

**THE INFLUENCE OF BOARD OF COMMISSIONERS AND
AUDIT COMMITTEE EFFECTIVENESS ON INSTITUTIONAL
INVESTORS INTEREST IN FAMILY FIRMS**

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ABSTRACT

The objective of this research is to analyze how the board of commissioners and audit committee effectiveness as the mechanisms for corporate governance, influence the institutional investor's interest in such firms. Furthermore, this study examines whether the family ownership would influence those associations. Board of commissioners and audit committee effectiveness are measured using a score developed by Hermawan (2009). Hypothesis testing is carried out using logistic regression models with 643 observations (firm-year) from companies listed in Indonesia Stock Exchange during the period of 2009 to 2011. The empirical result finds that institutional investors are more probable to have an interest to invest in companies with more effective board of commissioners and audit committee. However, family ownership appears to weaken the influence of the board of commissioners effectiveness, but also strengthen the influence of audit committee effectiveness.

Keywords: board of commissioners effectiveness, audit committee effectiveness, family ownership, institutional investor.

1. BACKGROUND

A key element in the development of modern financial market is the interaction between companies which are looking for financing and the existence of institutional investors which are allocating their managed funds. The potential growth of the funds managed by institutional investors is increasing. These funds come from worldwide individual investors who settle on mutual funds, pension funds, and other investment products offered by banks, investment banks, and insurance companies, as their major investment tools (Koh, 2003). Companies, on the other hand, begin to find alternative financing sources to reduce their dependence on traditional financing system such as bonds issuance or bank loans (Tappeiner et al., 2012).

La Porta et al. (1998) state that investors are willing to pay more for financial assets if they are convinced their rights will be properly protected. In the event that managers act on their own interests, shareholders or investors may rely on the legal system to guarantee their rights for proper return rate. The legal approach applied to corporate governance mechanism could be the key to inhibit expropriation, or frauds, committed by controlling shareholders and minimize the possibility of damage caused over the functions and finances of the companies concerned. This mechanism could originate from the companies internally, capital market regulatory authorities, bankruptcy regulations and other related regulations such as in market competition.

Indonesia adopts two-tier management system, which completely separate the supervisory function from the executive function. Therefore, the governance structure consists of board of commissioners which perform the supervisory function similar to the board of directors in other countries. Audit committee is also a mandatory committee under the board of commissioners which has the specific responsibilities related to the supervision of company's financial reporting, regulatory compliance, and risk management. Good corporate governance is influenced by how effective the board of commissioners and audit committee perform their duties. Hermawan (2009) develops an effectiveness score for board of commissioners and audit committee based on characteristics which are confirmed to influence their performance in previous studies, i.e. independence, activity, size, and competence. The higher the score represent the more effective board and audit committee in the company, and therefore the better corporate governance.

Ownership structure has an important influence in corporate governance implementation (Shleifer and Vishny, 1997). Majority shareholders in public companies in the South East Asia are generally families with concentrated ownership above 50% (Claessens et al., 2000). Family firms have unique traits. Among others is the domination of company founders in the management, which could weaken the implementation of corporate governance that requires the presence of independent board of commissioners. The objective of appointing independent members of the board becomes limited to comply with the regulation requirements, rather than to improve the company's general performance (Siregar and Utama, 2008). In addition, the elected members of the board of directors are not entirely independent as many

are based on acquaintanceships or business partnerships with company owners (Garcia-Ramos and Garcia-Olalla, 2011).

An effective monitoring by corporate governance structure may increase the interest of institutional investors to invest. The contribution of this study is to give an empirical result whether the effectiveness of board of commissioners and audit committee influence the institutional investors interest to invest. In addition, this study also examines how family ownership influences such association.

2. LITERATURE REVIEW

Agency problem occurs as the result of the delegation of company's management and supervisory function to professionals, which in turn creates segregation between company ownership and control (Fama and Jensen, 1983). The company's shareholders are defined as "principal" and the company's management is defined as "agent". The problems arise by this arrangement is that decisions made by agent are not always representing the principal's best interest which is to maximize shareholders' wealth. According to Jensen and Meckling (1976), the interests of managers and shareholders would be congruent if managers have relatively significant shares ownership. Bennedson and Wolfenzon (2000) argue that segregation scenario would not take place given that company's ownership is evenly spread and decision-making is based on votes.

Corporate governance is a system, process, and procedures that specifically attempt to regulate the relationship between managers and shareholders, as well as with the company's stakeholders at large. OECD Principles (2004) contributed to this definition, adding the emphasis on the need to involve the government to establish regulations, institutions, and rules, which companies are responsible to implement.

Hermalin and Weisbach (2003) state that the preference of institutional investors on the composition of the board of directors is a form of corporate governance internal mechanism in order to monitor the management's overall performance. Hemphill (2007) favors this statement, with SEC approving shareholders to propose candidates as members of board of directors. Meanwhile, audit committee is a committee formed under the board of commissioners (KNKG, 2006), with a highly essential role in the implementation of corporate governance. Audit committee is directly responsible to monitor company's financial reporting (Xie et al., 2003; Hoitash et al., 2009) as well as ensuring the rights of investors by overseeing company's internal control, financial reporting, risk assessment, audit activities and compliance to relevant laws and regulations.

Family firm is defined as company that is owned and controlled, whether directly or indirectly, by individuals with familial relationships (Sugiarto, 2009). Mroczkowski and Tanewski (2007) use a set of criteria to define family firm, among others are the involvement of founder(s) or his/her heir(s) in company's management as president director; or as director with more than 20% shares ownership with voting right. Also

included in the criteria is above 50% shares ownership with voting right by company's founding shareholder(s). This research adopts the definition of "family firm" as defined by La Porta et al. (1999), whose criteria includes ownership by domestic and foreign companies that are not public companies, banks, investment banks, pension funds, insurance and foundations; and individual ownership of above 5%.

Other factors influencing the interest of institutional investors among others refer to a research by Wahab et al. (2007) regarding the impact of corporate governance on company's performance and institutional investors' interest. Their research concludes that company's size, performance, growth opportunity, and leverage would affect the interest of institutional investors. Such factors are also identified in the research of Bushee and Noe (2000), Hamdani and Yafeh (2011).

3. HYPOTHESIS DEVELOPMENT

Research on corporate governance and the interest of institutional investors has often been carried out. A number of these researches have formed the basis of this research, such as the research of Bushee et al. (2010), which concludes that institutional investors prefer to invest in companies with corporate governance mechanism in place. In this research, Bushee et al. (2010) states that independent board of commissioners is effective in exerting supervisory function on company's management, thus hindering institutional investors from hiring external supervisors and augment company's costs. Based on the findings, this research proposes the following hypothesis:

H1a: Higher board of commissioners' effectiveness score increases the probability of institutional investor's interest in the firm.

A study conducted by Lin et al. (2009) on the relationship between audit committee and institutional investors find that frequency of audit committee meetings has positive impact on the quality of company's financial reporting. According to Bushee and Noe (2000), institutional investors with major share portfolio would prefer adequate disclosure report to balance the supervisory costs. Both studies conclude that corporate governance mechanism through the effectiveness of audit committee has positive influence on the probability of interest from institutional investors. Based on the findings, this research proposes the following hypothesis:

H2a: Higher audit committee's effectiveness score increases the probability of institutional investor's interest in the firm.

Research conducted by Siagian (2011) on the structure of ownership and corporate governance on Indonesian companies finds that family firms with a high ownership concentration implement lower corporate governance mechanism, with the aim of maintaining family control over their companies. This finding is consistent with a research carried out by Wong (2012), which states that family-owned companies have fewer independent members in the audit committee, as well as fewer members of the

committee with accounting and financial expertise. Although indirectly, the control exercised by owners may lead to ineffective implementation of supervisory duties over company's management by the board of commissioners and audit committee.

H3a: Family ownership weakens the influence of board of commissioners' effectiveness on the probability of institutional investor's interest in the firm.

H4a: Family ownership weakens the influence of audit committee's effectiveness on the probability of institutional investor's interest in the firm.

4. DATA AND METHODOLOGY

The population used in this research consists of non-financial companies listed in the Indonesian Stock Exchange from the period of 2009 to 2011. Based on sample selection criterion, 643 observations are qualified for the period of 2009 to 2011. In details, this research observes 189 companies from 2009 period, 219 companies from 2010 period and 235 companies from 2011 period.

As presented in Table 1, this research utilizes more samples from trade, service and investment industries, amounting to 26 % of the total sample in 2009, 28% in 2010 and 27% in 2011. The second industry group is base and chemical industries amounting to 16% in 2009, 16% in 2010 and 14% in 2011. Lastly, property, real estate and construction industries account for 14% in 2009, 13% in 2010 and 13% in 2011.

Table 1. Distribution of Sample Companies based on Industry

| No. | Industry | Percentage | | |
|-----|--|------------|------|------|
| | | 2009 | 2010 | 2011 |
| 1 | Trade, Service and Investment | 26% | 28% | 27% |
| 2 | Base and Chemical Industry | 16% | 16% | 14% |
| 3 | Property, Real Estate and Construction | 14% | 13% | 13% |
| 4 | Consumption Goods Industry | 10% | 11% | 11% |
| 5 | Various Industry | 10% | 10% | 11% |
| 6 | Infrastructure, Utility and Transportation | 9% | 9% | 9% |
| 7 | Mining | 9% | 9% | 9% |
| 8 | Agriculture | 6% | 5% | 6% |
| | Total | 100% | 100% | 100% |

To examine the proposed hypotheses, this research uses logistic regression analysis to assess the influence of the Board of Commissioners and Audit Committee effectiveness score on the probability of institutional investor's interest in the firms. The research model also uses control variables such as company size, accounting performance, growth opportunities, leverage, and business risks. This research also includes family ownership as a moderating variable, because family ownership

presumes to lower the effectiveness of the board of commissioners and audit committee.

Hypothesis testing is carried out using two models. Hypotheses 1 and 2 are tested by using the following model:

$$\text{Logit (INS}_{it}) = \text{Ln} \frac{\text{INS}_{it}}{1-\text{INS}_{it}} = \beta_0 + \beta_1.\text{BSCORE}_{it} + \beta_2.\text{ASCORE}_{it} + \beta_3.\text{FSIZE}_{it} + \beta_4.\text{ROA}_{it} + \beta_5.\text{GRWOPT}_{it} + \beta_6.\text{LEV}_{it} + \beta_7.\text{RISK}_{it} + \varepsilon_{it} \quad (3.1)$$

Hypotheses 3 and 4 are tested by using the following model:

$$\text{Logit (INS}_{it}) = \text{Ln} \frac{\text{INS}_{it}}{1-\text{INS}_{it}} = \beta_0 + \beta_1.\text{BSCORE}_{it} + \beta_2.\text{ASCORE}_{it} + \beta_3.\text{DFAM}_{it} + \beta_4.\text{BSCORE}_{it} * \text{DFAM}_{it} + \beta_5.\text{ASCORE}_{it} * \text{DFAM}_{it} + \beta_6.\text{FSIZE}_{it} + \beta_7.\text{ROA}_{it} + \beta_8.\text{GRWOPT}_{it} + \beta_9.\text{LEV}_{it} + \beta_{10}.\text{RISK}_{it} + \varepsilon_{it} \quad (3.2)$$

Where:

$\text{Ln} \frac{\text{INS}_{it}}{1-\text{INS}_{it}}$ = Dummy variable, with the value of 1 (one) if the company i has institutional investors as its shareholders at year t and the value of 0 (zero) if otherwise

BSCORE_{it} = Board of commissioners effectiveness score of company i at year t

ASCORE_{it} = Audit committee effectiveness score of company i at year t

DFAM_{it} = Dummy variable, with the value of 1 (one) if the the family shareholdings in company i is above 50% from total shareholders, and 0 (zero) if otherwise

FSIZE_{it} = Size of company i and year t measured based on natural logarithm of the company i total assets at the end of year t

ROA_{it} = Return on Assets of company i at year t

GRWOPT_{it} = Potential growth of company i which measured based on PBV (Price to Book Value) at the end of year t.

LEV_{it} = Ratio of total debt to total equity of company i at year t

RISK_{it} = Risk of company i at year t measured with beta

Scoring method in determining effectiveness of board of commissioners and audit committees are based on checklist developed by Hermawan (2009). There are 17 questions in the checklist for effectiveness of the board of commissioners which are grouped into four categories based on the characteristics of the board of commissioners such as independence of the board, activities of the board, size of the board, and board member's competency. Checklist for scoring effectiveness of audit committees have 11 questions grouped into 3 categories based on their characteristics, such as audit committee activities, size of audit committee and audit committee member's competency. Scores for each question are based on information given in

company financial report. It is rated in good, fair and poor, which is then translated in the form of numbers, a score of 3 for good, 2 for fair and 1 for poor. The final score for each company is by summing up the score of all questions.

5. DESCRIPTIVE STATISTICS

Descriptive statistics is associated with data collecting and ranking, which describe sample characteristics used in the research.

INS variable represents institutional investor's interest in companies, while DFAM variable represents family ownership. On average, companies with institutional investors' interest account for 34%, while companies with family ownership account for 45%. Based on deviation standard, family firms are more extensively distributed with 49.80%, compared to the distribution of companies with interest from institutional investors. These results show higher proportion of family ownership compared to institutional investors' ownership in sample companies.

Table 2. Descriptive Statistics of Research Variables

| | <i>Minimum</i> | <i>Maximum</i> | <i>Mean</i> | <i>Std. Deviation</i> |
|------------------------|----------------|----------------|-------------|-----------------------|
| INS | 0.0000 | 1.0000 | 0.0340 | 0.4750 |
| BSCORE | 0.3500 | 1.0000 | 0.6356 | 0.1043 |
| ASCORE | 0.3300 | 1.0000 | 0.6803 | 0.1587 |
| DFAM | 0.0000 | 1.0000 | 0.4500 | 0.4980 |
| FSIZE (In million Rp.) | 14.481 | 47,275.955 | 5,381.532 | 9,309.410 |
| ROA | -0.6200 | 4.8600 | 0.1213 | 0.2836 |
| GRWOPT | 0.0700 | 14.6400 | 2.2402 | 4.4091 |
| LEV | 0.0000 | 5.8800 | 1.2391 | 1.2036 |
| RISK | -4.0700 | 8.8500 | 0.7397 | 0.5516 |

BSCORE variable represents effectiveness score of the board of commissioners, while ASCORE represents effectiveness score of audit committee. The board of commissioners effectiveness score has the smallest sample with the value of 0.35; meanwhile, the biggest sample has a value of 1. This variable average worth 63.56%, which suggests that based on evaluation criteria the overall effectiveness score of the board of commissioners is acceptable. Meanwhile, deviation standard is 10.43%, which suggests narrow distribution of the board of commissioners' score, or narrow comparative score of the board of commissioners' effectiveness between companies. In terms of audit committee effectiveness, the lowest score sample is 0.33 and the

highest score is 33. Audit committee's average effectiveness score is 68.03%, which suggests that on average the companies have applied acceptable level of audit committee effectiveness. The deviation standard of audit committee effectiveness score is 15.87%, which indicates that overall distribution is not too widely spread.

The controlling variable includes the FSIZE variable that represents the size of companies based on proxy log of natural total asset. The companies show average score of 14.2841, which suggests that the companies on average have total assets of Rp5.381 trillion, with deviation standard of 1.6018, or equals to Rp9.309 trillion. ROA variable represents companies' performance, which is measured by dividing net income with total asset. The average score for ROA variable is 0.12, indicating that the companies on average generate return rate of 12% from the total asset used. GRWOPT variable represents the companies' growth opportunity based on PBV (price to book value) ratio, which is derived from the calculation of market price per share divided with the equity book value per share. The average GRWOPT score in this research is 2.24, indicating that the sample companies on average have market price per share 2.24 times higher than the equity book value. LEV variable, or *leverage*, measures the debt level applied by the companies. The average LEV value is 1.23, with a maximum value of 5.88. This indicates that the companies have long-term debts amounting to 5.88 times of their equity value. Lastly, risk variable RISK is measured using companies' beta value. Maximum value of 8.85 describes how some companies have high movement following market returns, while minimum value of -4.07 indicates that several companies are moving in contrary to market movements.

Omnibus Tests of Model Coefficients conducts simultaneous tests on all coefficient variables in a logistic regression. The Chi-square value represents the difference of -2LL model, measuring only constant value and model. The value of Chi-square model is a significant value of 196.935 with degrees of freedom $df = 7$. *P-value* = 0.000 is lower than $\alpha = 0.05$ (sig. 0.000 < 0.05), thus concludes that test result is significant. As such, H_0 is nullified, while other independent variables of BSCORE, ASCORE, FSIZE, ROA, GRWOPT, LEV and RISK are influencing the interest of institutional investors with significance level of 1%, 5%, or 10%.

6. RESULTS

The result of logistic regression Table 3-Model 1 is used to examine hypotheses 1a and 2a, while the result of Table 3-Model 2 is used to examine hypotheses 3a and 4a.

Table 3. Regression Result

Regression model 1.

$$\ln \frac{INS_{it}}{1-INS_{it}} = \beta_0 + \beta_1.BSCORE_{it} + \beta_2.ASCORE_{it} + \beta_3.FSIZE_{it} + \beta_4.ROA_{it} + \beta_5.GRWOPT_{it} + \beta_6.LEV_{it} + \beta_7.RISK_{it} + \varepsilon_{it}$$

Regression model 2

$$\ln \frac{INS_{it}}{1-INS_{it}} = \beta_0 + \beta_1.BSCORE_{it} + \beta_2.ASCORE_{it} + \beta_3.DFAM_{it} + \beta_4.BSCORE_{it} * DFAM_{it} + \beta_5.ASCORE_{it} * DFAM_{it} + \beta_6.FSIZE_{it} + \beta_7.ROA_{it} + \beta_8.GRWOPT_{it} + \beta_9.LEV_{it} + \beta_{10}.RISK_{it} + \varepsilon_{it}$$

| Variable | Expected Sign | Model 1 | | | Model 2 | | |
|----------------------|---------------|---------|----------|--------|---------|----------|---------------------|
| | | B | Sig | Exp(B) | B | Sig | Exp(B) |
| BSCORE | + | 3.981 | 0.001*** | 53.575 | 3.001 | 0.017** | 20.103 |
| ASCORE | + | 1.271 | 0.050** | 3.564 | -9.022 | 0.032** | 0.000 |
| DFAM | - | | | | -12.206 | 0.001*** | 0.000 |
| DFAM* BSCORE | - | | | | -4.743 | 0.001*** | 0.009 |
| DFAM* ASCORE | - | | | | 22.250 | 0.000*** | 4.6x10 ⁹ |
| FSIZE | + | 0.539 | 0.000*** | 1.714 | 0.510 | 0.000*** | 1.666 |
| ROA | + | 3.390 | 0.000*** | 29.656 | 3.076 | 0.001*** | 21.670 |
| GRWOPT | + | 0.009 | 0.419 | 1.009 | 0.019 | 0.343 | 1.019 |
| LEV | - | -0.110 | 0.117 | 0.896 | -0.114 | 0.118 | 0.892 |
| RISK | -/+ | 0.261 | 0.072* | 1.298 | 0.231 | 0.096* | 1.260 |
| Constant | | -12.463 | 0.000*** | 0.000 | -4.315 | 0.006*** | 0.013 |
| Omnibus Test | | 196.935 | 0.000*** | | | 215.929 | 0.000*** |
| Cox & Snell R Square | | 0.264 | | | | 0.285 | |
| Nagelkerke R Square | | 0.365 | | | | 0.394 | |

***significant at level $\alpha=1\%$

**significant at level $\alpha=5\%$

*significant at level $\alpha=10\%$

Number of observation: 643

BSCORE = Board of Commissioners effectiveness score, ASCORE = Audit Committee effectiveness score, DFAM = dummy variabls, with the value of 1 if company is owned by family > 50% and 0 if otherwise, FSIZE = size of company measured as the natural logarithm of total assets, ROA = profitability measured by the ratio of income to total assets, GRWOPT = growth opportunity measured by the ratio of price to book value, and RISK = the company risk measured by beta.

Based on the logistic regression analysis result of Table 3, the BSCORE variable that represents the board of commissioners' effectiveness score has *B* positive logistic coefficient value of 3.981, with significance level of 0.001 at $\alpha = 1\%$ (significant). The above result suggests that the effectiveness score of the board of commissioners has significant positive impact on the interest probability of institutional investors in companies. Higher score of the board of commissioners' effectiveness generate higher probability for companies to acquire interest of institutional investors.

This verifies hypothesis 1a that the effectiveness score of the board of commissioners has positive impact on the probability of institutional investor's interest in the company. Financial or accounting competencies of the board of directors influence the quality of financial reporting, by ensuring good performance of audit committee (Adam and Ferreira, 2008). As conveyed in a survey result of an international renowned consulting company McKinsey (2002), 71% institutional investors consider disclosure quality as the key factor in investment decision-making. The survey also reveals that members of the board with financial and accounting expertise are able to allocate more time performing advisory function rather than monitoring.

Hypothesis 2a examines the relationship between effectiveness of audit committee and interest probability of institutional investors. As presented by logistic regression result in Table 3, ASCOR variable has a logistic coefficient value of B positive amounting to 1.271 with a significance level of $\alpha = 5\%$. The result suggests that high effectiveness score of audit committee generates higher interest probability from institutional investors. Hypothesis 2a, which states that audit committee's effectiveness score has positive influence on the interest probability from institutional investors, is thus accepted.

The results presented in this research affirmed a research conducted by Lin et al. (2009) regarding the role of audit committee and preference of institutional investors, which observe companies listed in Hong Kong and China stock exchange. According to the said research, audit committee's independence, activities, and competencies, may minimize the practice of earnings management in Chinese companies that are listed in Hong Kong stock exchange. It also confirms that institutional investors have higher confidence toward earnings quality of Chinese companies listed in Hong Kong stock exchange, where compliance level to regulations regarding transparent financial reporting and sufficient disclosure is high. Audit committee effectiveness in this research is measured based on characteristics defined by Hermawan (2009), which comprises activities, size, and competence.

Based on the result presented in Table 3-Model 2, the DFAM*BSCORE variable has the value of logistic coefficient $B = -4.743$ with significance of 0.001 at 5%. This suggests that family ownership has negative and significant influence on the effectiveness of the board of commissioners. Hence, hypothesis 3a that states family ownership minimizes the influence of the board of commissioners' effectiveness on the interest probability of institutional investors is accepted.

Unique characteristic of board of directors within family-owned companies is identified in several previous researches. In general, family-owned companies do not demonstrate confidence toward effectiveness of board members who are considered as "outsiders", even though their presence is key for institutional investors' decision making (Hermalin and Weisbach, 2003). Hemphill (2007) later supports this statement. Other researches such as of Anderson et al. (2004), Bhagat and Bolton (2009), and Adam *et al.* (2010), confirm that the characteristic of a board of directors

with external influence, or having independent board members, provides multiple advantages for the companies, including lowering companies' debts; enforcing discipline in managers in poorly-performing companies, as well as offering new perspective, expertise and knowledge that may not be otherwise possessed by internally elected board-members.

Hypothesis 4a assesses how family ownership could minimize the influence of audit committee effectiveness on the interest probability of institutional investors. Ownership variable, DFAM, is included in the calculation model As presented in Table 3-Model 2, regression test result shows that DFAM*ASCORE variable has logistic coefficient value $B = 22.250$ with significance level of 0.000 at level $\alpha = 5\%$ (significant). The result suggests that family ownership has positive and significant influence on committee audit effectiveness score, in relation to interest from institutional investors. Hypothesis 4a is therefore rejected.

This research shows different results from an earlier research conducted by Wong (2011) regarding audit committee's characteristics, family firms, and earnings management. Wong's research states that audit committee in family firms had fewer independent members, fewer meetings, as well as fewer members with financial or accounting competence. This characteristic implies that audit committees are established as formality to fulfill compliance to reformed regulations of corporate governance, rather than conducting its monitory function. Meanwhile, according to Bushee *et al.* (2010) institutional investors rely on corporate governance internal mechanisms to implement monitoring function on the basis that external supervisory function would require substantial costs.

The impact of family ownership on the interest probability of institutional investors is reflected on the results of hypothesis assessment in Table 3-Model 2. DFAM variable represents family ownership valued 1 if the company is family firm and valued 0 if it is non-family firm. In Table 4.17-Model 2, the value of DFAM logistic regression coefficient is -12.022 with significance level of 0.001, achieves significance level of 1%. This result suggests that family ownership exerts negative and significant influence on interest probability of institutional investors. It is also in line with this research's assumption that institutional investors would avoid investing in family firms.

The above result supports the result of earlier researches that concluded institutional investors would prefer to invest in companies with good corporate governance mechanism (Hermalin and Weisbach, 2003; Bushee et al., 2010). Family firms, on the other hand, tend to implement weaker mechanism of corporate governance (Siregar and Utama, 2008).

In assessing the effectiveness of board of commissioners and audit committee, in relation to interest probability of institutional investors, this research also utilizes control variables such as companies' size, company performance based on ROA,

company's growth opportunities based on PBV, leverage, and companies' risks. For the purpose of this research, control variables are established as constant variables. This ensures that the influence of independent variables on dependent variables will not be affected by other variables that are not included in research observation. The FSIZE variable is found to have positive and significant influence to interest probability of institutional investors. ROA variable also generates positive and significant logistic regression result, confirming the assumption that higher performing companies has higher interest probability from institutional investors. Meanwhile, GRWOPT variable does not influence the interest of institutional investors. This result is in contrary with the research conducted by Martani *et al.* (2009), which conclude that PBV has positive influence on companies' returns. On the other hand, analysis result of leverage variable, or LEV, confirms that institutional investors prefer to invest in companies with lower risk, while analysis result on the RISK variable, or companies' risks, affirmed research result by Wahab *et al.* (2007) that institutional investors would prefer companies with high risk levels.

7. CONCLUSION

Based on the result of testing and analysis that have been conducted, this research concludes that the effectiveness of the board of commissioners has positive and significant influence on interest probability of institutional investors. Effectively, this means that higher effectiveness level of the board of commissioners' lead to higher probability of institutional investor's interest. For institutional investors, it is essential for a company to be able to perform internal supervisory function over its management through the effectiveness of the board of directors (Hermalin and Weisbach, 2003), rather than having external supervisory that would require high costs (Bushee et al., 2010). In addition, institutional investors also require protection against possible expropriation rendered by major shareholders over minority shareholders (Claessens et al., 1999).

Further, the result of this research also finds that the effectiveness of audit committee has positive and significant influence on interest probability of institutional investors. This indicates that companies would gain higher probability level of interest from institutional investors given higher effectiveness score of audit committee. As stated by McKinsey (2002), the quality of disclosure in financial reporting is a key factor to institutional investors' decision making. According to Bushee and Noe (2000), the quality of disclosure is closely linked independent characteristic of the board of directors, as well as with competence of audit committee competence.

In terms of family ownership, this research concludes that family ownership has significant influence in weakening the effectiveness of the board of commissioners, in relation to interest from institutional investors. This implies that the effectiveness of the board of commissioners is lower in family-firms. Several reasons contribute to the conclusion, including that the independent members of the board of directors in family firms are not fully independent, as they are elected based on business relationships or acquaintanceships. Subsequently, members of the board are not able

to work effectively out of hesitancy; aside from they are possibly without the necessary competence to carry out their duties (Garcia-Ramos and Garcia-Olalla, 2011). Other reason is the lack of assurance from company founders on the aptitude of external members of the board, although the company may benefit from their presence. This may be caused by the founder's high level of confidence on his/her own ability to manage the company.

This research also concludes that family ownership has significant influence in improving the effectiveness of audit committee, in relation to interest from institutional investors. The conclusion is based on probable involvement of institutional investors in family firms, in which the quality of disclosure in financial reporting becomes highly important, in order to ensure minimum monitoring costs (Bushee et al., 2010). This conclusion, however, requires further verification.

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