JRAK
Jurnal Riset Akuntansi Kontemporer

THE EFFECT OF CORPORATE GOVERNANCE ON FINANCIAL DISTRESS

https://journal.unpas.ac.id/index.php/jrak/index

Fitri Humairoh[1]✉, Suci Nurulita[2]
[1,2]Department of Accounting, Faculty of Economics and Business, Universitas Riau
✉[1]fitri.humairoh@lecturer.unri.ac.idd
Kampus Bina Widya KM. 12,5, Simpang Baru, Kec. Tampan, Pekanbaru, Riau, Indonesia

Article Info

History of Article
Received: 8/9/2022
Revised: 26/9/2022
Published: 24/10/2022

Jurnal Riset Akuntansi Kontemporer
Volume 14, No. 2, October 2022, Page 237-242
ISSN 2088-5091 (Print)
ISSN 2597-6826 (Online)

Keywords: board of director; audit committee; managerial ownership; institutional ownership; independent commissioner, financial distress

Abstract
This research aims at examining the effect of the board of directors, audit committee, managerial ownership, and institutional ownership on financial distress in manufacturing companies listed on the Indonesia Stock Exchange for the 2015-2020 period. The population in this research are manufacturing companies listed on the Indonesia iStock iExchange for the i2015-2020 period. The sampling technique in this research used a purposive sampling technique and obtained a sample of i13 companies with a total of 78 data observations. The data analysis method used is multiple regression analysis. The results of this research indicated that institutional ownership affected financial distress, while the board of directors, audit committee, managerial ownership, and independent commissioner did not affect financial distress.

INTRODUCTION

Financial distress in Indonesia is an issue that has become the centre of attention of many people, especially in the case of the COVID-19 pandemic in Indonesia. This COVID-19 pandemic has had an impact on many companies, as reported by the Central Statistics Agency data, during the pandemic 2.55% of companies were able to operate normally, 14.60% of companies did not experience a decrease in performance or increase, and even as many as 82, 45% of companies experienced a decline in revenue (Ayuni et al, 2020).

According Harlan & Marjorie (2006), financial distress is defined as the stage of decline in financial conditions that occurred before bankruptcy or liquidation. Financial distress can start from short-term liquidity issues to a bankruptcy declaration, which was the most severe form of financial distress. The financial distress model should be built because, by identifying the company's financial distress at an early stage, actions can be taken to anticipate situations that may result in bankruptcy. (Spica & Herdinigtyas, 2005).

Bankruptcy is an issue that businesses must be aware of. Typically, bankruptcy is defined as an organization's inability to manage its operations profitably. (Walisongo & Walisongo, 2011). A bankrupt firm indicated that it is facing a business failure; thus, some businesses that are experiencing financial difficulties try to solve the problem by making loans or combining their operations. Other businesses, on the other hand, choose different strategies, such as shutting down or ceasing operations.

A company must continue to improve and maintain its performance to become a healthy company and avoid financial problems (financial distress) or even bankruptcy. However, in reality, many large companies in Indonesia have gone bankrupt or bankrupt. For example, PT. Mrs Mener, who had been established since 1919, was declared bankrupt by the Semarang District Court on August 3, 2017 because she had debts of up to Rp.7.4 billion. Then PT. The Royal Standard (RS) Group, which oversees the jaya envelope, was declared bankrupt by the Central Jakarta Commercial Court on March 6, 2017 for having debts worth Rp.333 billion (Sandi, 2018).

Allowing financial problems to persist would lead to bankruptcy. A large number of people are affected by this financial issue. not only the corporation, but also the company's stakeholders and stockholders.This was the background of several research developments on the financial distress model, to be able to predict the company's financial distress early and then take action to anticipate conditions that led to bankruptcy (Piatt & Piatt, 2002).

In this research, the writers used good corporate governance as the factor to determine the financial distress in a company. According to International Finance Corporation (IFC), (2014), the governance structure of a limited liability company consisted of 8, the general meeting of shareholders, the board of commissioners, the board of directors, board of committee, external auditor, the internal auditor, the corporate secretary, and the ownership structure that consisted of managerial ownership and institutional ownership. In this research, the researcher used of the board of directors, of the audit committee, managerial ownership, institutional ownership, and independent commissioner as the indicators from corporate governance.

This research predicted that board of directors, audit committee, managerial ownership institutional ownership, and independent commissioners had an effect on financial distress. The effect prediction referred to the results of Widhiadnyana (2020) research which showed that audit committee, managerial ownership, and institutional ownership had an effect on financial distress. Also, this research referred to the result of Kusanti (2019) research which showed that board of directors and independent commissioners had an effect on financial distress.

Based on the background described above, the formulation of the problem are does the board of directors, audit committee, managerial ownership, institutional ownership, and independent commissioners have an effect on financial distress in manufacturing companies listed on the Indonesia Stock Exchange 2015-2020.

METHOD

The population in this research were manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the 2015-2020 periods. The reason for choosing manufacturing companies as the sample was because manufacturing companies consisted of various industrial sub-sectors. The sampling technique in this research used purposive sampling with the following criteria:

Table. 1 Population and Sample

Description	Amount
Manufacturing companies that listed on the Indonesia Stock Exchange from 2015-2020	136
Manufacturing companies that did not publish annual report and financial statements in a row from 2015-2020	(33)
Manufacturing companies that used foreign currency in financial statements	(26)
Manufacturing companies that were not in red are (distress zone) for at least two years in the 2015-2020 research periods	(63)
Total Company	13
Number of years	5
Total of observations	78

Financial Distress is the dependent variable in this research and is measured using the Altman Z-score. Altman Z-Score used a linear equation formed from several variables included in the ratio scale (Armadani et al., 2021). According to Kazemian et al., (2017). Z-score is a fairly accurate method for predicting financial distress compared to other methods (Springrate, Zmijewski, Foster, and Gover) and is very useful for managers, investors, and stakeholders in the future.

Altman Z-score is formulated as follows:

$$Z = 6,56X_1 + 3,26X_2 + 6,72X_3 + 1,05X_4$$

Where X_1 represented ratio of working capital to total assets, and X_2 stood for ratio of retained earnings to total assets, and X_3 stood for ratio of earnings before interest and taxes (EBIT) to total assets, X_4 stood for book value of equity to book value of total liability, while Z represents overall index.

Table 2. Measurement of Independent Variables

Variable	Definition	Indicator	Scale
Board of Directors (X_1)	The board of directors is a company organ that is tasked and responsible for managing finances and determining strategies or policies that will be taken in the short and long term (Emrinaldi, 2007)	The board of directors is measured by counting the number of members of the board of directors in the company in period t (Triwahyuningtias, 2012).	Nominal
Audit Committee (X_2)	Audit committee is the total number of audit committee members in one company. (Emrinaldi, 2007)	The variable size of the audit committee in this research was measured by the number of members of the audit committee in a company can be known from the company's annual report (Emrinaldi, 2007).	Nominal
Manajerial Ownership (X_3)	Managerial ownership is the amount of share ownership by management and company directors (Khafid, 2012).	This variable is obtained by dividing the number of shares owned by management by the total shares issued by the company (Triwahyuningtias, 2012).	Ratio
Institutional Ownership (X_4)	Institutional ownership is the percentage of shares owned by institutions of the total outstanding shares of the company (Triwahyuningtias, 2012).	In this research, institutional ownership is measured by the percentage of institutional ownership in the company under observation (Emrinaldi, 2007).	Ratio
Independent Commissioner (X_5)	Independent Commissioners are commissioners who have no relationship with the company and are trusted to provide good supervision. (Yosua & Ary, 2019)	In this research, the independent commissioner variable is obtained through the number of independent commissioners in period t / total commissioners in period t	Ratio

RESULTS

The results of descriptive statistical tests for the variables of financial distress, board of directors, audit committee, managerial ownership, institutional ownership and independent commissioners can be seen in Table 2.

Table 3 showed the amount of data (observations) studied as many as 78 data. The Board of Directors, Audit Committee and Institutional Ownership had an average value (mean) that was greater than the standard deviation. This indicated that the research data are grouped or not varied. While the variables financial distress, managerial ownership, and independent commissioners had an average value (mean) which was smaller than the standard deviation. This showed that the research data are not grouped or varied.

Table 3. Descriptive Statistic of Variables

	N	Minimum	Maximum	Mean	Std. Deviation
FD	78	-15.15	1.20	-.7128	2.81725
BoD	78	2.00	7.00	4.5584	1.21929
AC	78	3.00	5.00	4.8077	1.43299
MO	78	0.01	77.79	7.7150	21.20834
IO	78	3.17	93.71	46.1513	26.89222
IC	78	.20	.70	.4058	.13043
Valid N (listwise)	78				

The next step was examining the effect of each independent variable on the dependent variable. A summary of the results using multiple regression analysis is presented in Table 4.

Table 4. Multiple Linear Regression Analysis

	Unstan. Beta	Stan. Error	Stan. Coef. Beta	t	Sig.	Adj. R^2
Constant	-6.917	1.686		-4.103	.000	.520
BoD	.347	.223	.150	1.555	.124	
AC	.560	.297	.284	1.890	.063	
MO	-.001	.012	-.005	-.051	.959	
IO	.045	.015	.424	2.943	.004	
IC	-.344	1.974	-.016	-.174	.862	

Referring to Table 4 above presented, it can be concluded that the multiple linear regression equations produced in this research are:

$$Y = (-6.917) + 0.124\ X_1 + 0.063\ X_2 + 0.959\ X_3 + 0.004\ X_4 + 0.862\ X_5 + e$$

From the tabel, it showed that the value of a (Constant) is -6.917, it meant that when all independent variable, X_1, X_2, X_3, X_4, X_5 are zero or constant, then Y or financial distress would decrease with amount 6.917. Regression coefficient value for X_1 is 0.124, meant that each increasing of X_1 by 1 unit will increase the possibility of financial distress by 0.124. Regression coefficient value for X_2 is 0.063, meant that each increasing of X_2 by 1 unit would increase the possibility of financial distress by 0.063. Regression coefficient value for X_3 is 0.959, meant that each increasing of X_3 by 1 unit would increase the possibility of financial distress by 0.959. Regression coefficient value for X_4 is 0.004, meant that each increasing of X_4 by 1 unit would increase the possibility of financial distress by 0.004. Regression coefficient value for X_5 is 0.862, meant that each increased of X_3 by 1 unit would increase the possibility of financial distress by 0.862

The result showed that one out of five independent variables, institutional ownership, positively affected financial distress. The other variables, board of director, audit committee, managerial ownership, and independent commissioners, did not affect financial distress. The result also reveal that the squared multiple correlation (R^2) for the accountability is 0.52. Thus, it can be concluded that changes that occurred in Financial Distress are explained by board of directors, audit committee, managerial ownership, institutional ownership, and independent commissioner as independent variables of 52% while the remaining 48% is influenced by other independent factors not observed in this this research.

DISCUSSION

The findings showed that Board of Directors had no effect on financial distress. Law Number 40 of 2007 concerning Limited Liability Companies in article 92 paragraph (4) stated that the General Meeting of Shareholders (GMS) decided how the tasks and management authority would be distributed among the members of the board of directors, preserving the board of directors' restricted jurisdiction. Although the board of directors was aware of the state of the firm, decisions are still made at the general meeting of shareholders (GMS). This was why the number of boards of directors in a firm had little bearing on the likelihood that it would affect financial distress. (Merkusiwati, 2014).

This result was not in line with research conducted by Putri & Aminah (2019), Oktaviani (2019), and Kusanti (2015) stated that Board of Directors has effect on financial distress.The reason underlying the results of the research was that of the audit committee is less able to support the effectiveness of the performance of the audit committee. This statement is supported by research by Dalton (1999) which shows that audit committees with large numbers of members tend to lose focus and participate less actively in resolving agency problems. It became increasingly difficult for the audit committee's members to achieve agreement on decisions when carrying out their responsibilities at times. On the other hand, the audit committee is considered ineffective since it has a small number of members and a lack of diverse expertise in handling agency conflicts.

The result of this research supported the research conducted by Kusanti (2015) and Nuresa & Hadiprajitno (2013) stated that audit committee has no effect on financial distress in a company. Meanwhile this research has different result with research conducted by Masak & Noviyanti (2019) and Widhiadnyana (2020) stated that audit committee has negative effect on financial distress.

The rejection of hypothesis three (H3) might occur because managerial ownership was too low so that it has little impact on the company's worth since the manager's performance in managing the business is mediocre and also because, as a minority shareholder, they hasn't been allowed to actively engaged in company decision-making. When compared to pure managers as professionals who are paid by the company, the sense of belonging that managers feel over the company as shareholders does not sufficient to affect performance (Christiawan & Tarigan, 2007).

The result of this research supported the research conducted by Idarti (2018), Kusanti (2015), and Fathonah (2016) stated that managerial ownership had no effect on financial distress in a company. Meanwhile this research had different result with research conducted by Santoso & Nugrahanti (2022), Khairat (2019) and Widhiadnyana (2020) stated that managerial ownership had effected on financial distress.

The positive relationship between institutional ownership and the financial distress can be explained because if the company is owned by institutional investors, then the company's management is considered unable to hide the losses or failures that are being experienced, thus triggering financial distress (Aritonang, 2017).

The result of this research supported the research conducted by Emrinaldi (2007), Khairat (2019), and Widhiadnyana (2020) stated that institutional ownership can affect the financial distress in a company. Meanwhile this research had different result with research conducted by (Setiyawan (2020), Oktaviani (2019), and Kusanti (2015) stated that institutional ownership had no effect on financial distress.

The greater the proportion of independent commissioners in the company, the greater the occurrence of financial distress, which meant that there are several factors that cause the performance of independent commissioners to violate their proper work, such as no accounting background that can cause the influence of supervision in financial statements, Independent commissioners also serve as other positions in other public companies so that their work is not focused and participates in accompanying the company Yosua & Ary (2019).

This results is in line with research conducted by Merkusiwati (2014) and Ananto (2017) stated that independent commissioner had no effect on financial distress. Meanwhile this research had different results with research conducted by Fathonah (2016) stated that independent commissioner has effect on financial distress.

CONCLUSION

The results obtained from 13 manufacturing companies listed on the Indonesia Stock Exchange for the 2015-2020 period with 78 annual reports indicate that the board of directors, audit committee, managerial ownership and independent commissioners had no effect on financial distress. On the other hand, institutional ownership had an effect on financial distress. The implications of this research can be useful for companies as a reference to prevent financial distress and can be a source of reading for other researchers who wanted to research or learn about financial distress. However, this research had several limitations, Further research should be able to use more variables than the ones that already used in this research. The variables used in this research. The variables used in this research are limited such as board of director, audit committee, managerial ownership, and institutional ownership. This research used a limited observation period, which is for 6 years (2015- 2020); and This research only used manufacturing company listed on IDX from 2015-2020. Accordingly, the plan for Further research should be able to add other variables that are considered influential and provide a broader picture of financial distress, should be able to increase the number of samples from other companies and to extend the research period.

REFERENCES

Aritonang, A. P. 2017. *Pengaruh Praktik* Corporate Governance *dan Struktur Kepemilikan Terhadap Kemungkinan Kondisi Financial Distress Perusahaan*. Media Riset Akuntansi, 3(2), pp. 105–124.

Armadani, A., Fisabil, A. I. and Salsabila, D. T. 2021. *Analisis Rasio Kebangkrutan Perusahaan pada Masa Pandemi Covid-19*. Jurnal Akuntansi, 13, pp. 99–108. doi: 10.28932/jam.v13i1.3197.

Bps.go.id. 2020. *Katalog: 3101028. Analisis Hasil Survei Dampak COVID-19 terhadap Pelaku usaha, p. vi+ 22 halaman.* Available at: https://www.bps.go.id/publication/2020/09/15/9efe2fbda7d674c09ffd0978/analisis-hasil-survei-dampak-covid-19-terhadap-pelaku-usaha.html.

Dalton, D. 1999. Number of Directors and Financial Performance: A meta-analysis. Academy of Management Journal, 42(6), pp. 674–686. doi: 10.2307/256988.

Emrinaldi, N. D. 2007. *Analisis Pengaruh Praktek Tata Kelola Perusahaan (*Corporate Governance*) Terhadap Kesulitan Keuangan Perusahaan (*Financial Distress*): Suatu Kajian Empiris*. Jurnal Bisnis dan Akuntansi, pp. 88–108.

Erik Setiyawan, M. 2020. *Pengaruh Struktur Kepemilikan, Profitabilitas, Likuiditas, Leverage Dan Nilai Tukar Terhadap Financial Distress Pada Perusahaan Yang Terdaftar Di Idx Tahun 2016-2017.*

Fathonah, A. N. 2016. *Pengaruh Penerapan* Good Corporate Governance *Terhadap* Financial Distress.

Febri Masak, S. N. 2019. *Pengaruh Karakteristik Komite Audit terhadap* Financial Distress*.*

Harlan D, P. and Marjorie B, P. 2006. Understanding Differences Between Financial Distress and Bankruptcy. Review of Applied Economics, 2(2), pp. 1–17.

Idarti, A. H. 2018. *Analisis Pengaruh Struktur Kepemilikan, Kebijakan Hutang Dan Likuiditas Terhadap Financial Distress (Studi Empiris Pada Perusahaan Properti Dan Real Estate Yang Terdaftar Di Bursa Efek Indonesia Periode 2013 –2017).*

International Finance Corporation. 2014. The Indonesia Corporate Governance Manual - First Edition. Otoritas Jasa Keuangan, 1(7), pp. 1–533. Available at: http://www.ojk.go.id/Files/box/THE-INDONESIA-CORPORATE-GOVERNANCE-MANUAL-First-Edition.pdf#search=governance.

Kazemian, S. 2017. Monitoring Mechanisms and Financial Distress of Public Listed Companies in Malaysia. Journal of International Studies, 10(1), pp. 92–109. doi: 10.14254/2071-8330.2017/10-1/6.

Khafid, M. 2012. *Pengaruh Tata Kelola Perusahaan* (Corporate Governance) *dan Struktur Kepemilikan Terhadap Persistensi Laba*. Jurnal Dinamika Akuntansi, 4(2), pp. 139–148. doi: 10.15294/jda.v4i2.2172.

Khairat, F. 2019. *Pengaruh Kepemilikan Manajerial, Kepemilikan Institusional, Dewan Direksi, Likuiditas, dan Leverage Terhadap Financial Distress (Studi Empiris Perusahaan Manufaktur Yang Terdaftar di Bursa Efek Indonesia Periode 2016-2018)*.

Kusanti, O. (no date) Andayani Sekolah Tinggi Ilmu Ekonomi Indonesia (STIESIA) Surabaya. Available at: http://www.idx.co.id/idid/beranda/perusahaan.

Merkusiwati, N. W. K. A. P. dan N. K. L. A. 2014. *Pengaruh Mekanisme* Corporate Governance*, Likuiditas, Leverage, dan Ukuran Perusahaan pada* Financial Distress.

Nuresa, A. and Hadiprajitno, B. 2013. *Pengaruh Efektivitas Komite Audit Terhadap* Financial Distress. Diponegoro Journal Of Accounting, 2(2), pp. 1–10. Available at: http://ejournal-s1.undip.ac.id/index.php/accounting.

Oktaviani, C. A. 2019. *Pengaruh* Corporate Governance*, Likuiditas dan* Operating Capacity *Terhadap* Financial Distress*.*

Pamungkas, Y. 2019. *Pengaruh Mekanisme* Corporate Governance *Terhadap* Financial Distress.

Piatt, H. D. and Piatt, M. B. 2002. Predicting Corporate Financial Distress: Reflections On Choice-Based Sample Bias. Journal of Economics and Finance, 26(2), pp. 184–199. doi: 10.1007/bf02755985.

Putra Ananto, R., Mustika, R. and Handayani, D. 2017. Di Bursa Efek Indonesia.

Putri, G. W. and Aminah, W. 2019. *Faktor-Faktor Yang Memitigasi* Financial Distress *Pada Perusahaan Pertambangan*. Jurnal Riset Akuntansi Kontemporer, 11(1), pp. 1–8. doi: 10.23969/jrak.v11i1.1547.

Sandi, E. P. 2018. *Tak Hanya Sariwangi, 3 Perusahaan Legendaris Indonesia Ini Juga Pailit Artikel ini telah tayang di* Tribun-Bali.com dengan judul Tak Hanya Sariwangi, 3 Perusahaan Legendaris Indonesia Ini Juga Pailit, https://bali.tribunnews.com/2018/10/18/tak-hanya-sariwa.

Santoso, L. and Nugrahanti, Y. W. 2022. The Effect of Ownership Structure on Financial Distress: Evidence in Indonesian Manufacturing Companies. Jurnal Riset Akuntansi Kontemporer, 14(1), pp. 55–64. doi: 10.23969/jrak.v14i1.5178.

Spica, L. and Herdinigtyas, W. 2005. *Analisis Rasio Camel Terhadap Prediksi Kondisi Bermasalah Pada Lembaga Perbankan Perioda 2000-2002*. Jurnal Akuntansi dan Keuangan, 7(2), pp. 131-147–147. doi: 10.9744/jak.7.2.pp.131-147.

Triwahyuningtias, H. M. and M. 2012. *Analisis Pengaruh Struktur Kepemilikan, Ukuran Dewan, Komisaris Independen, Likuiditas Dan Leverage terhadap Terjadinya Kondisi Finacial Distress (Studi pada 109 Perusahaan Manufaktur yang Terdaftar Di Bursa Efek Indonesia Tahun 2008-2010)*.

Triwahyuningtias, M. 2012. *Analisis Pengaruh Struktur Kepemilikan, Ukuran Dewan, Komisaris Independen, Likuiditas, Dan Laverage Terhadap Terjadinya* Financial Distress. Semarang , universitas diponogoro, pp. 1–81.

Walisongo, S. and Walisongo, W. 2011. *Analisis Pengaruh* Financing to Deposit Rasio (FDR). 19(1), pp. 47–74.

Widhiadnyana, I. K. 2020. The Effect of Ownership Structure on Financial Distress with Audit Committee as Moderating Variable. International Research Journal of Management, IT and Social sciences. doi: 10.21744/irjmis.v7n1.830.

Yulius Jogi Christiawan and Josua Tarigan. 2007. *Kepemilikan Manajerial: Kebijakan Hutang, Kinerja Dan Nilai Perusahaan.* Jurnal Akuntansi dan Keuangan, 9(1), pp. 1–8. Available at: http://puslit2.petra.ac.id/ejournal/index.php/aku/article/view/16810.