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EFFECT OF INDEPENDENT AUDIT COMMITTEE TO EFFECTIVENESS OF CORPORATE GOVERNANCE

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ABSTRACT

The purposes of the research is to study and to analyze the effect of independent audit committeetoeffectiveness of corporate governance,this research used explanatory method, and unit of analysis is banking companies listed in the Indonesia Stock Exchange from 2011 to 2018.

INTRODUCTION

Ernst & Young and the Institute for Development & Research in Banking Technology (2013) and Ernst & Young (2014) in their 2014 survey in several countries including Indonesia, predicted that the banking industry would be increasingly faced with a challenging environment. Ernst & Young's survey (2014) found that the environment was in the form of alternative services provided by non-bank alternatives (growing non-bank alternatives), inconsistent customer satisfaction, increased use of digital banking, reduced process error rates for satisfaction customers, the loss of customer loyalty, and the increasing number of complaints from new customers over the services theyenjoy.

The complexity of the development of the banking industry, then various problems stemming from the internal multiple occur as well as in other industries. One of the latent problems for various types of businesses is an internal problem that is able to bring down the value of shares and even bankrupt a business, and more broadly cause various problems both for the authorities and for the wider community. This problem is a corporate scandal (corporate scandals) that began with the problem of corporate governance in various sectors that have occurred so far.

Monitoring of implementation in Indonesian banking, the Financial Services Authority (OJK) assesses that not all banks have good corporate governance or above that level, 66 banks (64.7%) out of 102 banks that were rated as "good" and 1 bank that was rated "above good". The rest (33 banks) are included in the "good enough" category.For this reason, it is necessary for the banking industry to have an adequate monitoring mechanism that is capable of acting as an extension of shareholders and, more broadly, stakeholders so that the company's path does not deviate from the objectives of meeting the needs of these parties. . The need is a guarantee of profits and a continuous increase in business value for the owner as well as other benefits for the stakeholders including the fulfillment of compliance with regulations set by the authorities.

OBJECTIVE OF THE STUDY

This research examinesthe effect ofindependent audit committeeto effectiveness of corporate governance.

LITERATURE REVIEW

Corporate governance is a way to monitor the relationship between company management (agent) and its principals and wider stakeholders. The implementation of corporate governance does not apply standards (not "one-size-fits-all"), but varies / varies in different countries and companies (OECD, 2000). This diversity reflects the social values that are unique in each country / company, different ownership structures, and the business environment, the competitive environment and the extent to which contracts can be implemented. The political position of shareholders and lenders (debt holders) as well as legal certainty is crucial for the implementation of effective corporate governance (Gregory and Simms, 1999).

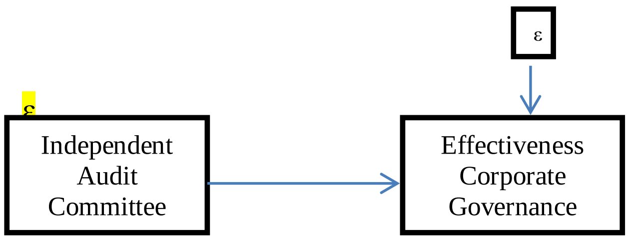
Corporate governance has an interest in the social, political and legal environment in which the company operates and the formal and informal regulations governing the company. Corporate governance, therefore, is very important for every organization / company because its good implementation will contribute to better organizational/company performance (Yusoff and Alhaji, 2012).

Good Corporate Governance (GCG)guideline of the Indonesian Banking (National Committee on Corporate Governance Policy, 2004) state that GCG contains 5 (five) main principles, namely transparency, accountability, responsibility, independence and fairness. The definition of GCG in a regulation issued by Bank Indonesia (PBI 8 / `4/006) is a corporate governance bank that applies 5 (five) principles similar to the above. The use of the five principles is to create protection for the interests of all interested parties (stakeholders). The corporate governance structure of banking can include several components: shareholders, board of commissioners, directors, auditors and audit committees, compliance officers, company secretaries, sharia supervisory boards (for sharia banking) and stakeholders.

Neeshu (2014) mentions that there are 3 (three) types of mechanisms and control of corporate governance that are known in this world. First, the internal mechanism that comes from the mechanism from within the company and serves to monitor the progress and activities of the organization and take corrective actions if the organization deviates from the stated objectives. This type of mechanism includes control (internal control) by management, an independent internal audit (independent internal audit) and the structure of the Board of Commissioners (board of directors). Second, external mechanisms that come from outside the company and function among others are for compliance with regulations. This type of mechanism includes the form of authority / regulator and the government, an independent audit that functions to audit financial statements for internal and external stakeholders of the company.In that context, to measure corporate governance the researchers use a variety of measures. As a measure of external control mechanisms used include the stock market and competition in the product market (Macey and O'Hara, 2003).

RESEARCH MODEL

The research modelcan be describedas follows:



HYPOTHESIS

Hypothesis can be defined as a tentative, yet testable, statement, which predicts what a researcher expects to find in an empirical data. Hypothesis is derived from the theory on which a conceptual model is based and often related in nature.The hypothesis proposed in this study is that independent audit committee influences effectiveness of corporate governance.

RESEARCH METHODOLOGY

This is research used explanatory method to describe relationship between variables through hypothetical testing. Whereas, the variables studied in this research are independent audit committee and corporate governance

Population and samples studied in this research is Banks from Indonesia Stock Exchange period 2011 to 2018.

Confident level used 95% with $\alpha = 5\%$ to evaluate the data quality and statistic test. The regression equation used to describe the number of change of independent variable to the dependent variable is as follows:

$$CG = \alpha + \beta IA + e$$

IA = Proportion of independent audit committee
CG = Corporate Governance
α_0= Constanta
ßi = Regression Coefficient
e= Epsilon/Controlling Variable

Statistic data analysis use regression test t-test and coefficient of determination to evaluate the effect of independent audit committeeto effectiveness corporate governance and how much further does the effect on the corporate governance.

DATA ANALYSIS&INTERPRETATION

This study uses a sample of 28 companies in the banking sector which are listed on the Indonesia Stock Exchange. The research period used was from 2011 to 2018.

Corporate banking governance is measured by the existence of an independent audit committee which is an important element of the sustainability of the governance. According to Suhadak et al., (2012) the success of corporate governance is determined by the mechanism of the independent audit committee and the independent commissioner.The average ratio of independent members on the audit committee was 40.35% of the total number of audit committee members, with a median of 40.21% and a standard deviation of 1.19%. A total of 13 banks only have 1 (one) independent member of the Audit Committee. On the other hand, there is 1 (one) bank that has all members of the audit committee coming from an independent element namely Bank Panin Indonesia Tbk.

Based on the results, can be explained as:

Table 1

Variable	Coefficient	Std. Error	t-Statistic	Prob.
IA	0.119261	0.041767	2.805357	0.0047
C	-0.000187	0.008698	-0.021521	0.9828

The results showed that the results of the hypothesis test showed t arithmetic> t table, which is 2.805> 1.96, meaning that the independent audit committee effect on effectiveness of corporate governance.

CONCLUSION

The results showed that the proposed regression model was fixed with a calculated t value> t table. Hypothesis test results show that the independent audit committee effect on effectiveness of corporate governance.

The existence of an independent audit committee is required by the authorities (the government) because it is expected to be able to realize additional oversight functions and advisory functions for the running of the company's business wheels. Both functions, if carried out by an independent party to the company, will be more objective and can provide a balance between the interests of the majority shareholders and also the protection of the interests of minority shareholders and the interests of other stakeholders. To emphasize this independence, the authority regulates that an independent audit committee is a member of the Board of Commissioners from outside the issuer or public company. In terms of ownership, independent audit committee may not own shares either directly or indirectly in issuers or public companies.

Meanwhile, for banking, an independent audit committee is defined as a member of the Board of Commissioners who has no financial, management, share ownership and/or family relationship with other members of the Board of Commissioners, Directors and/or controlling shareholders or other relationships that can affect his ability to act independently (PBI on the Implementation of Good Corporate Governance, 2006).

The existence of an independent commissioner is necessary given that in business practice, transactions that often contain conflicts of interest often overlook the interests of the public shareholders (minority shareholders) as well as other stakeholders. The existence of an independent commissioner is even more important, especially in companies that use public funds in business financing, such as banking. Meanwhile, an independent audit committee is a committee formed by the Board of Commissioners with the function of assisting the implementation of the supervisory duties of the company. To maintain its independence, the audit committee membership by the authorities is required to have a membership that is independent of the bank's management function as a company. The audit committee at least has members consisting of: an independent commissioner (as chair of the audit committee); an independent party who has expertise in finance or accounting; and one from an independent party who has expertise in the field of law or banking. The total number of independent commissioners and independent parties is at least 51% of the total number of members of the audit committee.

Foreign investors, especially those in the form of institutions in terms of concern for monitoring the running of the company they own, according to Hideaki et al., (2015) can have 2 (two) forms. First, what is called a positive view is that foreign ownership is interested in being fully involved in the monitoring process, including in determining the members of the independent commissioner in addition to encouraging the provision of incentives to management so as to encourage organizational reforms that lead to an increase in company performance. The results of this study found that independent audit committee can influence corporate governance. This is consistent with the results of the study of Mangena and Tauringana (2007), who found a positive and significant relationship between independence of the audit committee with corporate governance. This independence is measured by the proportion of the number of independent commissioners who are members of the audit committee. Meanwhile, in the Indonesian banking industry an independent audit committee has at least one independent commissioner who chairsthecommittee.

Based on the above, independent foreign ownership of company management has a tendency to influence the monitoring of company operations, including the appointment of an independent commissioner and an audit committee.

SUGGESTIONS

Foreign ownership for banks must be responded positively. Its influence on the existence of an independent audit committee will support the oversight function of the company's running well. The foreign ownership also has a positive effect on bank profitability and capital. The existence of foreign ownership in the banking industry must have a real contribution on the micro side of the company in the form of improved profitability which will ultimately increase tax contributions to the state, and also on the macro side, namely in the form of an intermediary function needed to finance development. Of course, this must be accompanied by the implementation of oversight functions both on-site and off-site to ensure that positive contributions occur.

The government/regulator should support the implementation of corporate banking governance through oversight of the independence of the audit committee in the banking industry as part of regulations for micro and macro reinforcement, as well as the capabilities of the audit committee members as the supervisory function of the company.

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