q	0.336	0.579	0.642	Med MGT	0	0	0
Sd Q	0.528	0.534	0.721	Sd MGT	0.06	0.064	0.064
Min Q	0.031	0.115	0.143	Min MGT	0	0	0
Max Q	3.467	3.369	3.892	Max MGT	0.288	0.288	0.288
Mean AGE	7.777	8.777	9.777	Mean BSIZE	1.458	1.443	1.48
Med AGE	8	9	10	Med BSIZE	1.386	1.498	1.386
Sd AGE	4.2	4.2	4.2	Sd BSIZE	0.427	0.454	0.475
Min AGE	0.417	1.417	2.417	Min BSIZE	0.693	0.693	0.693
Max AGE	18.833	19.833	20.833	Max BSIZE	2.398	2.639	2.639
Mean LEV	0.981	1.225	0.273	Mean BIDP	0.337	0.367	0.367
Med LEV	0.253	0.313	0.268	Med BIDP	0.333	0.333	0.333
Sd LEV	3.981	5.437	1.601	Sd BIDP	0.12	0.118	0.127
Min LEV	-0.004	-0.716	-9.451	Min BIDP	0	0	0
Max LEV	27.208	37.112	3.163	Max BIDP	0.6	0.6	0.667
Mean INSNOT	0.34	0.307	0.305	Mean ACSIZE	1.116	1.146	1.14
Med INSNOT	0.25	0.2	0.239	Med ACSIZE	1.099	1.099	1.099
Sd INSNOT	0.306	0.294	0.287	Sd ACSIZE	0.086	0.129	0.124
Min INSNOT	0	0	0	Min ACSIZE	1.099	1.099	1.099
Max INSNOT	0.975	0.923	0.874	Max ACSIZE	1.609	1.609	1.609
Mean BLOCK	0.005	0.294	0.285	Mean ACIDP	0.332	0.316	0.322
Med BLOCK	0	0.238	0.208	Med ACIDP	0.333	0.333	0.333
Sd BLOCK	0.02	0.302	0.3	Sd ACIDP	0.108	0.079	0.088
Min BLOCK	0	0	0	Min ACIDP	0	0	0
Max BLOCK	0.105	0.931	0.931	Max ACIDP	0.75	0.5	0.6
Mean INSRLTD	0.302	0.003	0.003	Mean BIG	27.469	27.448	27.492
Med INSRLTD	0.25	0	0	Med BIG	27.642	27.742	27.938
Sd INSRLTD	0.305	0.017	0.017	SdBIG	1.45	1.492	1.789
Min INSRLTD	0	0	0	Min BIG	24.43	24.282	22.623
Max INSRLTD	0.931	0.105	0.105	Max BIG	30.896	30.942	31.298

Notes:

Q	: Tobin's Q
AGE	: Listing period of a company in the JSX
LEV	: Leverage
INSNOT	: Ownership (%) of institution which has no relationship with the company
BLOCK	: Ownership (%) of individual outside of the company
INSRLTD	: Ownership (%) of institution which has relationship with the company (such as parent or subsidiary company)
MGT	: Ownership (%) of individual inside of the company
ACSIZE	: Size of audit committee
ACIDP	: Number of independent commissioners in audit committee
BIG	: Size of company in terms of assets

Table 2: Descriptive Statistics

	Q	AGE	LEV	INSNOT	BLOCK	INSRLTD	MGT	BSIZE	BIDP	ACSIZE	ACIDP	BIG
Mean	0.649	8.777	0.826	0.317	0.195	0.103	0.023	1.46	0.357	1.134	0.323	27.47
Median	0.5	8.792	0.269	0.232	0	0	1.05E-05	1.386	0.333	1.098612	0.333	27.776
Maximum	3.892	20.833	37.112	0.975	0.931	0.931	0.288	2.639	0.667	1.609	0.75	31.298
Minimum	0.031	0.417	-9.451	0	0	0	0	0.693147	0	1.098612	0	22.623
Standard Deviation	0.615	4.249	3.99	0.294	0.279	0.225	0.062	0.45	0.121	0.114	0.092	1.573
Skewness	3.139	0.121	7.5	0.445	1.032	2.038	3.354	0.224	-0.531	3.228	-0.557	-0.287
Kurtosis	15.271	2.682	64.664	1.863	2.523	5.783	13.242	2.596	4.428	12.348	12.515	3.368
Jarque-Bera	1092.503	0.917	23158.07	11.992	25.806	140.048	861.812	2.088	18.213	742.169	527.676	2.671
Probability	0	0.632	0	0.00249	0.000002	0	0	0.352113	0.000111	0	0	0.263
Sum	89.57	1211.25	114.032	43.775	26.848	14.215	3.144	201.548	49.281	156.464	44.6	3790.834
Sum Sq. Dev.	51.874	2473.585	2181.153	11.82	10.636	6.96	0.528	27.687	2.022	1.796	1.156	338.918

Notes:

Q : Tobin's Q
AGE : Listing period of a company in the JSX
LEV : Leverage
INSNOT : Ownership (%) of institution which has no relationship with the company
BLOCK : Ownership (%) of individual outside of the company
INSRLTD : Ownership (%) of institution which has relationship with the company (such as parent or subsidiary company)
MGT : Ownership (%) of individual inside of the company
ACSIZE : Size of audit committee
ACIDP : Number of independent commissioners in audit committee
BIG : Size of company in terms of assets

is three. Included in the audit committee was one independent commissioner, reflected by the mean of variable ACIDP (an independent commissioner who is also an audit committee member) which was 33%.

Overall, the figures related to board governance of the Indonesian companies shows that most of the companies complied with the best practice. However, this condition indicates that only the minimal conditions for corporate governance have been implemented by companies. The composition of independent commissioners of 30%, and the number of members in the audit committee of three just hit the minimum requirement of the JSX regulation. In fact, there are still companies that did not have any independent commissioners despite the requirement of corporate governance regulations being in place since 2002. Berle and Means (1933) suggest that this type of commissioner (director) increases the effectiveness of monitoring and the strategic planning role of the board.

The R-square in Table 3 of the model indicates that 97.65% of variance in company performance can be explained by the model. Furthermore, with the acceptance of a significant level of 5%, the F-statistic suggests the overall model is significant (P-value < 5%). Turning to the significance of each independent variable, the t-statistic suggests that most of the independent variables are significant in explaining Tobin's Q except three variables. The insignificant variables are size of board of commissioners, size of audit committee and management ownership. All other internal corporate governance variables: board independence, board leadership, audit committee independence, qualification of audit committee, size of a company, ownership of institutions, ownership of related companies and block ownership, have significant association with company performance.

Table 3 shows that the variable of board independence (BIDP) is positive and a significant predictor of company performance (Tobin's Q). It means that hypothesis 1 was accepted that the total number of independent commissioners related positively to company performance. However, the paper did not find evidence to support the theory suggesting that board size is an important factor that contributes to improved performance. Table 3 shows that the variable of board size (BSIZE) was not significant (p > 5%). Therefore, this study could not find evidence for hypothesis 2.

Hypothesis 3 was supported since the variable of board leadership (BLDR) as shown in Table 3 indicates that the performance of companies in which the board was not led by an independent commissioner was different from a company that had an independent commissioner as a chairperson of the board. The performance of companies in which the board commissioners was not led by an independent commissioner was lesser by 0.16 compared with a company which the board was led by the independent one.

Turning to the characteristics of the audit committee, this study found the composition of audit committee members who were also independent commissioners relates positively to company performance, hence hypothesis 4 was accepted. The results of variables of other characteristics of audit committee (ACOTHERS), following best practice: led by an independent commissioner and having a minimum of three members on an audit committee including at least one member with an accounting/financial background,

Table 3: Generalised Least Square Method (Remedy for Heteroskedasticity Problem)

Dependent variable: TOBINSQ
Method: Least squares
Date: 07/22/06 Time: 02:58
Sample: 1 138
Included observations: 126
Excluded observations: 12
Weighting series: LEV^(-.5)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1.426404	0.951686	1.498818	0.1367
BSIZE	-0.068077	0.115046	-0.591742	0.5552
BIDP	0.958418	0.263106	3.642708	0.0004
BLDR	-0.163166	0.04369	-3.73462	0.0003
ACIDP	1.260287	0.320988	3.926277	0.0001
ACOTHERS	0.330242	0.122759	2.690173	0.0082
ACSIZE	0.639819	0.410395	1.559033	0.1218
BIG	-0.090437	0.041623	-2.172758	0.0319
LEV	0.303423	0.126294	2.40252	0.0179
MGT	0.040959	0.800379	0.051175	0.9593
INSNOT	0.31079	0.119768	2.594938	0.0107
INSRLTD	0.236209	0.105006	2.249494	0.0264
BLOCK	0.333681	0.117333	2.843877	0.0053

Weighted statistics

R-squared	0.976459	Mean dependent var	0.356156
Adjusted R-squared	0.973959	S.D. dependent var	0.990096
S.E. of regression	0.159774	Akaike info criterion	-0.73266
Sum squared residual	2.884627	Schwarz criterion	-0.440028
Log likelihood	59.15758	F-statistic	125.0036
Durbin-Watson statistic	1.633067	Prob (F-statistic)	0

Unweighted statistics

R-squared	-3.655747	Mean dependent var	0.661812
Adjusted R-squared	-4.150163	S.D. dependent var	0.630943
S.E. of regression	1.43186	Sum squared resid	231.6753
Durbin-Watson statistic	0.604882		

Note: The proportionality factor from leverage is chosen because as the 'behaviour' of company performance changes as the leverage changes.

suggests that the performance of a company complying with best practice is significantly different from the company without these attributes in its audit committee.

Hypothesis 5: A company, which its audit committee was led by an independent commissioner and at least one of the members has accounting/ financial literacy, had better performance than a company which did not have any these characteristics. Hypothesis

5 was rejected since, anomalously, the performance of companies not following the best practice was greater by 0.33 compared with a complying company. This study found that the variable of audit committee size was insignificant, hence this study could not find evidence to support hypothesis 6: There is a positive relationship between size of audit committee and company performance.

This study did not find a relationship between management ownership (MGT) and company performance (hypothesis 10). However, the findings show that outsider ownership (both institutional, related and unrelated parties- and individual ownership) and leverage associated positively with performance measured by Tobin's Q, Therefore hypotheses 7, 8, and 9 were supported. Finally, Table 3 shows that there was a positive relationship between related parties' ownership and company's performance, hence hypothesis 11 was rejected.

Discussions: Implications for Indonesian Corporate Governance Practices

The descriptive study suggest that there was an increasing awareness of companies to have good board governance. Nevertheless, there were still a few companies which still did not have independent commissioners nor audit committee. In addition, a member of the audit committee could be in charge of more than one company (Kompas, 2004). This condition, hence, increases a conflict of interest in the audit committee that could decrease the performance of audit committee.

In spite of this increasing awareness, the results of this study confirmed the study of CGFRC (2004) that companies were still minimal in implementing the good corporate governance practices especially those related to board governance. JSX (2003) and CGFRC (2004) showed that there were still companies which did not implement the JSX corporate governance practice. This study, as shown in the descriptive investigation, found late responses of the JSX listed companies to comply with the JSX corporate governance practice that is compulsory for every listed company, despite the weakness of the legal system in Indonesia. Since the code for corporate governance practice is compulsory for listed companies, regulators have an important role in imposing the regulation so that market confidence increases.

Turning to the role of the internal corporate governance mechanisms of a company impacting performance, the results of this paper support an argument that board independence is an important attribute that can improve company performance. Leadership and the number of independent commissioners are significant positive predictors of company performance. These findings support the theory of Berle and Means (1933) suggesting an independent commissioner increases the effectiveness of monitoring and strategic planning role of the board that it leads to better company performance. Regarding the role of board size, this study could not find evidence to support the theory suggesting that board size is one of the factors which contributes to an effective board. Therefore, similar to previous studies (Beiner et al., 2004; Kula, 2005; Adams and Mehran, 2005), this study failed to detect the relationship between board size and company performance. This result further explains that the size of the board might not be important because dominant shareholders appoint the board of directors.

In contrast to BRC (1999) and DeZoort et al. (2002), the study found that the performance of companies which did not have an audit committee was higher than the performance of the complying companies. This suggests that, in Indonesia, an audit committee is not as important as in other countries. This result is consistent with the insignificant result on size of audit committee which suggests that the role of some special aspects of board practices in developed countries on firm performance does not exist in Indonesia. Similar to the insignificant board size, the insignificant result on size of audit committee imply that in an emerging country like Indonesia, where the capital market is still not developed and the external corporate governance mechanisms are weak, the market participants consider independent boards to be more important than size of the board or the strength of the audit committee. Since external governance mechanisms are less effective, independency of the board, which is reflected by the composition of independent of commissioners and leadership structure is preferred by the Indonesian capital market.

Finally, the positive effect of leverage shows a contrast result to the literature which suggests that in an emerging market, leverage is usually used as an expropriated tool of the majority shareholders to suppress the minority (Sarkar and Sarkar, 2008; Bunkanwanicha et al., 2003). The findings of this study were, therefore, different from other studies. In this study, leverage had a positive effect on the company's value while the other studies found that leverage was utilised as an expropriation tool by majority shareholders which then had negative effects on company's performance. This result suggests while many emerging economies face debt-financing problem due to high debt levels in their financial structure, the level of debt financing in Indonesia during 2002-2004 was still low, hence, leverage had a positive effect; market appreciates it by increasing its market value. In addition to this, since management ownership shows no effect to company performance compared to outsider ownership, the study suggests that in Indonesian case, institutional and block-outsider ownerships are more effective in mitigating the conflict between shareholders and between agent and principals thereby increasing company value.

Conclusions

Initially, the study presented literature of corporate governance and its practice in Indonesian companies. In the context of the unique business environment of Indonesia as an emerging market, the study tested its main proposition: whether the standard relationships between internal corporate governance instruments and company performance exist in Indonesia. The results on the descriptive study found that there was an increasing awareness of companies to have good board governance by complying to the JSX's corporate governance practice. The study also found that independence was the main attribute of board governance (including audit committee), which increased the company performance. The insignificant results on size of board governance, the lower Tobin's Q on audit committee having characteristics 'good audit committee' and following best corporate governance practice, and insignificant of management ownership show that the role of some special aspects of internal corporate governance practices in developed countries on firm performance did not exist in Indonesia. These can be explained by the Indonesian business characteristics, namely, developing capital market where the external corporate governance mechanisms are less effective. Overall, the findings offer a considerable insight for the understanding of the relationships between internal corporate governance mechanisms and company performance in an emerging market, such as, Indonesia.

Notes

1 In 2007, Surabaya Stock Exchange was merged into Jakarta Stock Exchange. As a result, JSX changed its name to the Indonesia Stock Exchange (IDX). Rather than using IDX, this study uses JSX term since the sample of this study was selected for the period before 2007.

2 See code of corporate governance of National Committee for Corporate Governance (NCCG) and Decision Letter of Director of Jakarta Stock Exchange No.: Kep-315/BEJ/06-2000 which later amended by Decision Letter of Director of Jakarta Stock Exchange No.: Kep-339/BEJ/07-2001.

3 Indonesia follows a two-tier board governance system of the corporate governance model where the function of Board of Commissioners is similar to Board of Directors in a one-tier system.

4 Dummy variable = 0: Committee led by an independent member and consists of at least one of members having accounting/ financial characteristics.

References

Abdullah, S. N. (2004). Board Composition, CEO Duality and Performance among Malaysian Listed Companies, *Corporate Governance: International Journal of Business in Society*, 4, 4: 47-61.

Abbott, L. J., Park, Y. and Parker, S. (2000). The Effects of Audit Committee Activity and Independence on Corporate Fraud, *Managerial Finance*, 26, 11: 55-68.

Adams, R. B. and Mehran, H. (2005). Corporate Performance, Board Structure and its Determinants in the Banking Industry, *EFA Moscow Meetings*.

Admati, A. R., Pfleiderer, P. and Zechner, J. (1994). Large Shareholder Activism, Risk Sharing, and Financial Market Equilibrium, *The Journal of Political Economy*, 102, 6: 1097-130.

Allen, J. (2000). Code Convergence in Asia: Smoke or Fire?, *Corporate Governance International*, 3, 1.

ASX 2007, *Corporate Governance Principles and Recommendations*, Australian Stock Exchange.

ASX 2010, *ASX Listing Rules*, Australian Stock Exchange.

Australia, Co 2002, *CLERP Paper No. 9: Proposals for Reform - Corporate Disclosure*, The Commonwealth Copyright Administration, Canberra, ACT, available at http://www.treasury.gov.au/contentitem.asp?NavId=013&ContentID=403.

Barnhart, S. W. and Rosenstein, S. (1998). Board Composition, Managerial Ownership, and Firm Performance: An Empirical Analysis, *The Financial Review*, 33, 4: 1-16.

Barton, D., Felton, R. F. and Song, R. (2000). Building Asian Boards, *McKinsey Quarterly, Special Edition*, 4: 64-74.

Bedard, J., Chtourou, S. M. and Courteau, L. (2004). The Effect of Audit Committee Expertise, Independence, and Activity on Aggressive Earnings Management, *Auditing: A Journal of Practice and Theory*, 23, 2: 13-37.

Beiner, S., Drobetz, W., Schmid, F. and Zimmermann, H. (2004). Is Board Size an Independent Corporate Governance Mechanism?, *Kyklos*, 57, 3: 327-356.

Berle, A. A. and Means, G. C. (1933), The Modern Corporation and Private Property [Electronic Resource], Macmillan Co., New York.

Bhagat, S. and Black, B. (2002).The Non-Correlation Between Board Independence and Long-Term Firm Performance, *Journal of Corporation Law*, 27, 2: 231-247.

Bhagat, S. and Bolton, B. (2008). Corporate Governance and Firm Performance, *Journal of Corporate Finance*, 14, 3: 257-273.

Black, B. S., Jang, H. and Kim, W. (2006). Does Corporate Governance Affect Firm Value?, *Journal of Law, Economics, and Organization*, 22, 2.

Blue Ribbon Committee (BRC) (1999). *Report and Recommendations of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees*, The New York Stock Exchange and The National Association of Securities Dealers.

Bodie, Z., Kane, A. and Marcus, A.J. (2005). Investments, 6^{th} edn, McGrawHill, pp. 660-663.

Brown, L. D. and Caylor, M. L. (2005). Corporate Governance and Firm Operating Performance, available at SSRN: http://ssrn.com/abstract=586423.

Bunkanwanicha, P., Gupta, J. and Rokhim, R. (2003), Debt and Entrenchment: Evidence from Thailand and Indonesia, *SSRN eLibrary*, Available at SSRN: http://ssrn.com/abstract=478302.

Bushman, R. M. and Smith, A. J. (2001). Financial Accounting Information and Corporate Governance, *Journal of Accounting and Economics*, 32, 1-3: 237-333.

Capulong, M. A., Edwards, D., Webb, D. and Zhuang, J. (2000). Corporate Governance and Finance in East Asia: A Study of Indonesia, Republicly of Korea, Malaysia, Philippines, and Thailand, Vol. 1 (Consolidated Report), Asia Development Bank (ADB).

CGFRC (2004). Corporate Governance Disclosures in Indonesia: A Study of LQ 45 Companies, CGFRC of NUS Business School and Standard & Poor's Joint Study, available at http://www.cgfrc.nus.edu.sg/events_news/CGFRC_Indon_study.htm.

Chung, K. H. and Pruitt, S. W. (1994). A Simple Approximation of Tobin's q, *FM: The Journal of the Financial Management Association*, 23, 3: 70-74.

Clarke, F., Dean, G. and Oliver, K. (2003). Corporate Collapse: Accounting, Regulatory, and Ethical Failure, Rev. Edn, Cambridge University Press, Melbourne, Australia.

Claessens, S. and Fan, J. P. H. (2002). Corporate Governance in Asia: A Survey, *International Review of Finance*, 3, 2, 71-103.

Cornett, M.M., Marcus, A.J., Saunders, A. and Tehranian, H. (2003). The Impact of Institutional Ownership on Corporate Operating Performance, NYU Stern Finance Working Paper No. 03-033, available at SSRN: http://ssrn.com/abstract=468800.

Dalton, D. R., Daily, C. M., Ellstrand, A. E. and Johnson, J. L. (1998). Meta-Analytic Reviews of Board Composition, Leadership Structure and Financial Performance, *Strategic Management Journal*, 19, 3: 269.

Darmawati, D., Khomsiyah and Rahayu, R. G. (2004). The Relationship between Corporate Governance and Company's Performance, Available at The Indonesian Institute for Corporate Governance: http://www.iicg.org/wacana.htm

Davidson III, W. N., Xie, B. and Xu, W. (2004). Market Reaction to Voluntary Announcements of Audit Committee Appointments: the Effect of Financial Expertise, *Journal of Accounting and Public Policy*, 23: 279-293.

DeAndreas, P., Azofra, V. and Lopez, F. (2005). Corporate Boards in OECD Countries: Size, Composition, Functioning and Effectiveness, *Corporate Governance: An International Review*, 13, 2: 197-210.

DeFond, M.L., Hann, R. N. and Hu, X. (2005). Does the Market Value Financial Expertise on Audit Committee of Boards of Directors?, *Journal of Accounting Research*, 43, 2: 153-193.

Demsetz, H. and Lehn, K. (1985). The Structure of Corporate Ownership: Causes and Consequences, *The Journal of Political Economy*, 93, 6: 1155-1177.

Demsetz, H. and Villalonga, B. (2001). Ownership Structure and Corporate Performance, *Journal of Corporate Finance*, 7, 3: 209-33.

DeZoort, F. T. and Salterio, S. E. (2001). The Effects of Corporate Governance Experience and Financial-Reporting and Audit Knowledge on Audit Committee Members' Judgments , *Auditing: A Journal of Practice and Theory*, 20, 2: 31-49.

DeZoort, F. T., Hermanson, D. R, Archambeault, D. S. and Reed, S. A. (2002). Audit Committee Effectiveness: A Synthesis of the Empirical Audit Committee Literature, *Journal of Accounting Literature*, 21, 38-75.

EIRIS (2005). *How Global Is Good Corporate Governance?*, available at http://www.ecgi.org/codes/all_codes.php#US, accessed at 3 December 2005.

Fahlenbrach, R. and Stulz, R.M. (2007). Managerial Ownership Dynamics and Firm Value, *National Bureau of Economic Research Working Paper Series*, No. 13202.

Fahlenbrach, Rüdiger and Stulz, René M. (2009). Managerial Ownership Dynamics and Firm Value, *Journal of Financial Economics*, Elsevier, 92, 3: 342-361, June.

Farinha, J. (2003). Corporate Governance: A Survey of the Literature, Universidade do Porto Economia Discussion Paper No. 2003-06. Available at SSRN: http://ssrn.com/abstract=470801 or doi:10.2139/ssrn.470801.

Farrar, J. (2005). Corporate Governance: Theories, Principles, and Practice, 2nd edn, Oxford University Press, New York.

Findlaw (2005). *One Hundred Seventh Congress of The United States of America at The Second Session,* H.R. 3763, available at http://news.findlaw.com/hdocs/docs/gwbush/sarbanesoxley072302.pdf, accessed at 3 December 2005.

Gillan, S.L. and Starks, L.T. (2003). Corporate Governance, Corporate Ownership, and the Role of Institutional Investors: A Global Perspective, Weinberg Center for Corporate Governance Working Paper No. 2003-01, available at SSRN: http://ssrn.com/abstract=439500 or DOI: 10.2139/ssrn.439500.

Gompers, P. A., Ishii, J. L. and Metrick, A. (2003). Corporate Governance and Equity Prices, Quarterly Journal of Economics, 118, 1: 107-155.

Hermalin, B. E., and Weisbach, M. S. (2003). Boards of Directors as an Endogenously Determined Institution: A Survey of the Economic Literature, *FRBNY Economic, Policy Review*, 9, 1: 7-27.

Himmelberg, C.P., Hubbard, R.G. and Palia, D. (1999). Understanding the Determinants of Managerial Ownership and the Link between Ownership and Performance. *Journal of Financial Economics*, 53, 3: 353-84.

Hung, H. (1998). A Typology of the Theories of the Roles of Governing Boards, *Corporate Governance: An International Review*, 6, 2: 101-111.

Huddart, S. (1993). The Effect of a Large Shareholder on Corporate Value, *Management Science*, 39, 11: 1407-1421.

International Monetary Fund (IMF) (1997). Indonesia – Memorandum of Economic and Financial Policies: Indonesia Letter of Intent, available at http://www.imf.org/external/np/loi/103197.htm - 76k - HTML

Iskander, M. R. and Chamlou, N. (2000). *Corporate Governance: A Framework for Implementation,* World Bank, Washington, D.C.

Jaafar, A. and El Shawa, M. (2009). Ownership Concentration, Board Characteristics and Performance: Evidence from Jordan, SSRN, available at SSRN: http://ssrn.com/abstract=1392727

JSX (2000), *The Decree of JSX's Director No.: Kep-315/BEJ/06/2000,* Jakarta Stock Exchange (JSX), available at http://www.jsx.co.id, accessed 21 March 2005.

JSX (2003), *JSX Announcement Related to Independent Commissioners and Audit Committee of the Listed Companies No. Peng. 199/BEJ-PEM/01-2003*, Jakarta Stock Exchange (JSX), available at http://www.jsx.co.id, accessed 21 March 2005.

Jensen, M. C. (1986). Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers, *American Economic Review*, 76, 2: 323.

Jensen, M. C. and Meckling, W. H. (1976). Theory of the Firm: Managerial Behavior, Agency Cost and Ownership Structure, *Journal of Financial Economics*, 3, 4: 305-360.

Johnson, S., Boone, P., Breach, A. and Friedman, E. (2000). Corporate Governance in the Asian Financial Crisis, *Journal of Financial Economics*, 58, (1-2): 141-186.

Kiel, G. C. and Nicholson, G. J. (2003). Board Composition and Corporate Performance: How the Australian Experience Informs Contrasting Theories of Corporate Governance, *Corporate Governance: An International Review*, 11, 3: 189-205.

Klapper, L. F. and Love, I. (2004). Corporate Governance, Investor Protection, and Performance In Emerging Markets, *Journal of Corporate Finance*, 10, 5: 703-28.

Kompas (2004). Bapepam Mengkaji Kembali Aturan Komited Audit (Re-assessment of Audit Committee Regulation by Bapepam-Indonesia Capital Market Supervisory Agency), available at http://www.kompas.com/kompas-cetak/0401/17/finansial/807336.htm, accessed 20 June 2006.

Krishnan, J. (2005). Audit Committee Quality and Internal Control: An Empirical Analysis, *Accounting Review*, 80, 2: 649-676.

Kula, V. (2005). The Impact of the Roles, Structure and Process of Boards on Firm Performance: Evidence from Turkey, *Corporate Governance: An International Review*, 13, 2: 265-276.

Lawrence, J. J. and Stapledon G. P. (1999). Is Board Composition Important? A Study of Listed Australian Companies, available at SSRN: http://ssrn.com/abstract=193528 or DOI: 10.2139/ssrn.193528.

Mangena, M. and Pike, R. (2005). The Effect of Audit Committee Shareholding, Financial Expertise and Size on Interim Financial Disclosures, *Accounting and Business Research*, 35, 4: 327-349.

McKinsey (2002). Global Investor Opinion Survey: Key Findings, available at www.mckinsey.com/governance, accessed 7 September 2005.

Morck, R., Shleifer, A. and Vishny, R.W. (1988). Management Ownership and Market Valuation: An Empirical Analysis, *Journal of Financial Economics*, 20: 293-315.

NCCG (2001). *Indonesian Code for Corporate Governance,* National Committee on Corporate Governance (NCCG), available at www.ecgi.org/codes/documents/indon_2001.pdf, accessed 7 April 2005.

Nasdaq (2006). *Equity Rules*, Nasdaq Stock Market.

Nasdaq (2010). *Regulatory Requirements*, Nasdaq Stock Market.

NYSE (2008). *NYSE Regulation*, New York Stock Exchange.

OECD (2004). *OECD Principles of Corporate Governance - 2004 Edition [electronic resource],* available at http://www.oecd.org/dataoecd/32/18/31557724.pdf

Pinkowitz, L., Stulz, R. M. and Williamson, R. (2003). Do Firms in Countries with Poor Protection of Investor Rights Hold More Cash?, *National Bureau of Economic Research Working Paper Series*, Vol. No. 10188.

Sarkar, J. and Sarkar, S. (2008). Debt and Corporate Governance in Emerging Economies: Evidence from India, *Economics of Transition*, 16, 2: 293-334.

Stulz, R. (1988). Managerial Control of Voting Rights: Financing Policies and the Market for Corporate Control, *Journal of Financial Economics*, 20: 25-54.

Suntraruk, P. (2009). Board of Directors, Ownership, and Firm's Performance: A Study of Set100 Firms in Thailand, SSRN, available at SSRN: http://ssrn.com/abstract=1409488

Van den Berghe, L. A. A. and Levrau, A. (2004). Evaluating Boards of Directors: What Constitutes a Good Corporate Board?, *Corporate Governance*, 12, 4: 461-478.

World Bank (2004). *Report on the Observance of Standards and Codes (ROSC), Corporate Governance Country Assessment: Republic of Indonesia*, available at http://www.worldbank.org/ifa/rosc_cg_idn.pdf, accessed 1 February 2005.

Xie, B., Davidson III, W.N. and DaDalt, P.J. (2003). Earnings Management and Corporate Governance: The Roles of the Board and the Audit Committee, *Journal of Corporate Finance*, 9, 3: 295-316.

Young, M. N., Peng, M. W., Ahlstrom, D., Bruton, G. D. and Jiang, Y. (2008). Corporate Governance in Emerging Economies: A Review of the Principal Perspective, *Journal of Management Studies*, 45, 1: 196-220.