FINANCIAL DISTRESS: THE IMPACT OF INSTITUTIONAL OWNERSHIP, INDEPENDENT COMMISSIONERS, MANAGERIAL OWNERSHIP, AND AUDIT COMMITTE

Angela Dirman

Universitas Mercu Buana, Jakarta, Indonesia

IJMSSSR 2020
VOLUME 2
ISSUE 4 JULY – AUGUST **ISSN: 2582 - 0265**

Abstract: The research objective to be achieved is to provide understanding and knowledge to the public, especially investors and creditors regarding the influence of institutional ownership, independent commissioners, managerial ownership, and audit committees on financial distress and can be used as a reference for further researchers and stakeholders (investors, creditors and government) in making relevant and reliable decisions.

The method used is quantitative research with secondary data taken from the issuer's financial statements on IDX with data collection techniques using the purposive sampling method. Analysis of the data used is multiple linear regression. The population in this research is manufacturing companies of basic and chemical industry sectors which are listed on the Indonesia Stock Exchange which is conducted for 3 years of observation, namely 2016-2018. Samples were determined by purposive sampling method so as many as 66 samples were obtained. The analysis technique used is the statistical test t, and the classic assumption test which includes normality test, multicollinearity test, heterokedasticity test, and autocorrelation test.

The results of this study indicate that the audit committee variable has a positive effect on financial distress, while the variables of institutional ownership, independent commissioners, and managerial ownership have no effect on financial distress.

Keywords: Institutional Ownership, Independent Commissioners, Managerial Ownership, Audit Committee, Financial Distress

INTRODUCTION

The global economic crisis is an event in which all sectors of the world market economy experience a collapse (degression) and affect other sectors throughout the world. The global economic crisis occurs because of the problems of market economies around the world that cannot be avoided because of bankruptcy and the turbulent economic situation. Sectors most affected by the global crisis are those that rely on external demand (tradable), such as manufacturing, agriculture and mining (kompas.com). In addition to the global financial crisis, the start of free trade between ASEAN countries also affected the company's performance. The more freedom of foreign companies entering Indonesia has caused competition among companies to increase. Companies that cannot survive facing the situation indicate that the company has experienced failure which is indicated by financial distress.

Financial distress becomes an interesting topic in the financial sector and financial health companies as an important indicator for users who are interested in knowing more about company performance (Pernamasari, Purwaningsih, Tanjung, & Rahayu, 2019). When a company experiences financial difficulties, it will be a consideration for investors and creditors who will invest their capital. Thus, companies should be able to show good company performance to be able to attract investors (Widhiari & Aryani Merkusiwati, 2015).

The failure of various companies around the world in achieving the expected goals, or even to be able to survive in the business world, is always associated with international capital markets, users of financial statements, and the accounting profession with weaknesses in the corporate governance structure adopted by the company(Elloumi & Gueyié, 2001).The company must implement good corporate governance in its management, with good governance the company will be less likely to experience financial distress.

According to Rebecca & Siregar (2012) the application of corporate governance means it is considered capable of increasing oversight of management to encourage effective decision making, preventing opportunistic actions that are not in line with company interests, and reducing information asymmetry between management, shareholders and creditors. The elements used in corporate governance in this study are institutional ownership, independent commissioners, managerial ownership, and audit committees.

Institutional ownership is part of the ownership structure in the company. Institutional ownership is the proportion of ordinary shares owned by institutional parties (Helena & Saifi, 2017). Institutional ownership from outside the company acts as an external supervisor who oversees the performance of management (Paramastri & Hadiprajitno, 2017). With institutional ownership can increase the efficiency of the use of company assets, with institutional ownership, it is expected that there will be oversight of management decisions. Thus, the application of good corporate governance can prevent the company from financial distress.

An independent commissioner is a corporate governance mechanism that can reduce problems in agency problems. Because with the existence of an independent commissioner can avoid the asymmetry of information between the two parties which can lead to the possibility of financial difficulties. Generally companies with a greater proportion of independent directors will have better corporate governance (Hanifah & Purwanto, 2013).
Ownership structure is one of the factors that can affect the company's condition in the future. Managerial ownership can reduce agency problems that arise in a company. Managerial ownership is the proportion of company ownership by management (directors or commissioners). The greater the proportion of ownership by management, the greater the responsibility of management in managing the company. Decisions that are born from management are expected to be decisions in the interests of the company. Thus the company can avoid the potential for financial distress.

The audit committee is a corporate governance mechanism that is assumed to be able to reduce agency problems that arise in a company (Hanifah & Purwanto, 2013). The number of audit committees that must be more than one person is intended so that the audit committee can hold meetings and exchange opinions with each other. This is because each member of the audit committee has different corporate governance experience and financial knowledge.

LITERATURE REVIEW

Agency Theory

Agency theory is a theory used to explain the relationship between agents and principals that are built so that company goals can be achieved to the maximum. Jensen & Meckling(1976) define agency relationships as contracts between one or more people (principals) by hiring other people (agents) to perform a number of services on their behalf that involve the transfer of authority over decision making to agents.

Asymmetric information occurs because of differences in preferences between owners and agents. Each individual is motivated by his own interests so that it can cause conflicts between principals and agents. Principals have an interest in increasing the prosperity of their companies by entering into contracts with agents, while agents tend to be opportunistic, ie trying to meet their economic and psychological needs.

The issue of corporate governance is motivated by agency theory which states that agency problems arise when the management of a company is separate from its ownership. The board of commissioners and Directors who act as agents in the company are given the authority to take care of the running of a company and make decisions on behalf of the owner. With this authority, it is possible that managers do not act in the best interests of the owner because of differences in interests (conflict of interest). To reduce the level of agency problems that arise in a company is to implement good corporate governance(Triwahyuningtias & Muharam, 2012).

Effect of Institutional Ownership on financial distress

Institutional ownership is one of the mechanisms of corporate governance that can reduce problems in agency theory between owners and managers so that the alignment of interests between company owners and managers arises. The greater the institutional ownership, the more efficient the use of company assets, so that the potential

for financial distress can be minimized. According to research conducted by Septiani & Dana(2019), the results show that institutional ownership negatively influences financial distress.

The following hypotheses are proposed:

H1: Institutional ownership has a negative effect on Financial Distress.

Effect of Proportion of Independent Commissioners on Financial Distress

The Independent Board of Commissioners is seen from the proportion of independent commissioners compared to members of the company's board of commissioners. Independent here means that the party is not involved with management duties that function to run the company. Independent commissioners do not take sides with any party and be objective in every situation. The independence of the board of commissioners can increase investor confidence in the financial statements issued by the company so that it can suppress the company's financial distress in the following year (Ignasia Natania Astria Gunawijaya, 2015). The higher independence of the board of commissioners shows a better monitoring process so that it will reduce the condition of financial distress on the performance of one year afterwards because the results of the financial statements will be assessed by investors and effective in the following year.

The following hypotheses are proposed:

H2: Independent commissioners negatively affect financial distress

Effect of Managerial Ownership on financial distress

The existence of managerial ownership in the company can be one of the efforts in reducing agency problems with managers and aligning interests between managers and shareholders. In addition, managerial ownership makes supervision of the practice of corporate financial fraud declining because in the company itself there are company owners so that it involves direct supervision by the owner (Nur & Yuyetta, 2019). With the supervision of the company will reduce the occurrence of financial distress. According to research conducted by Nur & Yuyetta (2019) found that managerial ownership has a negative effect on financial distress.

The following hypotheses are proposed:

H3: Managerial ownership has a negative effect on financial distress

The influence of the Audit Committee on financial distress

In Indonesia, guidelines for the formation of an effective audit committee explain that the audit committee members owned by the company consist of at least three people who are chaired by an independent commissioner of the company with two external people who are independent of the company and occupy and have an accounting and financial background (KNKG, 2002) . The higher or more audit committee in a company indicates that the audit results will be better because more opinions emerge from the audit committee after performing the supervisory function so that the company tends to avoid financial distress in the following year because the results of the financial statements for the audit committee will have an impact on management performance next year. In Ignasia Natania Astria Gunawijaya(2015)found that companies that have a high number of audit committees have the possibility of not experiencing financial distress.

The following hypotheses are proposed:

H4: The Audit Committee has a negative effect on financial distress

RESEARCH METHOD

Definition and Operationalization of Variables

Dependent variable

Altman forms 3 Z score formulas in which the three formulas are for 3 different categories of companies, namely for publicly traded companies, closed companies, and for non-manufacturing public companies. This study uses the altmanzscore model for public manufacturing companies as in the research Pernamasari et al (2019). Where shares or shares of a company are traded openly or listed on a stock exchange. The formula used is as follows:

Z = 1,2 (X1) + 1,4 (X2) + 3,3 (X3) + 0,6 (X4) + 1,0 (X5)
Information:
Z = Bankruptcy Indeks
X1 = Working Capital/Total Assets
X2 = Retained Earnings/Total Assets
X3 = Earning Before Interest and Taxes/Total Assets
X4 = Market Value of Equity/Book Value of Debt
X5 = Sales/Total Assets

Independent Variable

Institutional Ownership

Institutional ownership is ownership of shares by investors in the form of non-bank financial institutions / institutions that manage funds on behalf of others. In this study institutional ownership is measured by the number of institutional shares in relation to the number of shares outstanding. Institutional ownership can be formulated as follows D & Suartana(2014):

$$\text{Institutional ownership} = \frac{\text{Total of institutional share}}{\text{total of outstanding share}}$$

Independent Commissioner

An independent commissioner is a member of a board of commissioners who does not have a relationship that can affect his ability to act independently (Hanifah & Purwanto, 2013). The independent commissioner variable is measured by proportion. The proportion of independent commissioners is calculated by:

$$\text{Proportion of independent commissioners} = \frac{\text{Total of independent commissioners}}{\text{total of commissiners}}$$

Managerial Ownership

Managerial ownership is the percentage of shares owned by management that actively participates in corporate decision making which includes ownership by directors (Fitdini,2009 in Nur & Yuyetta, 2019). The existence of managerial ownership in the company can be one of the efforts in reducing agency problems with managers and aligning interests between managers and shareholders. In this study managerial ownership is measured by the percentage of shares owned by the company's management of the total number of shares outstanding. The formula for calculating the percentage of managerial ownership based on Sartono's (2010) research in D & Suartana (2014) is as follows:

$$\text{Managerial ownership} = \frac{\text{Total of managerial share}}{\text{total of outstanding share}}$$

Audit Committee

The definition of the number of audit committees is how many committee members are in a company. Based on Bapepam Chairman's Decree No. KEP-29 / PM / 2004 states that the Audit Committee in Indonesian public companies consists of at least three members and is chaired by an independent company commissioner with two independent external people, originating from outside the Issuer or Public Company. The number of Audit Committees will be measured by how many committee members in a company.

Population and Research Samples

The population of this study is companies listed on the Indonesia Stock Exchange. The sample used in this study is industrial and chemical manufacturing companies listed on the Indonesia Stock Exchange in 2016-2018. The sampling method used was purposive sampling so as many as 66 samples were obtained. Sampling is based on company criteria that provide information about financial data in the study year, has institutional ownership, has an independent commissioner, has managerial ownership, and has an audit committee.

Audit Committess = Total of Audit

Analysis Method

In testing the hypothesis proposed in this study. The researcher uses the method of multiple linear regression analysis because of the relationship between two or more independent variables where previously the classical assumptions were made in the first stage.

Classical Assumption Test

This analysis can also be referred to as a prerequisite test of the multiple linear regression model to be tested. A good regression model must produce the best unbiased linear estimator (Best Linear Unbias Estimator / BLUE). This condition will occur if it is fulfilled by several assumptions called classical assumptions including normality test, multicollinearity test, heteroscedasticity test, autocorrelation test.

The regression model in this study is stated as follows:

$$Z\text{-score} = \alpha + \beta 1KI + \beta 2KOMIND + \beta 3KM + \beta 4KA + e$$

Results and Discussion

Results

a. Classical Assumption Test

Normality test

Kolmogorov-Smirnov One Sample Results

One-Sample Kolmogorov-Smirnov Test

		Unstandardized Residual
N		66
Normal Parameters[a,b]	Mean	0E-7
	Std. Deviation	2,17154985
Most Extreme Differences	Absolute	,099
	Positive	,099
	Negative	-,092
Kolmogorov-Smirnov Z		,802
Asymp. Sig. (2-tailed)		,541

a. Test distribution is Normal.
b. Calculated from data.

The above table shows that the Kolmogorov-Smirnov value is 0.802 and the Asymp value. Sig. (2-tailed) of 0.541. Because the Asymp value. Sig is greater than the significance level of 0.05 (0.541> 0.05), it can be concluded that the residual data in this regression model is normally distributed.

Multicollinearity Test, Heteroskedaticity Test, Autocorrelation Test

There is no multicolliniarity among the independent variables. Then there is no multicolliniarity between the independent variables.Based on the scaterplott chart the points spread randomly showing that there was no heteroscedasticity.From the auticorrelation test can be concluded that the regression model used is free from the problem of autokoleration.

Hypothesis testing

Determination Coefficient Test

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	,418[a]	,175	,121	2,2416178	2,486

a. Predictors: (Constant), Komite Audit, Kepemilikan Manajerial, Komisaris Independen, Kepemilikan Institusional
b. Dependent Variable: Financial Distress

In the table above shows that the coefficient of determination that shows the value of R-square of 0.175. This means that 17.5% of the variation in financial distress can be explained significantly by variations in institutional ownership, independent commissioners, managerial ownership, and audit committees. While (100% - 17.5%) = 82.5% the amount of financial distress can be explained by other variables.

F Test

ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	65,030	4	16,257	3,235	,018[b]
	Residual	306,516	61	5,025		
	Total	371,546	65			

a. Dependent Variable: Financial Distress
b. Predictors: (Constant), Komite Audit, Kepemilikan Manajerial, Komisaris Independen, Kepemilikan Institusional

Based on the data above, a significant value of 0.018 is obtained. Since the significance is less than 0.05 or 5%, then Ho is rejected and Ha is accepted, so it can be concluded together that institutional ownership, independent commissioner, managerial ownership, and audit committee influence on financial distress.

T Test

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-,694	2,918		-,238	,813		
	Kepemilikan Institusional	,011	,015	,120	,734	,466	,505	1,980
	Komisaris Independen	-7,995	4,352	-,220	-1,837	,071	,946	1,058
	Kepemilikan Manajerial	-,014	,024	-,093	-,575	,567	,521	1,918
	Komite Audit	2,066	,712	,349	2,900	,005	,932	1,073

a. Dependent Variable: Financial Distress

From the above test results it can be concluded as follows:

1. This shows that institutional ownership has no effect on financial distress.
2. Concluded that independent commissioners has no effect on financial distress.
3. Concluded that manajerial ownership has no effect on financial distress.
4. Concluded that audit committee has a positive effect on Financial Distress.

Multiple Regression Analysis Test Results

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-,694	2,918		-,238	,813		
	Kepemilikan Institusional	,011	,015	,120	,734	,466	,505	1,980
	Komisaris Independen	-7,995	4,352	-,220	-1,837	,071	,946	1,058
	Kepemilikan Manajerial	-,014	,024	-,093	-,575	,567	,521	1,918
	Komite Audit	2,066	,712	,349	2,900	,005	,932	1,073

a. Dependent Variable: Financial Distress

Based on the table of the results of multiple linear regression tests, the regression equation is obtained as follows:
Zscore = -694 + 0,11KI + (-7,995KOMIND) + (-0,014KM) + 2,066KA + e

Discussion

The Effect of Institutional Ownership on Financial Distress

The test results show institutional ownership has no effect on financial distress. That is, the higher the institutional ownership or the lower the institutional ownership, the financial distress as measured by the z-score will have no effect. Ownership of shares by large institutions is the majority and centralized owner, where majority ownership will result in reduced transparency in the use of company funds. The results of this study are in line with the results of a previous study by Putri & Merkusiwati (2014) which states that institutional ownership has no effect on financial distress.

The Influence of Independent Commissioners on Financial Distress

The results showed that the independent commissioner variable had no effect on financial distress. No matter how large the size of the independent board of commissioners, it cannot prove that the size of the independent board of commissioners has an impact on financial distress. The number of board of commissioners that are small, medium or large cannot cover the possibility of the company still experiencing financial condition in the press. The existence of independent directors in Indonesia has been regulated by the IDX through the JSX regulations dated July 1, 2000 which explained that companies listed on the Exchange must have an independent commissioner of at least 30% of all members of the board of commissioners. So that the number of independent commissioners in the company is limited to following the existing regulations, so there is no effect on financial distress. The results of this study support previous research by Putri &Merkusiwati (2014) and Cinantya & Merkusiwati (2015) that independent commissioners have no effect on financial distress.

Effect of Managerial Ownership on Financial Distress

The test results show managerial ownership has no effect on financial distress. In other words, the size of managerial ownership is not an appropriate predictor to measure the company's financial distress. High managerial ownership companies are not necessarily categorized as companies experiencing financial distress, nor are companies with lower managerial ownership not necessarily categorized as non-financial distress companies. These results are consistent with research conducted by Cinantya & Merkusiwati (2015) which resulted in managerial ownership research having no effect on financial distress.

Influence of the Audit Committee on Financial Distress

The test results show the audit committee has a positive effect on financial distress. The competence of the audit committee should enable the audit committee to control matters relating to company finances early on, so that the audit committee is able to make corrections to the company's financial condition to escape the company from financial distress, but the results of the study indicate that the greater the number of audit committees, the more likely to occur financial distress.

Conclusion

Based on the results of the analysis and discussion explained in the previous chapter, the conclusions of this study are as follows:

1. Institutional ownership does not affect Financial Distress.
2. Independent Commissioners have no influence on Financial Distress.
3. Managerial ownership does not affect Financial Distress.
4. The Audit Committee has a positive effect on Financial Distress.

Suggestions

In the research that has been done, there are still some limitations. Based on the results of the conclusions, as for suggestions that can be given, among others:

1. For further researchers, because the results of research on Institutional Ownership, Independent Commissioners, and Managerial Ownership indicate that the company has no influence on financial distress over the samples that have been conducted, it is advisable to retest because it is not in accordance with applicable theories. Further researchers can also increase the number of research samples or compare manufacturing companies with other sub-sectors such as the food and beverage sub-sector, or even compare one sector with several companies between countries.
2. For the Company, it is expected to pay attention to factors that can cause the company's financial distress, so that if there is an indication the company is experiencing financial distress, the company can quickly take action to improve the company's financial condition.

BIBLIOGRAPHY

1. Cinantya, I., & Merkusiwati, N. (2015). Pengaruh Corporate Governance, Financial Indicators, Dan Ukuran Perusahaan Pada Financial Distress. *E-Jurnal Akuntansi*, *10*(3), 897–915.
2. D, N. P. W. P., & Suartana, I. W. (2014). *PENGARUH KEPEMILIKAN MANAJERIAL DAN KEPEMILIKAN INSTITUSIONAL PADA NILAI PERUSAHAAN*. *3*, 575–590.
3. Elloumi, F., & Gueyié, J. P. (2001). Financial distress and corporate governance: An empirical analysis. *Corporate Governance: The International Journal of Business in Society*, *1*(1), 15–23. https://doi.org/10.1108/14720700110389548
4. Hanifah, O. E., & Purwanto, A. (2013). PENGARUH STRUKTUR CORPORATE GOVERNANCE DAN FINANCIAL INDICATORS TERHADAP KONDISI FINANCIAL DISTRESS (Studi Pada Perusahaan Manufaktur yang Terdaftar di Bursa. *Diponegoro Journal of Accounting*, *2*, 1–15.
5. Helena, S., & Saifi, M. (2017). Pengaruh Corporate Governance Terhadap Financial Distress. *Universitas Brawijaya Malang*, *47*(1), 103–112.
6. Ignasia Natania Astria Gunawijaya. (2015). Pengaruh Karakteristik Komite Audit, Independensi Dewan Komisaris, Reputasi Auditor, Terhadap Financial Distress. *Jurnal Akuntansi Bisnis, Vol.XIV No.27 September 2015*, *16*(2), 39–55. https://doi.org/10.1377/hlthaff.2013.0625
7. Jensen, M. C., & Meckling, W. H. (1976). Theory of the Firm: Managerial. *Journal of Financial Economics*, *3*, 305–360. https://doi.org/http://dx.doi.org/10.1016/0304-405X(76)90026-X
8. Nur, E., & Yuyetta, A. (2019). Analisis Pengaruh Mekanisme Corporate Governance Terhadap Probabilitas Terjadinya Financial Distress. *Diponegoro Journal of Accounting*, *8*(3), 1–11.
9. Paramastri, W. W., & Hadiprajitno, P. B. (2017). PENGARUHMEKANISME TATA KELOLA PERUSAHAAN TERHADAP KESULITAN KEUANGAN (Studi Empiris pada Perusahaan Manufaktur yang Terdaftar di BEI Tahun 2014-2015). *Diponegoro Journal of Accounting*, *6*(4), 1–13.
10. Pernamasari, R., Purwaningsih, S., Tanjung, J., & Rahayu, D. P. (2019). *Good Corporate Governance and Prediction of Financial Distress to Stock Prices : Atman Z Score Approach*. *6*(11), 56–62.
11. Putri, N. W. K. A., & Merkusiwati, N. A. K. L. (2014). Pengaruh Mekanisme Corporate Governance, Likuiditas, Leverage, dan Ukuran Perusahaan Pada Financial Distress. *E-Jurnal Akuntansi Universitas Udayana*, *7*(1), 93–106.
12. Rebecca, Y., & Siregar, S. V. (2012). Pengaruh Corporate Governance Index, Kepemilikan Keluarga, dan Kepemilikan Institusional terhadap Biaya Ekuitas dan Biaya Utang: Studi Empiris pada Perusahaan Manufaktur yang Terdaftar di BEI. *Simposium Nasional Akuntansi XV, Banjarmasin*, (2004), 1–28.
13. Septiani, N. M. I., & Dana, I. M. (2019). Pengaruh Likuiditas, Leverage, Dan Kepemilikan Institusional Terhadap Financial Distress Pada Perusahaan Property Dan Real Estate. *E-Jurnal Manajemen Universitas Udayana*, *8*(5), 3110. https://doi.org/10.24843/ejmunud.2019.v08.i05.p19
14. Triwahyuningtias, M., & Muharam, H. (2012). Analisis Pengaruh Struktur Kepemilikan, Ukuran Dewan, Komisaris Independen, Likuiditas Dan Leverage Terhadap Terjadinya Kondisi Financial Distress (Studi Pada Perusahaan Manufaktur Yang Terdaftar Di Bursa Efek Indonesia Tahun 2008-2010). *Diponegoro Journal Of Management*, *1*(1), 1–14. Retrieved from file:///C:/Users/JAVIER/Downloads/30725.pdf
15. Widhiari, N., & Aryani Merkusiwati, N. (2015). Pengaruh Rasio Likuiditas, Leverage, Operating Capacity, Dan Sales Growth Terhadap Financial Distress. *E-Jurnal Akuntansi*, *11*(2), 456–469.