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Corporate Governance, Ownership Concentration, and Bank Risk-Taking

Harnung Octaviyanti[a], **Chorry Sulistyowati**[b*], [a,b]Department of Management, Faculty of Economics and Business, Universitas Airlangga, Email: [b*]chorry.sulistyowati@feb.unair.ac.id

The purpose of this study is to determine the relationship between corporate governance and ownership concentration of a bank in Indonesia. This study uses multiple linear regression models to determine the relationship of independent variables consisting of the proportion of independent directors, the frequency of board meetings, and the concentration of ownership with the bank risk-taking dependent variable. This study uses sample data from annual reports and financial statements of public banks going public during the year 2013-2016. The results show that the proportion of independent directors has a significant positive relationship with the G-ratio and has no significant relationship with total risk. Variable frequency of the board of commissioners meeting has a significant positive relationship with the G-ratio and has a significant negative relationship with total risk. Finally, the concentration of share ownership by the three largest shareholders is positively-related but not significantly-related to the G-ratio, and is significantly negatively-related to total risk.

Key words: *Corporate governance, ownership concentration, bank risk-taking.*

Introduction

The bank is a business entity whose main activity is to accept deposits from the public and then reallocate them to obtain profits and provide services in the payment traffic (Rivai et al., 2013: 1). A country's economic stability is also influenced by the health of its banking system (Irawati, Maksum, Sadalia & Muda, 2019). Banks as financial industries that have strict regulations need to apply the precautionary principle in all their activities, especially in dealing with risks. This is because the risks faced by banks can lead to the risk of failure which will disrupt the stability of the bank. Activities related to bank decisions that contain risks such as bank risk-taking by management must be appropriate because they can create large losses for banks so that through the implementation of Good Corporate Governance and controlling majority shareholders on management performance can reduce bank risk-taking. The development of the era of financial globalisation, the company is basically faced with complex risks so that the implementation of Corporate Governance increases company performance so as to minimise risk. Research on corporate governance has also been carried out before (Harymawan, Agustia, Aprilia, & Ratri, 2020; Larasati, Ratri, Nasih, & Harymawan, 2019; Marzuki et al., 2019; Syahri, Ginting, & Absah; 2019; Prabowo et al., 2017; Nowland, 2016). The concept of Corporate Governance is proposed to achieve more transparent company management for all users of financial statements (Muda, Maulana, Siregar, & Indra, 2018). The implementation of Corporate Governance is contained in Bank Indonesia Regulation No.8 / 4/2006 which regulates the application of Corporate Governance standards for commercial banks in Indonesia. The implementation of Corporate Governance in Indonesia is currently relatively behind compared to countries in the ASEAN region. The practice of Corporate Governance in Indonesia is still said to be higher than Vietnam but inferior to other ASEAN countries such as Thailand with the highest score of 87.53 in 2015 based on data from the ASEAN Capital Market Forum (ACMF) (2015).

Improved corporate governance in Indonesia continues to improve so that it can discipline the responsibilities of the company's organs, and manage risks well so as to increase the value of the company in accordance with the interests of stakeholders. This can be seen from Indonesia's score in each year between 2012-2015 when it experiences an increase of 43.29 in 2012 to 62.68 in 2015. The evaluation and improvement through the issuance of strict regulations in order to make good governance for corporate go-to Indonesian public is increasingly competitive. The presence of Good Corporate Governance in crisis recovery in Indonesia is absolutely necessary because Good Corporate Governance requires good management in an organisation. Good Corporate Governance is a system that is able to provide protection and guarantee rights to stakeholders. Both practitioners and academics agree on the lack of awareness and understanding towards the principles of GCG as one of the reasons why the Indonesian stock market does not make an adequate contribution to the national economy (Suhadak et al, 2019).

According to Effendi (2009: 114), companies that do not implement Good Corporate Governance can eventually be abandoned by investors, undervalued by the community, and subject to sanctions if based on the results of the assessment, the company is proven to violate the law. Companies like this will lose the opportunity (opportunity) to be able to continue their business activities smoothly. But on the contrary, a company that has implemented Good Corporate Governance can create value for the community, suppliers, distributors, the government and it turns out that investors are more interested so that it has a direct impact on the business continuity of the company.

Good Corporate Governance is proxied through the proportion of independent directors, and the frequency of meetings held annually. Andres and Vallelado (2008) show that the characteristics and functions of the board in banking benefit the better performance of banks. The results of the study explain that the characteristics and functions of the board at the bank provide benefits for supervision and input for management so as to reduce information asymmetry and improve bank performance. It can be seen that the number of independent commissioners in 2013 to 2016 has increased until after 2013, indicating that the independent commissioners in banks averaged more than 50% of the total number of boards in accordance with Bank Indonesia regulation No.8 / 14 / PBI / 2006. This shows the importance of their role in monitoring bank activities and also relates to risk-taking by management and risk mitigation faced by banks in the future.

The results of a study conducted by Pathan (2009) indicate that the presence of an independent commissioner will benefit the reduction in risk-taking by bank management. The existence of an Independent Commissioner is intended to create a more objective and independent climate, and also to maintain "fairness" and be able to provide a balance between the interests of the majority shareholders and the protection of minority interests, even the interests of other stakeholders. In addition, the principle of independence of independent commissioners, as parties appointed from outside the company, is an expectation to be able to carry out its responsibilities by not taking sides with certain parties or under pressure. Furthermore, resisting influence from certain parties is expected, toward the goals of shareholders and stakeholders to improve and minimise risks that arise in the future.

The next proxy is the frequency of board meetings that are held annually. The frequency of the board of commissioners meeting, according to research by De Andres and Vallelado (2008), explains the meeting provides an opportunity for board members to gather, to discuss and exchange ideas about how they want to monitor managers and bank strategies. Therefore, the more frequent meetings are held, the tighter the control of managers is so that banks can minimise management activities and anticipate the increasing risk so that bank risk-taking decreases.

Concentration of ownership of a bank can make the level of bank control affect decision-making, especially when a crisis occurs. Ownership structure can effect bank performance, both in terms of profitability and risk. Banks with concentrated stock ownership, will make managers get involved in less risky activities. This is due to the presence of majority shareholders who place restrictions on management due to the monitoring effect, so managers cannot take advantage personally. By applying better monitoring to managers, majority shareholders can find out information on complex and non-transparent bank activities that can increase bank risk (Bataglia and Gallo, 2017). Based on the background described above, the authors are therefore interested in researching on "Corporate Governance, Ownership Concentration, and Bank Risk-Taking."

The results show that the higher the proportion of independent directors, the further the distance of bankruptcy and bank risk-taking decreases. The frequency of meetings of the independent board of commissioners is positively related significantly to the G-ratio and negatively and significantly related to the total risk. In other words, the more frequent meeting of the board of commissioners can reduce risk-taking. The concentration of ownership by the majority shareholder is negatively significantly related to total risk or in other words the concentration of ownership can reduce total risk.

Structure of this paper is as follows: Part 2 is a literature review and hypotheses development; Part 3 is sample description and research variable; Part 4 is result and discussion; Part 5 is conclusions, limitations, and suggestions of this research.

Literature Review

Independent Commissioners and Bank Risk-Taking

Basically, independent commissioners are expected to be able to carry out their duties solely in the interests of the company and away from the influence of various parties who have interests that can conflict with the interests of the company (Alijoyo and Zaini, 2004: 50). Independent Commissioners are members of commissioners from outside the company (not affiliated with the company) who are chosen transparently and independently, have adequate integrity and competence, are free from influences related to personal interests or other parties, and can act objectively and independently based on the principles of good corporate governance (Alijoyo and Zaini, 2004). Implementation of corporate governance according to Bank Indonesia circular No.15 / 15 / DPNP letter F explains the existence of independent commissioners and independent parties to avoid conflicts of interest in carrying out the tasks of all levels or levels of the Bank's organisation. It also explains check and balance, and protects the interests of stakeholders, especially fund owners and minority shareholders.
The presence of commissioners can make it more effective in monitoring management because they can bring different views to face problems (Adams and Mehran, 2012). According to Bataglia and Gallo’s (2017) research, independent commissioners are expected to be negatively associated with risk-taking. This is because a strong board with more independent commissioners is expected to better monitor managers for shareholders. Independent commissioners can provide support to managers when in a difficult decision-making process.

A more independent board (ie. those who do not have a business relationship with management) will be more effective from the perspective of the shareholders, so the existence of an independent commissioner is associated with better decisions (Bebchuk and Weisbach, 2010). Thus, a strong independent commissioner can improve performance supported by increased profits and reduced ROA volatility so as to reduce the risk of bankruptcy and total risk (Vallascas, 2017). The higher the proportion of independent commissioners, the lower bank risk-takings can be.

H1: The proportion of independent commissioners is positively related to the G-ratio.
H2: The proportion of independent commissioners is negatively related to total risk.

Frequency of Meetings and Bank Risk-Taking

The high frequency of board of commissioners' meetings has an impact on the increasing amount of information obtained regarding intensive bank conditions and bank performance. The focus of the board meeting is to improve communication between the directors and the internal control function and make the board more effective in its oversight duties. The holding of the meeting will make the board of commissioners become more active (Yatim, 2009). Board meetings that are held more often will show that the board members look more active and that will benefit shareholders. Board meetings are also a resource in enhancing the effectiveness of the board such that the board can improve the effectiveness of bank performance and appropriate decision-making.

Based on the research of de Andres and Vallelado (2008), board meetings provide opportunities for board members to gather, and to discuss and exchange ideas about how they want to monitor managers and bank strategies. The more meetings, the closer the control of directors, and managers can carry out their role as supervisor. According to article 9 No. 8/14 / PBI / 2006 board of commissioners meeting is one of the intensive spaces to direct, monitor, and evaluate the bank's strategic implementation. Organising meetings according to article 15 8/14 / PBI / 2006: (1) Board of Commissioners meetings must be held periodically at least four times a year; (2) The meeting of the Board of Commissioners as referred to in paragraph (1) must be attended by all members of the Board of Commissioners physically at least two times a year. The more frequent meetings are held, the lower bank risk-takings can be.

H3: The frequency of board of commissioner's meetings is positively related to G-ratio.
H4: The frequency of board of commissioners' meetings is negatively related to total risk.

Ownership Concentration and Bank Risk-Taking

The ownership structure can be divided into dispersed and concentrated ownership structures. Share ownership is said to be concentrated if most are owned by a small number of individuals or groups, so that the shareholders have a relatively dominant number of shares compared to others. Share ownership is said to spread if share ownership spreads relatively evenly to the public, no one owns a very large number of shares compared to the others. If the company's share ownership tends to spread, the owner's control will be weak because of weak supervision (monitoring). If share ownership is concentrated, then the largest shareholder can exercise total control over management (Shinta and Ahmar, 2011).

The research of Leaven and Leavine (2007) found the influence between concentrated ownership and bank risk. Banks with concentrated stock ownership, will make managers engage in activities that are less risky. This is due to the presence of majority shareholders who place restrictions on management due to the monitoring effect, so managers cannot take advantage of high risk-taking activities. By applying better monitoring to managers, majority shareholders can find out information on complex and opaque bank activities that can increase bank risk (Bataglia and Gallo, 2017).

Concentrated ownership can increase monitoring of management. The effect of monitoring by the largest shareholders will have an impact on risk reduction, lower ROA volatility, lower insolvency risk, lower credit risk and a better capital adequacy ratio so that risk-taking will decrease (Dong, Y et al., 2014). The bank's concentrated ownership is measured by the percentage of shares owned by the three largest shareholders according to the study (Dong, Y et al., 2014).

H_5: Ownership concentration is positively related to G-ratio.
H_6: Ownership concentration is negatively related to total risk.

Research Design

Sample and Data Source

The data used in this study is in the form of data from conventional annual reports that have gone public in the year 2013-2016. Islamic bank companies are excluded in this study. Data was obtained from the website namely the Indonesian Stock Exchange (www.idx.co.id).

Data Definition and Variable Measurement

The dependent variable in this study is bank risk-taking as measured through the G-ratio and total risk as measured by using a standard deviation of stock returns. The G-ratio was developed by Liang and Savage to estimate the bankruptcy distance indicator which will lead to bankruptcy risk due to the inability of the bank to pay off its existing obligations using the assets owned.

The independent variable in this study consisted of independent commissioners, the frequency of board meetings, and ownership concentration. Independent commissioners are calculated by the formula of the number of independent commissioners compared to the total board of commissioners in the company (Purwantini, 2011). The frequency of board of commissioners' meetings is the number of meetings held during one year (Yatim, 2009). Ownership concentration is the percentage of shares owned by the three largest shareholders. This study uses two control variables namely bank size and non-performing loans. The size of the bank (SIZE) can describe the size of the total assets owned by the company. In this study company size is measured by using Ln from the company's total assets (Arifuddin, Hanafi, & Usman, 2017). Non-Performing Loans (NPLs) show the debtor's failure to pay their obligations to the bank. The NPL ratio is measured from the ratio between non-performing loans to total loans.

Research Method

The method used in the study uses multiple linear regression models (multiple linear regression method). This study identifies the symptoms of the classic assumptions arising in the regression analysis to determine the presence or absence of symptoms of sample deviation. The classic assumption test consists of tests of normality, multicollinearity, heteroscedasticity, and autocorrelation. The analysis was carried out with the help of SPSS software.

Model 1:

$$\text{G-ratio}_{i,t} = \alpha + \beta_1 \text{KOMIND}_{it} + \beta_2 \text{MEET}_{it} + \beta_3 \text{OWNS}_{it} + \beta_4 \text{SIZE}_{it} + \beta_5 \text{NPL}_{it} + \varepsilon$$

Model 2:

$$\text{RISK}_{i,t} = \alpha + \beta_1 \text{KOMIND}_{it} + \beta_2 \text{MEET}_{it} + \beta_3 \text{OWNS}_{it} + \beta_4 \text{SIZE}_{it} + \beta_5 \text{NPL}_{it} + \varepsilon$$

Result and Discussion

Descriptive Statistics

Tables 1 and 2 show the results of the study where the known lowest value (minimum), the highest value (maximum), the average value (mean) and standard deviation (std. Deviation) of each variable of the company was sampled during 2013-2016.

Table 1: Descriptive Statistics Model 1

Variables	N	Minimum	Maximum	Mean	Std Dev.
G-ratio	90	1.13	119.82	43.53	26.04
Komind	90	0.43	1.00	0.58	0.09
Meet	90	2.00	64.00	15.37	14.35
Own	90	0.33	0.99	0.72	0.17
NPL	90	0.23	12.28	2.99	2.28
Size	90	15.46	22.36	17.94	1.57
Valid N (listwise)	90				

Table 2: Descriptive Statistics Model 2

Variables	N	Minimum	Maximum	Mean	Std Dev.
Vol	86	0.01	0.04	0.02	0.005
Komind	86	0.43	0.75	0.58	0.088
Meet	86	4.00	64.00	16.51	14.621
Owns	86	0.38	0.98	0.71	0.163
NPL	86	0.21	6.94	2.30	1.388
Size	86	15.21	22.85	18.33	1.720
Valid N (listwise)	86				

Independent Commissioner and Bank Risk-Taking

In Model 1 the independent commissioner is positively related to the G-ratio. This means that the more independent commissioners, the higher the G-ratio value or the longer the bankruptcy distance, thus a reduction in risk-taking. This shows that with a stronger corporate governance mechanism, the presence of more independent boards of commissioners can improve bank performance so that profits can increase and risk will decrease, this is supported by strong capital increases and reduced ROA volatility. In addition, more independent commissioners will balance the interests of shareholders and other stakeholders in the bank, including depositors and policy makers. The presence of independent commissioners can make it more effective in monitoring management because they can bring different views to deal with problems that arise which are considered very important for the company. In accordance with Bank Indonesia Circular Letter No.15 / 15 / DPNP letter F, it explains the existence of independent commissioners and independent parties to avoid conflicts of interest in carrying out the tasks of all levels or levels of the Bank's organisation, checks and balances, and protecting the interests of stakeholders especially fund owners and minority shareholders. The results of the study are in accordance with research conducted by Bataglia and Gall (2017); Peni and Vähämaa (2012); Vallascas et al. (2017).

In Model 2 the test results show that the independent commissioner has a negative but not significant relationship to total risk. This shows that the presence of independent commissioners as supervisory boards from outside the company does not contribute optimally in managing total risk. The monitoring mechanism of the independent commissioner does not optimally affect the total risk because there is a part of the total risk that cannot be reduced through diversification, that is the systematic risk where the risk arises due to external factors that will affect the entire company or industry. Therefore, with support through strict regulations from the government as a strong authority holder, it can assist independent commissioners in carrying out their duties as supervisors so that the drivers of risk-taking carried out by independent commissioners are also influenced by external supervision from regulators who play an important role in safeguarding the interests of stakeholders. These results are consistent with research by Bataglia and Gallo (2017); Akhyar (2010); Vallasca et al (2017).

Table 3: Multiple Linear Regression Test Results

Variables	MODEL 1		MODEL 2	
	Coeff.	**Sig**	**Coeff.**	**Sig**
Constant	-40.282	0.242	0.045	0.000
Komind	46.013	0.029*	-0.002	0.812
MEET	0.643	0.000*	-0,000098	0.030*
OWN	11.562	0.332	-0.007	0.054*
NPL	-6.294	0.000*	-0.001	0.134
SIZE	3.197	0.034*	-0.001	0.042*
R^2	0.600			0.187
DW	1.728			1.560

Frequency of Board of Commissioner Meeting and Bank Risk-Taking

In Model 1 the frequency of board of commissioner meetings had a positive and significant relationship with the G-ratio. This means that the higher the board of commissioners meeting, the higher the G-ratio or bankruptcy distance and the bank risk-taking will decrease. This is because more frequent meetings held by the board of commissioners are considered to be a more timely response to members of the board of commissioners to the external conditions of the company and shows that members of the board of commissioners have carried out their duties in accordance with the interests of shareholders, and supervisory activities have become more controlled and can reduce risk because the board of commissioners meeting in accordance with article 9 No. 8/14 / PBI / 2006 is one of the intensive spaces to direct, monitor and evaluate the bank's strategic implementation. Meetings must be increased when uncertainty and high complexity occur so that the board of commissioners proactively plays their role in order to reduce the occurrence of risk. The study is in accordance with research

from Bataglia and Gallo (2017), De Andreas and Vallelado (2008) and Hahn and Lasfer (2015).
In Model 2 the frequency of board of commissioner meetings is also negatively related to total risk. This means that a higher number of board of commissioners' meetings can reduce risk and risk-taking will decrease. Meetings provide an opportunity for board members to gather and discuss and exchange ideas about manager monitoring and discuss bank strategies. Frequently held meetings are also considered to be able to reduce the occurrence of external conditions, namely changing market conditions that can have an impact on bank performance. Therefore, high meetings as a proxy for good corporate governance can be used as a more appropriate board response for reducing risk. This is also supported by Bank Indonesia Regulation Article 15 No. 8/14 / PBI / 2006, namely, board of commissioners' meetings must be held periodically at least four times a year. The results of the study are in accordance with research by Bataglia and Gallo (2017).

Ownership Concentration and Bank Risk-Taking

In Model 1 the concentration of ownership has a positive value and is not significant to the G-ratio or bankruptcy distance. Concentrated ownership by majority shareholders cannot significantly reduce risk because the task of monitoring managers in decision-making can be impeded by differences in the interests of minority shareholders. The majority shareholders have rights in the decision-making mechanism based on the percentage of shares owned so that they can use the opportunity for their interests by transferring the allocation of company resources. This can make minority shareholders feel disadvantaged. These results are consistent with research by Bataglia and Gallo (2017) and Dong et al. (2014).

In Model 2 the concentration of ownership of the largest shareholder has a negative and significant value of total risk. That is, the higher concentration of ownership by shareholders can reduce risk so risk-taking decreases. A large concentration of ownership can place restrictions on management because of the effects of such monitoring so managers cannot take advantage personally. Banks with concentrated ownership, namely majority shareholders, have a strong preference for controlling management and increasing supervision at the place where they invest. The majority shareholding in accordance with the Regulation of the Business Competition Supervisory Commission No.7 of 2011 concerning Guidelines for Article 27 (Share Ownership) Law No.5 of 1999 is a form of control over the portion of company capital that results in the relevant shareholders holding control over management, determining the direction, corporate strategies and policies. This is including but not limited to corporate actions, the determination of directors / commissioners, the exercise of veto rights, access to sensitive information (private information), profit sharing, mergers, consolidations and or takeovers. They can engage with management to set company policies, influence voting and receive special attention from management so that the majority shareholder can monitor managerial discontinuities that occur within the company, so that the risks faced can be reduced. These results are in accordance with the research of Akhyar (2010), Bataglia and Gallo (2017) and Desender (2010).

In Model 1 the bank size variable (SIZE) has a significant positive relationship with the G-ratio. That is, the greater the size of a bank, the longer the bankruptcy distance so that the bank risk-taking will decrease and vice versa. That is because, more total assets owned by the bank will result in a greater G-ratio value and the risk of bankruptcy is lower so risk-taking is smaller. Whereas in Model 2, bank size is negatively related and significant with total risk. In Model 1, the NPL ratio has a significant negative value to the G-ratio while in Model 2 the NPL ratio has a non-significant negative value to total risk.

Conclusion

Based on the results of data analysis that refers to the research objectives, hypotheses and analysis models, the results show that independent commissioners are positively related significantly to the G-ratio or in other words the higher the proportion of independent directors, the further the distance of bankruptcy and bank risk-taking decreases. The frequency of meetings of the independent board of commissioners is significantly positively related to the G-ratio and has a negative and significant relationship with the total risk or in other words the more frequency of the meetings of the board of commissioners can reduce risk-taking. The concentration of ownership by the majority shareholder has a significant negative relationship with total risk – the concentration of ownership can reduce total risk.

The results of this study can be taken into consideration for banks where the application of good governance in accordance with the principles of good corporate governance can reduce bank risk, one of which is through the supervision of external parties, namely the board of commissioners as a neutral party. For regulators, the application of good governance can be done through improving regulations, evaluating and issuing increasingly stringent rules in order to increase the confidence of foreign and domestic investors to invest and put their funds in Indonesia. For shareholders, the presence of majority shareholders as controllers is expected to provide benefits to companies and minority shareholders with appropriate risk-taking behaviour by not taking unilateral profits.

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