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The Effect of the Audit Committee on Financial Performance in Banking Companies Listed on the Indonesia Stock Exchange

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ABSTRACT

The purpose of this study is to empirically examine the effects of audit committees on financial performance in banking companies listed on the Indonesia Stock Exchange during 2016-2017 consisting of 43 companies. The method used in this research is purposive sampling method where companies that meet the criteria amount to 31. However, by removing outlier data as many as 7 companies leaving 55 companies. The analysis shows that the data used in this study meet the classic assumption test which includes: there is no autocorrelation, heteroscedasticity does not occur and the data is normally distributed. Based on the results of testing with simple regression, the following regression equation Y = 0.018 - 0.002KA is obtained. The test results indicate the value of t-counted is equal to -1.260 compared to the value of t-table (df = 52, α= 0.05) that is equal to 2.007. Because the research data is tested in 2-way, the critical point of acceptance of the hypothesis H0 is between -2.007 to 2.007. Therefore, because t-counted < t-table, i.e. -1.260 <2.007 and the probability obtained is 0.213 which is greater than 0.05 (α), then the hypothesis Ha is rejected. From the results of the simple regression analysis, it can be concluded that the variable audit committee has no significant effect on financial performance.

INTRODUCTION

The implementation of Good Corporate Governance (GCG) has been more intense since the emergence of accounting scandals such as the Enron and WorldCom cases involving accountants. In Indonesia, there have also been recorded several cases involving financial reporting issues such as PT. Lippo and PT. Kimia Farma which originated from the detection of manipulation (Boediono, 2005).The effective implementation of GCG can improve efficiency and economic growth as well as investor confidence (OECD, 2004). Improving the application of GCG has become a basic requirement because investment will follow sectors that adopt efficient governance standards (OECD, 2004). Companies that adopt GCG should have good financial performance.

The company's financial performance is one measure of the successful implementation of financial functions within the company. A good measure of company performance begins with investor confidence in a company that the funds they invest are in safe conditions and are expected to provide good returns.

The audit committee is one of the committees formed by the board of commissioners and is responsible to the board of commissioners with the main duty and responsibility being to ensure the principles of good corporate governance is upheld. To support the creation of good bank governance, every banking company that has been listed on the exchange must have an audit committee.

Several studies on the effects of GCG show mixed results. This is because the indicators for each variable to measure GCG and financial performance are different. Arifani (2013) in his research indicated that GCG measured by an independent commissioner had a significant positive effect on financial performance. However, this is not in line with research conducted by Tertius (2015) which shows that an independent commissioner has a negative effect on financial performance, while research by Veno (2015) indicates that an independent commissioner has no significant effect on financial performance. An independent commissioner is a member of the board of commissioners from outside the company that aims to provide protection for minority shareholders in a company.

Hartono (2014) in his research showed that GCG, as measured by the audit committee, had no effect on financial performance. This is different from Arifani (2013) and Veno (2015) whose respective studies show that the audit committee has a significant positive effect on financial performance. The audit committee is an extension of the board of commissioners in enforcing control and monitoring of the board of directors.

Based on empirical evidence linking between GCG as measured by independent commissioners and audit committees on financial performance that still shows different results, the specific purpose of this study is to examine how the influence of GCG on financial performance, especially in the banking sector in the Indonesia Stock Exchange in the period 2016-2017. Banking companies were chosen because universally this sector is an industry regulator and banks have access to government safety networks. Therefore, banks must have a strong GCG.

The purpose of this research is that the application of GCG today is no longer just an obligation, but has become a necessity for every company and organization. GCG is needed to drive the progress of a company's performance and to make the company live long and trustworthy.

Based on the description above, the authors are interested in conducting further research with the title “The Influence of the Audit Committee on “Financial Performance in Banking Companies Listed on the Indonesia Stock Exchange”.

FORMULATION OF THE PROBLEM

Based on the description presented in the background above, the authors conclude the formulation of the research problem as to whether the audit committee influences financial performance in banking companies listed on the Indonesia Stock Exchange.

THEORETICAL STUDY

1. Theoretical Study

a. Agency Theory

The agency theory perspective is the basis on which to understand corporate governance. Agency theory is a concept that explains the contractual relationship between the principal (owner) and agent (manager).In this agency relationship, the manager is the party who has more information about the company than the owner, so that here information asymmetry arises, a situation where there is a party that has more information from outside parties so that it benefits them (Deegan, 2004: 220).

Agency theory is very difficult to apply and has many obstacles and is still inadequate, so we need a clearer concept of funding protection for stakeholders. The concept must relate to issues of conflict of interest and agency costs that arise so that a new concept develops that pays attention to and regulates the interests of parties related to ownership and operation (stakeholders) of a company, namely the concept of good corporate governance.

Corporate governance as the effectiveness of mechanisms aimed at minimizing agency conflicts, with special emphasis on legal mechanisms that prevent the expropriation of both majority and minority shareholders. Corporate governance is one of the key elements in increasing economic efficiency, which includes a series of relationships between company management, the board of commissioners, shareholders, and other stakeholders. Corporate governance also provides a structure that facilitates the determination of the objectives of a company, and as a means of determining performance monitoring techniques.

b. Financial Performance

Financial performance is a picture of a company's financial condition that is analyzed by financial analysis tools so that the good or bad financial condition of a company can be known that reflects the work performance in a certain period. Financial performance is used as a reflection of the company's ability to allocate the sources of funds it has. Measurement of the company's financial performance is carried out to make improvements and control over the company's operational activities in order to compete with other companies. The financial performance of a company can be measured using financial ratios. Investors invest by taking into account, among other things, a profitability ratio. The profitability ratio used in this study is Return On Assets (ROA) because this ratio can provide an overview of the rate of return that investors can obtain for their investments (Prasinta, 2012).

c. Good Corporate Governance (GCG)

In their book, Brigham and Erhardt (2005) defines GCG as a set of rules and procedures that ensure that managers apply values-based management principles. GCG is defined by the Indonesian Institute of Corporate Governance (IICG) as a process and structure that is implemented to run a company with the primary objective of increasing value for shareholders in the long run and still paying attention to the interests of other stakeholders.

There are five basic principles in implementing good corporate governance practices, namely: (1) transparency that contains an element of disclosure, (2) accountability that contains an element of clarity of functions within the organization and ways of taking responsibility for it, (3) responsibility that contains the element of compliance with laws and regulations and the internal provisions of the bank as well as the responsibility of the bank to the community and the environment,(4) independence that contains an element of autonomy from the dominance of other parties and objectivity in carrying out their duties and obligations, and (5) fairness and equality that contains elements of fair treatment and equal opportunity in accordance with their proportions.

The mechanism of good corporate governance is divided into two parts, namely internal and external. The internal mechanism is carried out by the board of directors, the board of commissioners, the audit committee, and the ownership structure, while the external mechanism is more concerned with market influence in terms of control over the company and the applicable legal system.

The term good corporate governance is generally known as a good system and structure for managing companies with the aim of increasing value for shareholders as well as accommodating various stakeholders with companies that include creditors, suppliers, business associations, consumers, workers, government, and society large. The principle of good corporate governance can be used to protect minority parties from expropriations carried out by managers and shareholders with legal mechanisms.

d. Audit Committee

The audit committee is responsible for overseeing financial reports and external audits and observing internal control systems (including internal audits). The audit committee is placed as a monitoring mechanism between management and external parties. The audit committee on accounting and financial reporting aspects is expected to carry out several functions, namely: reviewing all financial statements to ensure objectivity, credibility, reliability, integrity, accuracy and timeliness of financial statement presentation; review accounting policies and pay special attention to the impact caused by changes in accounting policies, examine the effectiveness of internal control structures and ensure the level of compliance with them, evaluate the possibility of fraud and fraudulence, assess estimates, policies and management judgments considered to have a material effect on the financial statements.

The formation of audit committees by public companies has been widely carried out in various countries including Indonesia. As demands are strengthened so that companies are more transparent and reliable about their performance, the role of the audit committee is increasingly important. Capital Market and Financial Institution Supervisory Agency Circular Letter No. SE-03 / PM / 2000 states that the audit committee at public companies in Indonesia consists of at least three members and is chaired by an independent commissioner of the company with two to two from outside the company and independent. This illustrates that the increasing number of independent audit committee members in a company is expected to increase supervision so that company performance and financial report integrity can be better.

2. Relationship of Audit Committee and Financial Performance

One of the objectives of forming an audit committee is to improve the supervisory function of the board of commissioners as one of the governance structures. As revealed by Manik (2011), the audit committee as one of the structures of corporate governance, which in practice can inhibit fraud and manipulation of the company by upholding the principles of corporate governance. The existence of an audit committee can monitor the company's managers so as to minimize agency costs which can then make the company more efficient so that it can improve the performance of banking companies. This is supported by Veno (2015) and Arifani (2013) who in their research showed that the audit committee had a positive effect on financial performance.

3. Conceptual Framework

The conceptual framework was formed to show the influence of the independent variable namely the audit committee on the dependent variable namely financial performance as shown below:

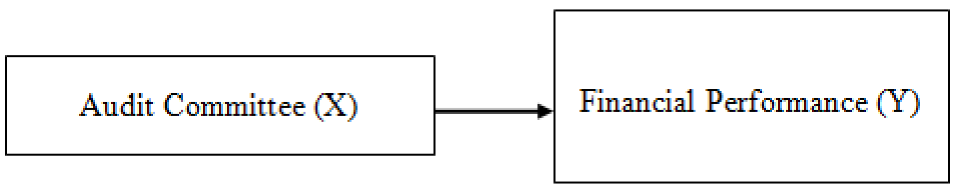

Figure 1. Conceptual Framework

4. Research Hypothesis

The hypothesis is a temporary answer to the problem in the research object. Based on the formulation of the problem, the hypothesis of this study is that the audit committee influences the financial performance of banking companies listed on the Indonesia Stock Exchange.

RESEARCH METHOD

1. Population and Sample

The population in this study is all banking companies listed on the Indonesia Stock Exchange during 2016-2017. The sampling technique in this study is by purposive sampling method with the aim of getting a representative sample. Purposive sampling is a sampling method based on a certain criteria, where the criteria used can be based on certain considerations or quotas (Erlina, 2011).

In this study, the criteria for banking companies that are used as a research sample are:

Banking companies listing during the research years.

Banking companies that submit audited financial statements in the research years.

Banking companies that use the rupiah.

Banking companies that did not generate negative profits during the research years.

The population in this study consisted of 43 banking companies. Banking companies in the population that meet the criteria to be sampled amounted to 31 with 62 units of analysis (21 x 3 years). However, by getting rid of outlier data consisting of 7 companies, the study sample consisted of 55 units of analysis.

2. Operationalization of Variables

Operationalization of variables is the main limitation of the problem to be examined. The variables that will be examined in this study are:

An audit committee is a committee formed by the board of commissioners to carry out supervisory duties over the management of the company. In this study, the variable audit committee is measured based on the number of audit committee members contained in the company profile (Sekaredi, 2011).

In this study, the dependent variable is financial performance where the proxy for this variable is ROA which is calculated by dividing net income after tax by total assets. Financial performance is formulated as follows (Syamsuddin, 2009):

$$ROA = \frac{Net\ Income\ After\ Tax}{Total\ Assets} \times 100\%$$

3. Classical Assumption Test

Before conducting hypothesis testing with simple regression analysis, there are several assumptions that must be met, namely:

Normality test

Autocorrelation test

Heteroscedasticity test

4. Data Analysis Technique

This study uses a simple regression analysis method that aims to measure the strength of a linear relationship between two or more variables.

The model used is simple regression, that is

$$Y = a + bX + \varepsilon$$

where:

Y = ROA

X = Audit Committee

a = Constant

b = Coefficient of Regression

ε = Confounding Variable

RESEARCH RESULTS AND DISCUSSION

1. Descriptive Statistic

Descriptive statistics provide an overview of data in terms of minimum, maximum, mean and standard deviation values. In this study, descriptive statistics will describe each of the following variables.

Table 1. Descriptive Statistics Test Results

	N	Minimum	Maximum	Mean	Std. Deviation
ROA	55	,0013	,0311	,011669	,0074827
KA	55	3,0000	5,0000	3,654545	,72567146
Valid N (listwise)	55				

Source: Research Results in 2019 (data processed by SPSS)

Descriptive statistical results for the variable financial performance measured by ROA (Y) show a minimum value of 0.0013 and a maximum value of 0.011 with a mean of 0.011669 and a standard deviation of 0.0074827.

Meanwhile, the results of descriptive statistics for the audit committee variable showed a minimum value of 3.0000, a maximum value of 5.0000, a mean of 3.654545, and a standard deviation of 0.7256716.

2. Classical Assumption Test

a. Normality Test

A good regression model is that each variable's data is normally distributed or close to normal. Normality testing can be performed by histogram charts and the Kolmogorov-Smirnov (K-S) test. If the histogram is shaped like a bell, then the data is normally distributed. If the value of Asymp. Sig. in the K-S test> 0.05, the data is said to be normally distributed. The results of complete data processing can be seen in the following table 2.

Table 2. Kolmogorov-Smirnov Test Results before Discarding Outlier Data

One-Sample Kolmogorov-Smirnov Test

		Unstandardized Residual
N	Mean	62
Normal Parametersa,b	Std. Deviation	,0000000
Most Extreme Differences	Absolute	,00883887
	Positive	,249
	Negative	,249
		-,161
Kolmogorov-Smirnov Z		1,961
Asymp. Sig. (2-tailed)		,001

a. Test distribution is Normal.

b. Calculated from data.

Source: Research Results in 2019 (data processed by SPSS)

From the table above it appears that the value of the significance of the K-S test is equal to 0.001 <0.05 which means the data is normally distributed. One way to overcome this is to remove outlier data or extreme data. After the outlier data is discarded, the data is tested again, the results of which are as follows.

Table 3. Kolmogorov-Smirnov Test Results after Outlier Data Are Removed

		Unstandardized Residual
N		55
Normal Parametersa,b	Mean	,0000000
Most Extreme Differences	Std. Deviation	,00737316
	Absolute	,105
	Positive	,105
	Negative	-,083
Kolmogorov-Smirnov Z		,780
Asymp. Sig. (2-tailed)		,576

a. Test distribution is Normal.

b. Calculated from data.

Source: Research Results in 2019 (data processed by SPSS)

From Table 3 it appears that the value of the significance of the K-S test is 0.576> 0.05, so it can be concluded that the data is normally distributed.

b. Autocorrelation Test

According to Ghozali (2016), the autocorrelation test aims to test whether in a linear regression model there is a correlation between confounding errors in the t period with confounding error in the t-1 period. If there is a correlation, it is said that there is an autocorrelation problem. Autocorrelation arises because consecutive observations over time relate to one another. This problem arises because the residual (confounding error) is not independent between observations with one another. This is often found in time series because "confounding" in individuals or groups tends to affect individuals or groups in the next period. A good regression model is a regression that is free from the autocorrelation problem.

In this study, autocorrelation symptoms were detected using the Durbin-Watson or DW-statistic test. A criterion for decision making is if du ≤DW ≤4.00 - du, then there are no symptoms of autocorrelation in the model. The results of data processing are shown in the following table.

Table 4. Autocorrelation Test Results

Model Summary b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	,170a	,029	,011	,0074424	1,977

a. Predictors: (Constant), KA

b. Dependent Variable: ROA

Source: Research Results in 2019 (data processed by SPSS)

From Table 4 it is known that the value of DW is 1.977. The test criteria are du ≤DW ≤4.00 - du. The value of du is 1.641, thus 1.641 ≤1.977 ≤ 2.359. This means that autocorrelation symptoms do not occur in the regression model.

c. Heteroscedasticity Test

The next classic assumption test is the heteroscedasticity test which aims to test whether in the regression model there is an inequality of variance of residuals from one observation to another. This research uses the glejser test. If the value of significance> 0.05, heteroscedasticity does not occur. The results by data are shown in the following table.

Table 5. Heteroscedasticity Test Results

Coefficients a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	,004	,003		1,311	,195
	KA	,001	,001	,086	,631	,530

a. Dependent Variable: ABS_RES

Source: Research Results in 2019 (data processed by SPSS)

From Table 5 above it is known that the value of significance is 0.530 for the independent variables greater than 0.05. This means that there are no symptoms of heteroscedasticity in the regression model.

3. Hypothesis testing

a. Coefficient of Determination (R2)

According to Ghozali (2018) the coefficient of determination (R2) or also called the goodness of fit of the model is measuring the extent to which the ability of the model explains the variation of the dependent variable. The value of the coefficient of determination has a range between zero and one. A value of R2 close to one means that the independent variable provides almost all the information needed to predict the dependent variable. The results of the coefficient of determination test are shown in Table 4.6 below.

Table 6. Determination Coefficient Test Results

Model Summary b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	,170a	,029	,011	,0074424

a. Predictors: (Constant), KA

b. Dependent Variable: ROA

Source: Research Results in 2019 (data processed by SPSS)

From Table 6 it is known that the value of the coefficient of determination in the R Square column is 0.029. This means that the audit committee variable affects financial performance by only 2.9%, while the remaining 97.1% is influenced by other variables not examined in this study. A value of determination coefficient that is very small or much smaller than 1 indicates that the influence of the audit committee on financial performance is very weak.

b. t-Statistic Test

Testing this hypothesis aims to determine whether the audit committee has an individual effect on financial performance. By using the probability value, if the probability is less than 0.05, then there is a significant effect of the independent variable on the dependent variable. The results of this test are shown in the following Table 7.

Table 7. t-Statistic Test

Coefficients a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	,018	,005		3,481	,001
	KA	-,002	,001	-,070	-1.260	,213

a. Dependent Variable: ROA

Source: Research Results in 2019 (data processed by SPSS)

Based on the results of tests with the simple regression shown in Table 7 above, the simple linear regression equation is obtained as follows.

$$Y = 0{,}018 – 0{,}002KA$$

A constant of 0.018 indicates that if the audit committee is not taken into account, then the probability of the company's financial performance is 0.018.

Independent variables included in the regression model had no significant effect on the company's financial performance.

4. **DISCUSSION**

The Effect of the Audit Committee on Financial Performance

The test results in Table 7 indicate that the audit committee variable has no significant effect on financial performance. This is evident from the value of t-counted at -1.260 compared to the value of t-table (df = 52, α= 0.05) which is equal to 2.007. Because this research was tested in 2-way, the critical point of acceptance of the hypothesis H0 is between -2.007 to 2.007. Therefore, because t-counted <t-table, which is -1.260 <2.007, and the probability obtained is 0.213 which is greater than 0.05 (α, it is concluded that the hypothesis Ha is rejected. The value of the regression coefficient, which is equal to -0.002 means that for every 1-audit committee, the financial performance will decrease by 0.002. The results of this study are not consistent with the research of Arifani (2013) which shows that the audit committee has a significant positive effect on financial performance. This indicates that with the establishment of the audit committee, this committee will be able to oversee management in improving its financial performance. However, the results of this study support research by Hartono (2014) which indicates that the audit committee has no significant effect on financial performance. Regulation of the Capital Market and Financial Institution Supervisory Agency No. LK. IX.1.5 requires companies that go public to have at least 3 audit committees so that the appointment of an audit committee is possible in banking companies which are only based on regulations but not based on company needs. In addition, there are indications that the formation of an audit committee is only limited to meeting formal requirements.

CONCLUSIONS AND SUGGESTIONS

1. CONCLUSION

From the results of the analysis and hypothesis testing that has been done, the researcher draws the conclusion that the audit committee has no significant effect on the financial performance of banking companies listed on the Indonesia Stock Exchange in 2016-2017.

2. SUGGESTION

From the conclusions outlined in the briefcase, the authors propose the following suggestions:

The next researcher should increase the number of companies as a sample to be studied, so it's not just banking companies.

The next researcher should extend the observation period.

The next researcher is recommended to examine other variables that might have an effect on the company's financial performance.

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