Analysis of Determinants of Corporate Governance Rating (Empirical Study of Companies Listed in the CGPI Index Report 2015 – 2020)

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ABSTRACT: The monetary crisis that hit Indonesia in 1998 added to the confidence of economists and company management to implement Good Corporate Governance (GCG) practices in Indonesia. The implementation of good corporate governance is expected to be able to create added value for all interested parties. This study aims to determine the effect of ownership concentration, investment opportunity, leverage, profitability, and firm size on corporate governance rating. Using annual data for the period January 1, 2015 – December 31, 2020, with Panel Data Regression analysis with the Eviews 11 tool. The panel data regression test results show that leverage, profitability, and company size as macroeconomic variables influence corporate governance rating. Meanwhile, Ownership Concentration and Investment Opportunity do not affect corporate governance rating.

KEYWORDS: Ownership Concentration, Investment Opportunity, Leverage, Profitability, Company Size, Corporate Governance Rating

1. INTRODUCTION

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 (CG) aims to create added value for all interested parties (stakeholders). Corporate governance also provides a structure that facilitates the determination of a company's goals, and as a means to determine performance monitoring techniques (Darmawati et al. 2004).

The monetary crisis that hit Indonesia in 1998 added to the confidence of economists and company management to implement Good Corporate Governance (GCG) practices in Indonesia. The implementation of good corporate governance is expected to be able to create added value for all interested parties. Good Corporate Governance (GCG) has been implemented in Indonesia since the Letter of Intent was signed. The factors that can affect the success of Good Corporate Governance (GCG) in each company vary. This is due to the variation in the benefits of control provided and the costs incurred for managers and company shareholders (Gillan et al. 2003:27). These variations include:

1. The concentration of company ownership in a company can affect the implementation of organizational strategy if the company's majority capital comes from shares or other securities so that the company's controlling shareholders can affect the quality of the implementation of corporate governance (GC) in the company through the implementation of the policies they design.
2. High investment opportunities owned by the company,
3. The use of a debt structure or leverage, where the high leverage ratio of the company causes the principal to put pressure on management to improve the company's performance so that the debt ratio decreases

Profitability which is assessing the extent to which the company can generate profits. So that high profitability can increase investor confidence and attract investors

4. Company size is the sum of total assets 2021

2. LITERATUR REVIEW

The grand theory used in this research is the theory which states that the Corporate Governance Perception Index (CGPI) report conducted by The Indonesian Institute for Corporate Governance (IICG) can be considered as information for investors in making

investment decisions, including Agency Theory and Signaling Theory. teori yang digunakan dalam penelitian ini adalah teori yang menyatakan bahwa laporan *Corporate Governance Perception Index* (CGPI) yang dilakukan *The Indonesian Institute for Corporate Governance* (IICG) dapat dianggap sebagai sebuah informasi bagi investor dalam pengambilan keputusan investasi diantaranya *Agency Theory* dan *Signalling Theory*.

2.1 Corporate Governance

Corporate Governance is defined as the structure, system, and process used by the company's organs as an effort to provide added value to the company on an ongoing basis in the long term while taking into account the interests of other stakeholders based on applicable laws and norms (IICG, 2009).

2.2 Corporate Governance Perception Index (CGPI)

The Corporate Governance Perception Index (CGPI) is a form of assessment produced in the form of a rating based on the implementation of GCG in companies in Indonesia. This assessment is carried out through research conducted to assess the implementation of the existing CG concept in a company through continuous improvement and evaluation through benchmarking.

2.3 Ownership Concentration

The concentration of ownership is a model that describes how the order or structure of the stakeholders, in this case, the shareholders or owners (principals) of a company and anyone who has control over all or most of the ownership of the company and wholly or most of the controlling shareholders. on the company's business activities. The majority of ownership concentration is used to test the effect of ownership concentration on the quality of CG implementation (Darmawati, 2006).

2.4 Investment Opportunities

The investment opportunity or Investment Opportunity Set (IOS) is a combination of company assets that have an investment choice in the future with a positive net present value (NPV) which will affect the value of the company (Myers, 1977).

2.5 Leverage

Leverage is a ratio used to show the extent to which the company's assets are financed by debt funds. The greater the leverage number, the more stakeholders are involved in the company's operational activities (Kasmir, 2014).

2.6 Profitability

Profitability is the company's ability to generate profit or profit. Return on Assets (ROA) was used to measure the company's performance and found that companies with better financial management resulted in higher operational performance (Klapper and Love, 2003).

2.7 Company Size

Company size is the size of a company measured using total assets (Klapper and Love, 2002). Total assets are the sum of tangible assets such as current assets and fixed assets in one year. Company size is expressed in total assets owned by the company.

FRAMEWORK
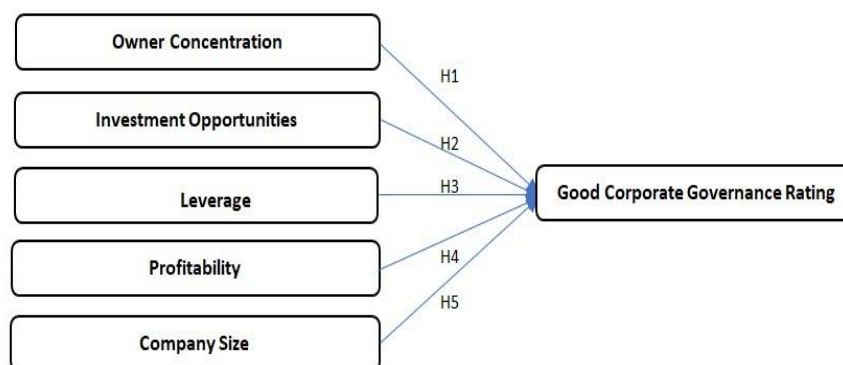
2.7 Research Hypothesis

Positive ownership concentration on corporate governance rating

Large share ownership by certain parties in a company will have several impacts on the quality of the company's corporate governance implementation. Company managers who have a high level of ownership of a company, it is possible to exercise

discretion over company resources will be reduced (Jansen and Meckling, 1976: 56). The amount of ownership owned by the controlling shareholder will result in profitable business policies and principles which in turn can improve the quality of corporate governance implementation (Durnev and Kim, 2003). With this, sometimes the concentration of ownership can increase or even decrease the quality of a company's implementation of corporate governance. Previous research by (Taman & Nugroho, 2016) found that the concentration of ownership influences the implementation of corporate governance.

H1: Concentration of positive ownership on corporate governance rating

Investment opportunities have a positive effect on corporate governance rating

Companies that have high investment opportunities require large external funds to expand, thus encouraging companies to make improvements in the implementation of corporate governance (Durnev and Kim, 2003; Black et al, 2006). Previous research by Setyani (2012) stated that investment opportunities have a positive effect on the implementation of good corporate governance.

H2: Investment opportunities have a positive effect on corporate governance rating.

Leverage has a positive effect on corporate governance rating

The effect of financial leverage on a company on the implementation of corporate governance can be viewed from two perspectives, namely a substitution story and an investor pressure story (Black et. al., 2006: 14). Previous research by Taman and Nugroho (2011) stated that leverage has a significant positive effect on the quality of CG implementation.

H3: Leverage has a positive effect on corporate governance rating.

Profitability has a positive effect on corporate governance rating

The relationship between CG quality and profitability is the main focus of CG learning, but no one can predict it with certainty because the results of previous studies show different results. Klapper and Love (2004) use the rate of Return on Assets (ROA) to measure company performance and found that companies with better financial management produce higher operational performance. Previous research by Irmawatih (2016) found that profitability had a positive and significant effect on CG implementation. With the increasing number of investors, the responsibility of management to continuously improve performance is getting bigger. Management's sense of responsibility toward shareholders can be done by increasing the implementation of GCG. Therefore, the assessment score of the company's GCG implementation is also getting better

H4: Profitability has a positive effect on corporate governance rating.

Company size has a positive effect on corporate governance rating

Larger companies usually have a wider stakeholder role. This causes each company policy will have an impact on the public so management must manage the company well. Klapper and Love (2004) who examined firm size using total sales as a proxy, found that firm size was positively related to the level of CG. Darmawati (2006) also states that company size has a significant positive effect on the quality of CG implementation with the CGPI index as a proxy. In agency theory, it is said that there is information asymmetric between the agent and the principal. With the increasing size of the company, the role of CG practices is increasingly needed to reduce the information gap between agents and principals. In line with this, shareholders carry out stricter supervision of management, resulting in a high CG assessment of the company.

H5: Firm size has a positive effect on corporate governance rating.

3. RESEARCH METHODS

This study uses annual data for the period January 1, 2015, to December 31, 2020, with the corporate governance rating as the independent variable, then the concentration of ownership, investment opportunities, leverage, profitability, and company size as the dependent variable. Thus the number of samples obtained is 42. The approach used is descriptive and inferential which is expected to be able to provide information and draw conclusions to explain the relationship between the independent and dependent variables. The analysis technique used is panel data regression. The panel data regression method will be used when the data has a certain time range with several samples.

The general specification of the Panel Data Regression model is as follows:

$$Y_{it} = a_i + bX_{it} + g_i \Sigma D_i + e_{it}$$

Or in the form of a covariance model can be written:

Information:

$W_{it} = 1$: for the ith individual unit, i = 2 , …, N

$W_{it} = o$: other

$Z_{it} = I$: for time period t, t = 2,… T

$Z_{it} = : o$: other

4. RESEARCH RESULTS AND DISCUSSION

4.1 Panel Data Regression Analysis

Results of the Common-Constant Model Method

This model does not pay attention to the dimensions of time or individuals, so it is assumed that the behavior of the company's data is the same in various periods. This model means to estimate the value which is constant for all dimensions of the cross-section.

Fixed Effect Model Result:

Dependent Variable: Y
Method: Panel Least Squares
Date: 07/20/22   Time: 20:07
Sample: 2015 2020
Periods included: 6
Cross-sections included: 7
Total panel (balanced) observations: 42

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	59.45316	10.90964	5.449599	0.0000
X1	-0.021564	0.067695	-0.318556	0.7519
X2	7.649074	5.406258	1.414855	0.1657
X3	-0.117681	0.078476	-1.499588	0.1424
X4	-0.285567	0.299944	-0.952070	0.3474
X5	1.704753	0.304719	5.594504	0.0000

R-squared	0.835200	Mean depend ent var	87.04119	
Adjusted R-squared	0.812312	S.D. dependent var	5.120111	
S.E. of regression	2.218187	Akaike info criterion	4.562821	
Sum squared resid	177.1327	Schwarz criterion	4.811060	
Log likelihood	-89.81924	Hannan-Quinn criter.	4.653810	
F-statistic	36.48942	Durbin-Watson stat	0.324923	
Prob(F-statistic)	0.000000			

Source: E-views 10 (by the researcher)

To estimate this model can use regression with dummy variables where each individual will be a dummy variable. By making each a dummy variable, there will be one as a basis for comparison to avoid the dummy variable trap.

Random Effect Model Results

Dependent Variable: Y
Method: Panel EGLS (Cross-section random effects)
Date: 07/20/22   Time: 20:28
Sample: 2015 2020
Periods included: 6
Cross-sections included: 7
Total panel (balanced) observations: 42
Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	56.74157	5.596237	10.13924	0.0000
X1	-0.023683	0.035755	-0.662360	0.5120
X2	5.819693	2.614378	2.226034	0.0324
X3	-0.100491	0.039015	-2.575739	0.0143
X4	-0.031807	0.150918	-0.210759	0.8343
X5	1.850161	0.163428	11.32094	0.0000

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Effects Specification			
		S.D.	Rho
Cross-section random		0.408732	0.1333
Idiosyncratic random		1.042422	0.8667
Weighted Statistics			
R-squared	0.794945	Mean depend ent var	62.77658
Adjusted R-squared	0.766466	S.D. dependent var	3.891640
S.E. of regression	1.880650	Sum squared resid	127.3264
F-statistic	27.91261	Durbin-Watson stat	0.351291
Prob(F-statistic)	0.000000		
Unweighted Statistics			
R-squared	0.830317	Mean dependent var	87.04119
Sum squared resid	182.3812	Durbin-Watson stat	0.245248

Source: E-views 10 (by the researcher)

The Random Effect Model estimates panel data in which residual variables are thought to have a relationship between time and between subjects. Panel data analysis method with Random effect Model must meet the requirements, namely, the number of cross sections must be greater than the number of research variables.

4.2 Panel Data Regression Model Selection

Chow Test Results

Redundant Fixed Effects Tests
Equation: Untitled
Test cross-section fixed effects

Effects Test	Statistic	d.f.	Prob.
Cross-section F	22.168191	(6,30)	0.0000
Cross-section Chi-square	71.089575	6	0.0000

Source: E-views 11 (by the researcher)

From the results of the Chow Test, it can be seen that the probability value of F is 0.0000 less than the value of (0.05), so it can be determined that the correct estimation model is used, namely the Fixed Effect Model, which means H0 is rejected and H1 is accepted.

Hausman Test Results

Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	86.174124	5	0.0000

Cross-section random effects test comp arisons:				
Variable	Fixed	Random	Var(Diff.)	Prob.
X1	0.149216	-0.023683	0.019598	0.2168
X2	4.771142	5.819693	0.898680	0.2687
X3	-0.200665	-0.100491	0.000801	0.0004
X4	0.360059	-0.031807	0.006961	0.0000
X5	4.979625	1.850161	0.427361	0.0000

Source: E-views 11 (by the researcher)

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From the Hausman Test results, it can be seen that the probability value of a random cross-section of 0.0000 is smaller than the value of (0.05), it can be determined that the correct estimation model is used, namely the Fixed Effect Model, which means H0 is rejected and H1 is accepted.

Lagrange Multiplier Test Results

Lagrange Multiplier Tests for Random Effects

Null hypotheses: No effects

Alternative hypotheses: Two-sided (Breusch-Pagan) and one-sided

(all others) alternatives

	Test Hypothesis		
	Cross-section	Time	Both
Breusch-Pagan	20.30768	4.922894	25.23057
	(0.0000)	(0.0265)	(0.0000)
Honda	4.506404	2.218759	4.755409
	(0.0000)	(0.0133)	(0.0000)
King-Wu	4.506404	2.218759	4.676880
	(0.0000)	(0.0133)	(0.0000)
Standardized Honda	7.203585	2.463153	3.366225
	(0.0000)	(0.0069)	(0.0004)
Standardized King-Wu	7.203585	2.463153	3.208846
	(0.0000)	(0.0069)	(0.0007)
Gourieroux, et al.	--	--	25.23057
			(0.0000)

Source: E-views 11 (by the researcher)

From the output above, it can be seen that the Breusch-Pagan (Both) probability value of 25.23057 is greater than 0.05, so the correct estimation model is used, namely the common effect model, then H0 is accepted and H1 is rejected.

4.3. Goodness of Fit Test

In this study, the most appropriate estimation model is the Fixed Effect Model. After the selection of the Fixed Effect Model, a goodness of fit test will be carried out to know the results of the F statistic test and the coefficient of determination (R^2) test.

F. Test Results

Dependent Variable: Y

Method: Panel Least Squares

Date: 07/20/22   Time: 20:15

Sample: 2015 2020

Periods included: 6

Cross-sections included: 7

Total panel (balanced) observations: 42

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-3.833985	18.17364	-0.210964	0.8343
X1	0.149216	0.144488	1.032726	0.3100
X2	4.771142	2.780944	1.715655	0.0965
X3	-0.200665	0.048197	-4.163469	0.0002
X4	0.360059	0.172446	2.087959	0.0454
X5	4.979625	0.673847	7.389849	0.0000
	Effects Speci fication			
Cross-section fixed (dum my variables)				

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R-squared	0.969670	Mean depend ent var	87.04119
Adjusted R-squared	0.958550	S.D. dependent var	5.120111
S.E. of regression	1.042422	Akaike info criterion	3.155927
Sum squared resid	32.59929	Schwarz criterion	3.652404
Log likelihood	-54.27446	Hannan-Quinn criter.	3.337905
F-statistic	87.19412	Durbin-Watson stat	1.236387
Prob(F-statistic)	0.000000		

Source: E-views 11 (by the researcher)

Based on the results of the F test calculation above, the calculated F value > F table is 87,19412 > 2,364, then H0 is rejected which means that the variables of ownership concentration, investment opportunities, leverage, profitability, and company size together affect the corporate governance rating in 2015 - 2020.

Coefficient of Determination Test Results R^2

Cross-section fixed (dummy variables)

R-squared	0.969670	Mean dependent var	87.04119
Adjusted R-squared	0.958550	S.D. dependent var	5.120111
S.E. of regression	1.042422	Akaike info criterion	3.155927
Sum squared resid	32.59929	Schwarz criterion	3.652404
Log likelihood	-54.27446	Hannan-Quinn criter.	3.337905
F-statistic	87.19412	Durbin-Watson stat	1.236387
Prob(F-statistic)	0.000000		

Source: E-views 11 (by the researcher)

From the table above, the Adjusted R-squared value is 0.9585 or 95.85%, which means that 95.85% of the CGPI rating is influenced by the variables of ownership concentration, investment opportunities, leverage, profitability, and company size, while the rest is 4 .15% (1 – 95.85%) is influenced by other variables not included in this study.

Hypothesis Test Results (t-test)

Dependent Variable: Y
Method: Panel Least Squares
Date: 07/20/22   Time: 20:15
Sample: 2015 2020
Periods included: 6
Cross-sections included: 7
Total panel (balanced) observations: 42

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-3.833985	18.17364	-0.210964	0.8343
X1	0.149216	0.144488	1.032726	0.3100
X2	4.771142	2.780944	1.715655	0.0965
X3	-0.200665	0.048197	-4.163469	0.0002
X4	0.360059	0.172446	2.087959	0.0454
X5	4.979625	0.673847	7.389849	0.0000
	Effects Speci fication			
Cross-section fixed (dum my variables)				
R-squared	0.969670	Mean depend ent var		87.04119
Adjusted R-squared	0.958550	S.D. dependent var		5.120111
S.E. of regression	1.042422	Akaike info criterion		3.155927
Sum squared resid	32.59929	Schwarz criterion		3.652404

Log likelihood	-54.27446	Hannan-Quinn criter.	3.337905
F-statistic	87.19412	Durbin-Watson stat	1.236387
Prob(F-statistic)	0.000000		

Source: E-views 11 (by the researcher)

From testing the hypothesis, the following results were obtained:

1) Ownership concentration (X1) has a probability value of 0.3100 > 0.05, so H0 is accepted, which means that ownership concentration does not affect corporate governance rating.
2) Investment Opportunity (X2) has a probability value of 0.0965 > 0.05, then H0 is accepted, which means that investment opportunities do not affect the corporate governance rating.
3) Leverage (X3) has a probability value of 0.0002 < 0.05, so H0 is rejected, which means that leverage affects corporate governance rating.
4) Profitability (X4) has a probability value of 0.0454 <0.05, then H0 is rejected, which means that profitability affects corporate governance rating.
5) Company size (X5) has a probability value of 0.0000 <0.05, then H0 is rejected, which means that firm size affects the corporate governance rating.

4.4 Panel Data Regression Analysis Results
Panel Data Regression Equation
From testing the panel data regression model above using the Fixed Effect model, a panel data regression equation model is formed which can be formulated as follows:

$$Y = -3.8339 + 0.1492X1 + 4.7711X2 + -0.2006X3 + 0.3600X4 + 4.9796X5$$

The panel data regression equation above can be concluded:

1) The constant coefficient value is = -3.8339 which means that if the variables OWN (X1), MVBVA (X2), LEV (X3), PRO (X4), and SIZE (X5) is zero, then the value of CGPI Rating (Y) of -3.8339.
2) The regression coefficient value of the Ownership Concentration (OWN) variable on the CGPI rating is significantly 0.3100 > 0.05. This means that the Corporate Governance Perception Index rating does not affect the Ownership Concentration (OWN) variable.
3) The regression coefficient value of the Investment Opportunity variable (MVBVA) on the CGPI rating is significantly 0.0965 > 0.05. This means that MVBVA does not affect the CGPI rating.
4) The value of the regression coefficient of the Leverage variable (LEV) on the CGPI rating is significantly 0.0002 < 0.05. This means that leverage has a significant effect on the CGPI rating.
5) The regression coefficient value of the Profitability variable (PRO) on the CGPI rating with a significant 0.0454 <0.05. This means that profitability has a significant effect on the CGPI rating.
6) The regression coefficient value of the Firm Size (SIZE) variable on the CGPI rating with a significance of 0.0000 <0.05. This means that the size of the company has a significant effect on the CGPI rating.

4.5 Discussion
Ownership Concentration does not affect Corporate Governance Rating
The results of the panel data regression test show that the concentration of ownership does not affect the corporate governance rating variable, meaning that if there is an increase in the OWN variable (X1) by 1 unit, the CGPI Rating variable (Y) will increase by 0.1492 units.

The results of this study are not the same as the initial hypothesis and theory which states that ownership concentration has a positive effect on the Corporate Governance Perception Index (CGPI) rating, namely the higher the concentration of ownership, the more likely there is an agency conflict between shareholders so that there will be demands to implement better corporate governance. . The results of this study are also consistent or in line with the research of Irmawatih (2016), and accordance with the research of Tjandra and Suryathi (2017).

The more concentrated share ownership, causes majority shareholders to tend not to pay attention to the interests of minority shareholders, and the existing regulations, many policies are carried out only for their interests. So the concentration of share ownership tends to ignore the quality of the implementation of corporate governance and the low CGPI rating.

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Investment Opportunity does not affect Corporate Governance Rating

The results of the panel data regression test show that investment opportunities do not affect the corporate governance rating variable, which means that if there is an increase in the MVBVA variable (X2) by 1 unit, the CGPI Rating variable (Y) will increase by 4.7711 units.

The results of this study are consistent with the research of Hormati (2009) and Sopiani (2020), which found that investment opportunities did not affect the implementation of GCG. Companies that use internal funding, these companies tend to ignore corporate governance because investment funding has been fulfilled without having to improve the quality of corporate governance so the implementation of the quality of corporate governance practices is low and the CGPI rating decreases.

Leverage affects Corporate Governance Rating

The results of the panel data regression test show that leverage has an influence on Corporate Governance Rating, which means that if there is a decrease in the LEV variable (X3) by 1 unit, the CGPI Rating variable (Y) will decrease by -0.2006 units.

Companies with high levels of leverage tend to apply good corporate governance properly to obtain a better reputation. Cho and Kim (2003) suggest that a high level of leverage ratio management will come under pressure from the lenders so it is necessary to implement good corporate governance and a CGPI rating level with a very reliable predicate. This opinion is evidenced by the research of Tjandra and Suryathi (2017), and the research of Sopiani (2020), with the results that there is a positive influence between corporate leverage on the implementation of GCG.

Profitability affects Corporate Governance Rating

The results of the panel data regression test show that profitability influences Corporate Governance Rating, meaning that if there is an increase in the PRO variable (X4) by 1 unit, the CGPI Rating variable (Y) will increase by 0.3600 units. This is by the hypothesis statement made earlier.

High profitability is a reflection of a company with a commitment to good corporate governance because the company can improve its performance and have an impact on better credibility so that it will increase the weight of the CGPI assessment. This is by the hypothesis statement made previously and in line with the research of Irmawatih (2016) and Tjandra & Suryathi (2017) which state that profitability has a significant influence on GCG implementation.

Company Size affects Corporate Governance Rating

The results of the panel data regression test show that the size of the company influences the Corporate Governance Rating, meaning that if there is an increase in the SIZE variable (X5) by 1 unit, the CGPI Rating variable (Y) will increase by 4.9796 units.

These results indicate that the larger the size of the company, the more it will affect the rating of the Corporate Governance Perception Index (CGPI). Because large companies tend to attract public attention, it will encourage company management to implement better GCG and will affect the increase in the weight of the CGPI rating score. The results of this study are consistent with research conducted by Setyani (2012) and Chandra & Yusbardini (2020) which found that company size affects companies in implementing good corporate governance.

5. CONCLUSIONS AND SUGGESTIONS

5.1 Conclusion

The Panel Data Regression Model in this study shows that leverage, profitability, and firm size as macroeconomic variables influence corporate governance rating. Meanwhile, Ownership Concentration and Investment Opportunity do not affect corporate governance rating.
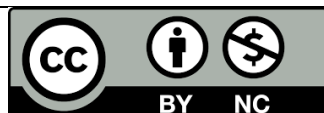
5.2 Suggestions

Based on the results of previous research and research, some suggestions can be considered to improve further research:

1. Investors / potential investors in making investment decisions can consider fundamental analysis, such as leverage ratios, profitability ratios, and company size in assessing company performance. Companies with a high level of leverage tend to implement good corporate governance properly and correctly.

2. The Financial Services Authority (OJK) should pay attention to and encourage the implementation of good corporate governance (GCG) in companies in Indonesia, where the implementation of GCG in Indonesia is currently relatively lagging behind other countries in the ASEAN region.

3. Further researchers are advised to conduct research not only on companies that are included in the CGPI rating so that the The results obtained can reflect the actual situation in the capital market and obtain a more optimal sample of companies.

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