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Corporate Governance Structure and Internal Control Disclosure of Consumer Goods Firm in Indonesia

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ABSTRACT

The aim of this study is to find empirical evidences about the effect of corporate governance structure on internal control disclosure. Corporate governance structure is measured by using proxy of public ownership, managerial ownership, institutional ownership, board of commissioner's activity, and the proportion of audit committee that have educational background in accounting or financial. All of consumer goods listed companies become the population of this study and the samples are the annual reports taken from the consumer goods listed companies in the period of 2010-2012, that have met the study criteria. It uses 90 companies. This study is examined with multiple regression analysis. The results of this study indicate that public ownership, managerial ownership, institutional ownership, and board of commissioner's activity have positive effect on internal control disclosure. The proportion of audit committee that have educational background in accounting or financial has no effect on internal control disclosure.

Keywords: Internal control disclosure, Corporate governance structures, Public ownership, Managerial ownership, Institutional ownership, Board of commissioner's activity, Audit committee.

1. Introduction

In the globalization era, companies compete to be the best at what they do. Many ways done, include doing fraud to cover companies actual position (Ernst & Young, 2013). As WorldCom did, fraud happen because of the internal control failure and lack of awareness to disclose apropriate information. A good internal control will create an effective control system and will help identification process, management, and on comunicating information to stakeholder (Saha and Arifuzzaman, 2011). An effective internal control system is management's responsibility that should be inform to stakeholders. Management could informed company's internal control trough disclosure on yearly report, so information users can make a judgemnet on situation, growth and company's development relevant on company's internal control (Leng and Ding, 2011). Disclosure also needed to avoid conflict appearance caused by information asymmetry due to a diference in information received by agen and pricipal (Hunziker, 2013). To reduce the possibility of information asymmetry, companies need to disclose their information on their annual report (Khodadadi et al., 2010). Only then, information disclosure on internal control said as monitoring mechanism which can make less conflict between management and stakeholders (Deumes, 2004).

To give guarantees on the existence of broader disclosure, needs institutional system, that is Corporate Governace which is aims to monitoring manager so they disclose sufficient information that can give company a good impression and reputation to publics (Akhtaruddin et al., 2009). Corporate governance is a kit of rules that manage the relationship between stockholder, management, krediturs, government, employees, and other extern and intern stakeholder, related to their rights and responsibilities, or a system that is manage and lead company (FCGI, 2002).

Many countries was doing studies on internal control. Spira and Page (2010) in England discuss on internal control disclosure as regulatory tool, while Mc Mullen et al. (1996) discusing internal control reporting and financial reporting. Results of those studies find that only 742 out of 2221 companies in America whose disclose internal control in their annual report. Owusu-Ansah (2010) study the relationship between internal control disclosure with the characteristic of non-financial domestic company in America. The result show that there is a significant negative influence between internal control disclosure and inpartiesr (management) ownership, and there are no significant influence on institutional ownership. Zhang et al. (2007) examine the relationship between audit commitee quality, independent auditor, and disclosure of internal control weakness after Sarbanes Oxley Act (SOX) enforcement. The result show that there is a connection between audit commitee quality, independent auditor, and disclosure of internal control weakness. Zhang et al. (2007) also find that companies identified to have a weakness on internal control if the audit commitee lack or do not have skill in accounting or finance.

Other research on internal control disclosure doing Leng and Ding (2011) whose analyze the influence corporate governance structure on non financial companies listed on China Stock Exchange in 2010. Eng and Mak (2003) examine the influence of ownership structure and board ownership on voluntary disclosure which include internal control disclosure. The result show that lower managerial ownership and a significant government ownership related to the increase of voluntary disclosure. Therefor, the number of blockholder ownership do not related to the number of voluntary disclosure. Deumes (2004) studying on internal control disclosure as monitoring mechanism that can reduce conflict between agen and principal, the result show that voluntary disclosure on internal control significantly corelated with management ownership and stock precentage own by big investor, but it is not corelated to leverage and asset proportion. In addition, voluntary disclosure on internal control significantly corelated with company's size.

This research is rever to Leng and Ding (2011) which is analyze the effect of corporate governance structure to internal control disclosure of non financial companies listed in China stock exchange on 2010. Corporate governance structure studied by Leng and Ding (2011) are, the degree of ownership concentration, the proportion of state ownership, Board size, director's remuneration, director's education level, the proportion of independence directors, two part-time posts of chairman and general manager, the size of board of supervisors, and supervisor's education level. These research use control variable, company's size, profitability (earning per share), listed age, and stock exchange.

Result from these research, director's remuneration, two part-time posts of chairman and general manager, director's education level, and supervisor's education level positively affecting internal control. The proportion of state ownership negatively affecting internal control, while the degree of ownership concentration, Board size, the proportion of independence directors, and the size of board of supervisor do not significantly affect internal control disclosure.

This research have some differences with Leng and Ding's (2011). First, this research using sample of consumer goods companies listed in Indonesia stock exchange on the period of 2010-2012 as research object, while Leng and Ding (2011) use non financial companies listed in China stock exchange on 2010 as research object.

Second, corporate governance structure discuss in this research are company's ownership structure, Chairman board activities, and the proportion of audit comitee having accounting and financial education background. Company's ownership structure in this research are public ownership, managerial ownership, and institutional ownership. Third, internal control disclosure in this research is using internal control component in the Committee of Sponsoring Organozations of the Treadway Commission's (COSO's) 1992 Framework.

Motivation of doing this research is because as author's known, research on internal control disclosure has been found in some countries, but hardly find in Indonesia. Research perform to find an empirical evidence on the effect of corporate governance to internal control disclosure on consumer goods companies listed in Indonesia Stock Exchange in the period of year 2010-2012.

2. Literature Review and Hyphotetic Development

2.1. Agency Theory

Agency theory is a concept that explain the relationship between two parties called principal and agent. Principal will delegate its authority to agent for running and manage the company (Jensen and

Meckling, 1976). These both parties working together with aim to get benefit from the company (Watts and Zimmerman, 1990). Principal is willng to give facilities such as money and all resources they have, so the company managed by the agent will runing well and get huge profit. Agent willing to manage the company also with aim to get benefit. Frequently conflict of interest appear in the working process of these two parties (Jensen and Meckling, 1976). Agent who is directly manage the company will have more detail information about the company than the principal. Hendrikson and Van Breda (2000) said that these different information get by two parties will make one parties have a biger advantage, so an asimatry information would happen.

Asymmetry information happen would lead the agents to hide and faking information that should be report to principal (Eisenhardt, 1989). This is happen because the agent as company's manager want to get a big advantage from the company they manage, and they have a lot more information and detail on company's position (Saphiro, 2005).

To minimize the conflict of interest, anythings happen in the company have to be reported to principal. These report can be formed on information disclosure in annual report, so the principal can get information they need easier (Lang and Lundholm, 1996). Internal control disclosure hopefully can reduce information asymmetry (Kimbrough and Louis, 2010). With information disclosure, everythings happen in the company will be more transparant and known by stakeholders, and will press the possibilities of agents doing fraud.

2.2. Signaling Theory

Suwardjono (2005) state that signaling theory based the boluntary disclosure. Signaling theory shows an information asymmetry between management and other stakeholders. Tearney (2000) in Estiyanti and Yasa (2012) say that signaling theory explain why company have an iniciative and courage to give information to external parties. Signaling theory state that the most profittable company is the company whose disclose better and broader company's information (Bini et al., 2011).

2.3. Internal Control Disclosure

William L. Cary in Spira and Page (2010) say that disclosre is a realistic way to handle conflict taht always happen lately. Hunziker (2013) also explain that internal control system as management's tool to reach profitability and productivity target, and prevent to loose the resources. As explain above, disclosure serv accounting information in company's annual report to give accounting information for users, both internal and external parties. Internal control disclosure is a media which become an integral part of financial reporting and give information on company's internal control. Internal control system which is disclose in annuak report will help all information's users in the process of decision making. That is why, an effective internal control system should be disclose (Leng and Ding, 2011).

Barra et al. (2010) state that company needs internal control to ensure their company's efficiency and effectiveness. Internal control system judge to be effective, should be disclose in company's annual report so the external parties can decide better and mistake in decision making can be minimize (Al-Janadi et al, 2013).

2.4. Corporate Governance Structure

Corporate Governance Perception Index in The Indonesian for Corporate Governance (2012) state that corporate governance is a series of mechanism which is controls and leads a company, so the company's operation can run well as the stakeholders want.

Corporate governance as an operational base become a center to ensure the whole process and mechanism occurance to reach company's aims and preventing the company from fraud and any risk that can cause failure in reaching company's aim (IICG, 2000). Corporate governance sees capable to handle the agen problem or conflict of interest that may happen (FCGI, 2000).

Based on Indonesian Languange Big Dictionary (Kamus Besar Bahasa Indonesia), structure is an arrangement consist of elements connecting eachother in one whole piece, so corporate governance structure means as an arrangement of connective elements that is commission Board, audit committee, directors, and Share holder, acting as their rights and responsibilities (Miqdad, 2012).

Corporate governance required an elements structure in the company in order to reach the aims and monitoring of company's kinerja (Mintara, 2008). Forum Corporate Governance in Indonesia (FCGI, 2002) state that there are two form of board in the company that is, One Tier System which is come from Anglo Saxon law system, and Two Tier System from Europe continental. At the practice, Indonesia adopting Deutch law system which is follow Two Tier System. However, Two Tier System in Indonesia have difference with Two Tier System in Deutch. At Deutch, the Board of Director ellected and could be replace by Commissioner Board, while in Indonesia, at common situation Commissioner Board do not have right to point and fire the Board of Director (FCGI, 2002).

a. Public Ownership

Public ownership is company's share owned by public or society. Subiyantoro (2006) in Benardi et al. (2009) say that the more numbers of company's share owned by public, the more parties having interest and conflict occurs due to information asymmetry. That is why, companies whose share owned by public get a bigger pressure to disclose additional information on their annual report (Khan et al., 2012). Parties involved in the company will try to minimize conflict by giving assurance of their success in operational effectivness and efficiency, reliance on financial reporting, and obligation on law and regulations, result in a good internal control process. These supported by Akhtaruddin et al. (2009), to minimize information asymmetry, company need to disclose information on internal control (Healy and Palepu, 2001).

Based on those explanation, the hyphotesis are as follow:

H_1 : Public ownership positively affecting internal control disclosure.

b. Managerial Ownership

Soliman et al. (2012) say that the smaller shares owned by manager, the bigger interest conflicts will happen. These makes manager triying to maximize their own profit without conpartiesring pribcipal's interest. But, if manager as an agent have bigger shares, then the agent will try to perform productive and increase company's value (Juhmani, 2013). To increase company's value, information disclosure of company's performance on operational efficiency and effectiveness, reliance on financial reporting, and obligation on law and regulations are needed.

These reflect that company have been doing a good internal control and can minimize conflict of interest between agen and principal. Deumes (2004) in his research find that managerial ownership have a significant influence on internal control disclosure. Based on those, then the hypothesis in this research is as follow:

H_2: Managerial ownership have a positive influence on internal control disclosure.

c. Institutional Ownership

Shleifer and Vishny (1986) say that institutional investor is an investor who have a big fund invested in the company, so they have a huge influence on company's life. The numbers of share's proportion planted in the company give an effect on internal control disclosure, because these shareholder can demand disclosure on all information related in the annual report (Owusu-Ansah and Ganguli, 2010). Those disclosures shows in annual report hopefully can give information to shareholder institution regarding company's activity on internal control, which are operational efficiency and effectiveness, reliance on financial reporting, and obligation to law and regulations.

Research by Deumes (2004) state that there a significant influence of investor who have big numbers of company's share to internal control disclosure. Base on those explanatios, hypothesis develop is as following :

H_3: Institutional Ownership have a Positive Influence on Internal Control Disclosure.

d. Commissioner Board's Activities

National comission on Governance Policy (KNKG, 2006), state that one of Commissioner board and director's responsibility in keeping company's continuity at a long term shows in a good practice of internal control. Clearly, independency can affect Commissioner board's performance to make an objective and transparant decision. Commissioner board's activities, includes independent commissioner, such as commissioner board's meeting and supervisory activities is an important element to create a good corporate governance (ADES's annual report, 2011).

Commissioner board's activity is an important element to make a good corporate governance, because in activities such as commissioner board's meeting would discuss about company's strategy, policy evaluation, and handle interest's difference in the company (FCGI, 2002). More meeting activity by commissioner board, expected to have good implication on the company's supervision. Conger et al. (1998) say that commissioner board activities is important to increase commissioner board effectiveness.

A good supervision mechanism will also shows a good company's internal control. Commissioner board activities in this research measure using the frequency or the numbers of meeting conduct by Commissioner board in a year, just like the research by Achmad (2012) and Gantyowati and Fitria (2012). According to those explanation, then the hypothesis is as below :
H_4: Commissioner Board Activities positively influence internal control disclosure

e. Audit Committee with Accounting and Finance Education background

Audit committee is a supporting committee for commissioner board whose responsible to help commissioner board to ensure that the financial statement fairly reported as generally accepted accounting principle, that company's internal control structure running well, that internal and external audit performed suitable with audit standard, and the follow up of audit results perform by management (KNKG, 2006). With those duty and responsibilities, audit committee should have a good competency and capabilities. That is why, at least one of company's audit committee should have education bckground in accounting or finance (BAPEPAM, 2004).

Competency and capabilities they have will decrease weakness indication on internal control (Zhang et al., 2007). Accounting and finance education background at least provide overview that a member of audit committee who have competency and capabilitiy can ensure that company's internal controll running effectively (Wardhani and Joseph, 2010). Based on above explanation, the hypothesis is :
H_5: The Proportion of Audit Committe having accountingn or Finance education backgroud positively affecting internal control disclosure

3. Research Methodology

3.1. Population and Sample

The population used in this study are all companies included in the consumer goods industry sectors listed in Indonesia Stock Exchange (IDX) in 2010-2012. Samples were obtained using purposive sampling method (Bhattacherjee, 2012) to obtain a sample with predetermined criteria, so that the samples obtained by the company in the consumer goods industry that have met the established criteria.

The criteria used in the selection of the sample is the consumer goods industry companies listed on the Indonesia Stock Exchange in 2010-2012, the company publishes an annual report in full in 2010-2012 respectively, and the company has a complete data related to the variables used in the study.

This study uses secondary data derived from company annual reports obtained from the website of the Indonesia Stock Exchange (www.idx.co.id) or the official website of the company. Secondary data is data obtained from sources that already exist, in this study is the annual report.

3.2. Independent Variables

The independent variables are variables that influence or explain other variables (Bhattacherjee, 2012). Independent variables used in this research is public ownership, managerial ownership, institutional ownership, activities board of commissioners, and the proportion of the audit committee educational background in accounting or finance.

3.3. Dependent Variables

The dependent variable is a variable that is affected or explained by other variables (Bhattacherjee, 2012). The dependent variable is a variable that is caused or influenced by the independent variable (Nisfiannoor, 2013). The dependent variable used in this study is the disclosure of internal control.

Measurement of internal control disclosure in this study using the internal control disclosure checklist based on the COSO's Internal Control Framework in 1992 with a total of eighteen items are grouped into five components and forth in Internal Control Disclosure Index as measurements made by Leng and Ding (2011). If the item is contained in the annual report, then obtained a score of 1, if it is not found in the annual report of the obtained score of 0. Then, the total score obtained is divided by the total overall score.

4. Analysis and Discussion

Table-1. Descriptive Statistic Result

	N	Min	Max	Mean	Std. Deviation
Public Ownership	90	0,01	0,67	0,2424	0,14747
Managerial Ownership	90	0,00	0,43	0,0742	0,11578
Institutional Ownership	90	0,33	0,99	0,7767	0,18397
Activities board of commissioners	90	1,00	9,00	3,7778	1,95326
The proportion of the audit committee educational background in accounting or finance	90	0,20	1,00	0,5090	0,23706
Internal Control Disclosure	90	0,50	0,89	0,7394	0,08256

Based on the above data obtained results that public ownership in the company that tested has a minimum value of 0.01 or 1%, namely PT. Bentoel International Investama, Tbk, the maximum value of 0.67 or 67%, namely PT. Mayora Indah Tbk, the average value of 0.2424, or 24.2%, and the standard deviation of 0.14747 or 14.8%.

Managerial ownership has a minimum value of 0.00 or 0%, which means that some of the companies studied managerial ranks have no or very few have a stake in the company, the maximum value of 0.43 or 43%, which means that the maximum value of shares owned by the management of a company by 43%, ie by PT. Mandom Indonesia Tbk, the average value of 0.0742, or 7.4%, with a standard deviation of 0.11578 or 11.6%.

Institutional ownership has a minimum value of 0.33 or 33%, the maximum value of 0.99 or 99%, which means that institutional ownership still dominates the number of shares owned by the company, the average value of 0.7767 or 77.7% and a standard deviation of 0.18397 or 18.4%. Companies that have a minimum value in institutional ownership is PT. Mayora Indah Tbk, and which has a maximum value is PT. Bentoel International Investama Tbk.

Activities of the Board of Commissioners has a minimum value of 1.00 and a maximum of 9.00, which means that the activity or the amount of the meeting at least that one time and at most nine times in one year, the average value of 3.7778, or 3.8%, and a standard deviation of 1.95326.

The proportion of the Audit Committee educational background or financial accounting has a minimum value of 0.20 or 20%, the maximum value of 1.00 or 100%, the average value of 0.5090 or 51%, and the standard deviation of 0.23706 or 23, 7% which indicates that this amount in accordance with established criteria that must be at least one person who has the educational background in accounting or finance the entire amount of the Audit Committee.

Internal control disclosure has a minimum value of 0.50 or 50%, namely PT. Delta Djakarta Tbk and a maximum value of 0.89 or 89%, namely PT. Indofarma (Persero) Tbk and PT. Kalbe Farma Tbk, which indicates that the awareness of the company to disclose internal control information is already quite high, but still need to be improved again so that the survival of the company in the long term can be maintained.

4.1. Hypothesis Test

Before performing regression testing has been performed classical assumption and the results showed that all the assumptions of classical test criteria have been met. Hypothesis testing using multiple linear regression analysis. Testing with multiple linear regression showed Adjusted R^2 values in the model summary of 0.238 or 23.8%. This shows that public ownership, managerial ownership, institutional ownership, Activities Board of Commissioners, and the Audit Committee educational background in accounting and finance 23.8% have influence on the disclosure of internal control, while the remaining 76.2% is explained by other variables outside of research.

Table-2. t-Test Statistics Result

Variabel	Sig.	Unstandardized Coeffisients	Keterangan
KP	,028	,152	signifikan
KM	,002	,223	signifikan
			Continue

KI	,011	,133	signifikan
ADK	,013	,010	signifikan
PKA	,222	,040	tidak signifikan
R^2	,281		
Adjusted R^2	,238		
F	6,565		
Sig	,000		

The test results of public ownership variables on the disclosure of internal control has a significant value of 0.028 and a regression coefficient of 0.152, so it can be interpreted that public ownership has a significant influence on the disclosure of internal control. Positive coefficient indicates that public ownership mengingkat will also improve their internal control disclosure in annual reports. The more shares held by the public or the community, the more knowledgeable of internal control disclosures required by the public to know the real state of the company associated with the achievement of the effectiveness and efficiency of operations, reliability of financial reporting, and compliance with laws and regulations applicable and useful for reduce agency conflicts that arise between the agent and the principal (Akhtaruddin et al, 2009). These results are consistent with the hypothesis of this study, so the first hypothesis can be accepted. The results of this study are consistent with the results of research conducted by Aljifri and Hussainey (2006) and Akhtaruddin et al. (2009).

The test results of managerial ownership variable on the disclosure of internal control has a significance value of 0.002 and a regression coefficient of 0.223 and is positive, so it can be interpreted that managerial ownership has a positive significant effect on the disclosure of internal control. The results obtained in this study is consistent with the hypothesis, then the second hypothesis can be accepted. The greater the number of shares held by the managerial would encourage management do their job well, one of them by revealing the internal control information in its annual report, so that the value of the company is also increasing and greater profits will also be obtained by the management who have a stake in the company (Juhmani, 2013). Adequate internal control disclosure shows that the company has demonstrated achievement in the effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations well and can reduce conflicts between agents with the principal (Deumes, 2004; Saha and Arifuzzaman 2011). These results are consistent with the results of research conducted by Deumes (2004).

The test results of institutional ownership variable on the disclosure of internal control has a significance value of 0.011 and 0.133 for the regression coefficient is positive, so it can be interpreted that institutional ownership has a positive significant effect on the disclosure of internal control. This is consistent with the hypothesis, that the third hypothesis can be accepted. A large number of shares owned by institutions will encourage the management to disclose the required information relating to internal control in the annual report issued by the company. This happens because the institutional shareholders want transparency from companies associated with what is happening in the company as a whole (Ling and Lee, 2012). In other words, to assess a company, institutional shareholders requiring specific information (Lev, 1999), quoted by Nekhili, et al. (2012). The results are consistent with research conducted by Bronson et al. (2006) and Akhtaruddin et al. (2009).

The test results of the activities of the Board of Commissioners on the disclosure of internal control has a significant value of 0.013 and a regression coefficient of 0.010 is positive, so it can be interpreted that the activities of the Board of Commissioners has a positive significant effect on the disclosure of internal control. This is consistent with the hypothesis, the fourth hypothesis can be accepted. Meetings of the Board of Commissioners is a means to discuss and exchange ideas in monitoring and providing input to the Board of Directors, so that the continuity of the company in the long term can be maintained (NCG, 2006). Thus, the more the number of meetings held by the Board of Commissioners, will have an impact on the broad disclosure of internal control which shows that the internal controls in the company has executed well. The results are consistent with research conducted by Gantyowati and Fitria (2012), Ahmad (2012).

The test results of a variable proportion of the Audit Committee educational background in accounting or finance on the disclosure of internal control has a significant value of 0.222 and a regression coefficient of 0.040, so it can be interpreted that the proportion of the Audit Committee educational background in accounting or finance does not have a significant effect on the disclosure of internal control with positive coefficient. Thus, the hypothesis of this study is not in accordance with the results of the study, the fifth hypothesis can not be accepted or rejected.

The proportion of the Audit Committee educational background or financial accounting does not have a significant effect on the disclosure of internal control, as members of the Audit Committee educational background in accounting or finance may not be able to guarantee the control of the company is better because of the formation of the Audit Committee educational background in accounting or based solely on the financial regulations (Khomsiyah, 2005, in Pamudji and Trihartati, 2010). Based on the function, the Audit Committee is a committee of the Board of Commissioners whose job it helps to ensure that the financial statements are presented fairly in accordance with generally accepted accounting principles, internal control structure is implemented, the implementation of internal and external audit conducted in accordance with auditing standards applicable, and follow-up audit findings conducted by management. Thus, it is not enough only ability or competence in the field of accounting or finance is owned by the Audit Committee, but the Audit Committee should have the ability or competence in other areas such as in the field of regulation and legislation, regulation of capital markets, as well as related business processes in order to carry out its functions well (Alijoyo, 2003).

5. Conclusion and Limitation

Based on the test results of multiple linear regression, it is concluded that public ownership, managerial ownership, institutional ownership, and Activities Board of Commissioners has a positive significant effect on the disclosure of internal control. The proportion of the Audit Committee and educational background in accounting or finance does not have a significant effect on the disclosure of internal control.

Limitations of this study are: first, the sample companies studied only from the consumer goods industry companies that are part of the manufacturing industry. The results of the study can not be generalized to other industries listed in the Stock Exchange as a public company. Second, the variables used only public ownership, managerial ownership, institutional ownership, Activities Board of Commissioners, the proportion of the Audit Committee educational background in accounting or finance so that the independent variables only have the effect of 23.8% on the disclosure of internal control, while the rest of 76, 2% is explained by other variables outside of research.

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