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The Effect of Good Corporate Governance on Performance of Pharmaceutical Company

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Abstract - The purpose of this study is to analyze the effect of good corporate governance which consists of the audit committee, board of directors, quality of External Auditor, and independent commissioners on the performance of pharmaceutical companies in Indonesia. Data of this study is all pharmaceutical companies in Indonesia, which in 2018 are listed in the Indonesian Capital Market Directory (2019), totaling 100 companies. Samples were taken by purposive sampling technique, based on the specified criteria obtained a sample of 88 companies. The data analysis method used is multiple regression analysis model usingthe SPSS for Windows Release 16.0 program. The results of this study indicate that the variable of the board of directors and the quality of External Auditor has a significant effect on company performance, whereas the audit committee and independent commissioners have no effect on company performance. The adjusted R2 value was 36.7%, the remaining 63.3% was explained by other factors outside the model under study.

Keywords: *good corporate governance, audit committee, board of directors, quality of external auditor, independent commissioners*

INTRODUCTION

Corporate governance is corporate governance that explains the relationship between various participants in the company that determines the direction of company performance. Issues regarding corporate governance began to emerge, especially in Indonesia in 1998 when Indonesia experienced a prolonged crisis. The main characteristic of weak corporate governance is the act of selfishness on the part of company managers by ignoring the interests of investors. Thus, this will result in a decrease in capital inflows to a country while the capital outflows from a country will increase. The next result is a decline in share prices in that country, so that the capital market does not develop and the exchange rate of the country's currency decreases. (Darmawati and Rika, 2004). The company's performance will be good if the company is able to control the behavior of the company's top executives to protect the interests of the company owners (shareholders), one of which is the existence of an audit committee. The audit committee is expected to be able to supervise financial reports, supervise external audits and supervise the internal control system.. The board of directors has the duty to determine the direction of all resources owned by the company, both for the short and long term. (Iqbal Bukhori, 2012). The greater the distribution in board members can lead to more conflict, but this distribution can provide alternative solutions to a more diverse problem than a homogeneous board member. External Auditirsthat are included in the Big four auditor category are often considered to be able to provide high-quality audits. Higher quality audits are associated with less likelihood of reporting problems and more effective financial and internal controls. Thus, Big Four External Auditors is more qualified in detecting value according to Teoh and Wong (1993) in Herawaty (2008). To comply with Good Corporate Governance guidelines in order to maintain independence, effective, precise and fast decision making, companies must have independent commissioners who have at least 30% (thirty percent) of the total number of commissioners. (Pratiwi, 2010). Thus, the role of the independent board of commissioners can improve earnings quality by limiting the level of earnings management through the monitoring function of financial reporting. This research is a continuation of research conducted by Carningsih (2009), Herawaty (2008), and Jati (2009). This study aims to analyze the effect of good corporate governance which consists of the audit committee, board of directors, quality of public accounting firms, and independent commissioners on company performance.

LITERATURE REVIEW

In agency theory, the principal is the shareholder and the agent is the management who manages the company. Agency relationships can create problems when the parties concerned have different goals. Owners of capital want increased wealth and prosperity for capital owners, while managers also want increased welfare for managers, so that conflicts of interest arise between owners (investors) and managers (agents). (Darwis, 2009).

Corporate Governance according to Nasution and Setiawan (2007) is a concept proposed to improve company performance through supervision or monitoring of management performance and guarantee management accountability to stakeholders based on the regulatory framework. The concept of corporate governance is proposed in order to achieve a more transparent company management for all users of financial reports.

The pillars that underlie the principles put forward by the Organization for Economic Corporation and Development (OECD) are as follows: a. Transparency (Transparency) b. Fairness majority and minority shares as well as foreign shareholders. c. Accountability d.Responsibility. According to Carningsih (2009), the elements of Good Corporate Governance are: a. Commissioners and Directors b. Shareholders c. Audit Committee d. Managers and Workersand e. company secretary. The corporate secretary is in charge of regulating all access to information on activities related to the company, including: 1) Internal Auditor, is tasked with auditing the company's control system and at the same time providing reports on the results of the assessment. 2) External Auditor, in charge of auditing the financial statements produced by the company. and3) The Stakeholders consists of creditor, investor, government, public and employee.

According to Aldridge and Sutojo (2005) in Susanti (2010), the implementation of good Good Corporate Governance has five benefits, including: a. Able to increase the value of the company and its shareholders. b. Able to improve the efficiency and effectiveness of level management work above and the board of commissioners. c.Able to protect the rights and interests of shareholders. d. Able to protect the rights and interests of members who interests other than shareholders. e. Improve the quality of the relationship between shareholders, the board of commissioners, and the top level management of the company.

The company's performance is influenced by several factors, including the concentration or lack of concentration of earnings manipulation and disclosure of financial statements. The interests that are concentrated by many institutions will facilitate control so that it will improve company performance. (Hastuti, 2005). In this study, company performance is measured using Tobin's Q. Tobin's Q is the most widely used assessment measure in corporate financial data. The reason for using Tobin's Q as a company performance measurement is because with Tobin's Q, it can be seen that the company's market value reflects the company's future profits such as current profit. The greater the value of Tobin's Q ratio indicates that the company has good growth prospects and has bigger intangible assets. Companies with high Tobin's Q value usually have a very strong company brand image, while companies that have low Tobin's Q value are generally in very competitive industries or industries that are starting to shrink.

Companies listed in the corporate governance rating score conducted by IICG have implemented good corporate governance and have directly increased the value of their shares. The higher the implementation of corporate governance as measured by Tobins' Q, the higher the level of company compliance and resulting in good company performance. (Dervish, 2009)

Development Research conducted by Carningsih (2009) states that there is no relationship between corporate governance and firm value as measured by using Tobin's Q and company performance as measured by using ROA. There is also research conducted by Herawaty (2008) which states that there is a positive relationship between Good Corporate Governance and company performance. The variables that have a significant effect on firm value are corporate governance, firm size and earnings management. Independent commissioner, audit quality, institutional ownership are moderating variables between earnings management and firm value. The next research is Jati (2009), which states that there is a positive relationship between Good Corporate Governance and company performance. The result of this study is that there is a significant influence between the corporate governance structure variables on company performance as measured by ROA and there is no significant influence between the corporate governance structure variables on the company performance as measured by ROE. The audit committee is a committee appointed by the company to act as a liaison between the board of directors and external audit, internal auditors and independent members. The audit committee is assigned to provide oversight to the company's internal and external auditors, as well as ensure that management takes its corrective actions 5 appropriate periodically and can control weaknesses, inconsistencies with policies, laws and regulations. (Jati, 2009). On the basis of the description above, the research hypothesis can be stated as follows:

H1: The audit committee has an effect on company performance The board of directors has a very vital role in a company.

The board of directors has the duty to determine the direction of all resources owned by the company, both for the short and long term. (Iqbal Bukhori, 2012). The greater the distribution in board members can lead to more conflict, but this distribution can provide alternative solutions to a more diverse problem than a homogeneous board member. On the basis of the description above, the research hypothesis can be stated as follows:

H2: The board of directors has an effect on company performance.

External Auditor which is included in the Big four category of auditors are often considered to be able to provide high quality audits. Higher quality audits are associated with reduced likelihood of financial reporting problems and more effective internal control. Thus the Big Four external auditor is more qualified in detecting value according to Teoh and Wong (1993) in Herawaty (2008). On the basis of the description above, the research hypothesis can be stated as follows:

H3: The quality of the External Auditor has an effect on company performance.

Independent commissioners who have at least 30% (thirty percent) of the total members of the commissioners, have fulfilled the Good Corporate Governance guidelines in order to maintain independence, effective, precise and fast decision making. (Pratiwi, 2010). The number of independent boards of commissioners is increasing, indicating that the board of commissioners who performs supervisory and coordination functions in the company is getting better. On the basis of the description above, the research hypothesis can be stated as follows:

H4: Independent commissioners have an effect on company performance.

METHODOLOGY

This study uses secondary data. The data used comes from data and annual financial reports of pharmaceutical companies in the Indonesian Capital Market Directory (ICMD), www.idx.co.id and the websites of pharmaceutical companies that were selected as research samples.

The population in this study were all companies included in the pharmaceutical industry which were listed on the Indonesia Stock Exchange (IDX) in the 20018 period. The sampling technique was carried out by purposive sampling. The criteria used to determine the sample are as follows: 1 The company publishes annual financial reports for the period ended December 31, 2018. 2. The company is a manufacturing industry group listed on the Indonesia Stock Exchange (IDX) during the 2018 period. 3.Has complete data with the variables used.

The dependent variable in this study is company performance. The company's performance in this study is measured by Tobin's Q. The calculation of Tobin's Q is adjusted to financial transactions in Indonesia (Darmawati and Rika, 2004) which are contained in this study as follows: Tobin's Q = Market Value of Equity + Debt Total Assets. Where: MVE = closing price at the end of the financial year x the number of ordinary shares outstanding. DEBT = (Current Debt - Current Assets) + Book Value of Inventory + Long-Term Debt

The audit committee is measured by the number of audit committee members in a company (Kusumawati&Riyanto, 2005).Board of Directors in this study is measured by the number of members of the board of directors in a company. (Kusumawati&Riyanto, 2005). Quality of External Auditor in this study uses a group of auditors (Big four). In measurement using dummy variables. If the company's financial statements are audited by external auditor in the Big four group it is denoted by number 1, for companies whose financial statements audited by external auditor that are not included in the Big four are denoted by the number 0. Independent Commissioner in this study are measured by the total number of independent commissioners in a company.

Multiple Regression Analysis is used by using Classical Assumption Test which includes normality test, multicollinearity test, heteroscedasticity test, and autocorrelation test.

RESULTS AND DISCUSSION

The normality test in this study used the Kolmogorov-Smirnov (K-S) test.

Variable	Kolmogorov Smirnov Z	P Value	

Unstandardized Residual	0,867	0,744	Normal

Source: The results of data processing

The results of the normality test above indicate that the research data has been normally distributed as evidenced by the asymp sig. amounting to 0.744 which is greater than the significance level of the study of 5% or 0.05. Because the research data has been normally distributed, the data can be used in testing with multiple regression models.

Multicollinearity testing is done by looking at the magnitude of the Tolerance Value and Variance Inflation Factor (VIF).

Variable	Tolerance	VIF
Audit Committee	0,775	1,101
Board of Directors	0,654	1,563
External Auditor Quality	0,866	1,362
Independent Commissioners	0,651	1,677
Dependent Variable: TobinsQ		
Source : Data Processing results		

The table above shows that the tolerance value for all variables in each regression model is greater than 0.1 and the value of the inflating factor value for all variables in each regression model is less than 10. The results of this test indicate that in the models The regression used in this study did not occur multicollinearity symptoms. To detect the presence or absence of deep heteroscedasticity model, used the Glejser test.

Variable	Sig.	Criteria	Remarks
(Constant)	0,752	α>5%	No Heteroscedasticity
Audit Committee	0,364	α>5%	No Heteroscedasticty
Board of Directors	0232	α>5%	No Heteroscedasticity
External Auditor	0,773	α>5%	No Heteroscedasticity
Independent Commis.	0,767	α>5%	No Heteroscedasticity

Source: Processed Data

To find out whether the regression model contains autocorrelation, the D-W approach (Durbin Watson) can be used.

D-W	Criteria	Remarks
1,544	-2 to 2	No Autocorrelation

Sources: Processed Data

The table above shows that the D-W value is 1.544 which is between -2 to 2. These results indicate that there is no autocorrelation symptom in the regression model used in the study.

5.2 MULTIPLE REGRESSION TESTING

Variable		coefficient	t test	Sig
Constant		0,008	0,021	0,665
Audit Committee		0,215	0,446	0,754
Board of Directors		0,078	2,876	0,003
External Auditor Quality		0,445	3,143	0,064
Independent Commissioner		-0,028	0,337	0,508
Ftest		12,469		0,001
Adjusted R^2		0,367		
Source: Processed Data				

The F testis used to test the regression model whether the independent variable is appropriate in measuring the dependent variable. From the test results obtained a significance value of F of 0.001, this indicates a significance value of F <0.05, so it can be concluded that the model used for this study is a fit model.

The coefficient of determination states the percentage of the total variation of the dependent variable that can be explained by the independent variables in the model. In this study using the adjusted R2 value. Based on the table above, it is known that the adjusted R2 is 0.367. This means that 36.7% of the variance in company performance can be explained by independent variables (audit committee, board of directors, quality of External Auditor, and independent commissioners). While the remaining 63.3% is explained by other variables outside the model.

To see whether the hypothesis is accepted or rejected in this study is to compare the significance value t with the significance level used, namely 0.05 ($\alpha = 5\%$). The significance value of t for the audit committee variable of 0.170 is greater than 0.05 so that H1 is rejected. The significance value of t for the board of directors variable is 0.003 less than 0.05, so that H2 is accepted. The significance value of t for the quality variable of External Auditor is 0.034, which is greater than 0.05, so that H3 is accepted. The significance value of t for the quality variable of External Auditor is 0.032 which is smaller than 0.05 so that H3 is accepted. The significance value of t for the independent commissioner variable, it is 0.608, which is greater than 0.05, so H4 is rejected.

DISCUSSION

The test results show that the audit committee has no effect on company performance with a significance value of 0.546> 0.050. Thus, it can be stated that the number of audit committees does not affect the level of company performance. The results of this study are inconsistent with the research of FramudyoJati (2009) that the audit committee has an effect on company performance. 5.3.2 The Effect of the Board of Directors on Company Performance The test results show that the board of directors has a positive and significant effect on company performance with a significance value of 0.003 <0.050. Thus, it can be stated that the size of the board of directors can affect the level of company performance. The board of directors has a very vital role in a company. The board of directors has the duty to determine all resource directions owned by the company, both for the short and long term. (Iqbal Bukhori, 2012). The distribution of the board of directors is thought to have had a positive impact. The greater the distribution in board members can lead to more conflict, but this distribution can provide alternative solutions to a more diverse problem than a homogeneous board member. The results of this study are consistent and support the research of FramudyoJati (2009) that the board of directors has an effect on company performance 12

The test results show that the quality of External Auditor has a positive and significant effect on company performance with a significance value of 0.034 <0.050. Thus, it can be stated that the high and low quality of External Auditor can affect the level of company performance. Public accounting firms that provide high quality audits can reduce financial reporting problems and more effective internal control. Thus, Big Four KAP is more qualified in detecting value according to Teoh and Wong (1993) in Herawaty (2008). The results of this study are consistent and support the research of VinolaHerawaty (2008) that the quality of the Public Accounting Firm (KAP) has an effect on company performance.

The test results show that the independent commissioners have no significant effect on company performance with a significance value of 0.608> 0.050. Thus, it can be stated that the number of independent commissioners does not affect the level of company performance. The results of this study are inconsistent with research by Carningsih (2009) and VinolaHerawaty (2008) that independent commissioners have an effect on company performance.

CONCLUSION

Based on the data obtained and from the data analysis carried out, the following conclusions can be drawn:

1. The results of the F test show that the independent variables have a significant effect together on company performance.
2. The number of members of the audit committee does not affect the level of company performance.
3. The amount of the board of directors can affect the high and low company performance.
4. High and low quality offices Public Accountants (KAP) can affect the level of performance company
5. The number of independent commissioners does not affect the height low company performance.

Some suggestions or recommendations for further research is that for future studies should carry out research over a longer period of time in order to significantly increase the sample size and result in a more in-depth study. Further research should use other proxies such as Return On Equity (ROE) or Return On Assets (ROA) because investors also see the company's equity in buying shares. Further research should also use the previous year's data (t-1) so that the results can be used for comparisons for the following year.

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