# CORPORATE GOVERNANCE AND EARNINGS MANAGEMENT IN INDONESIAN PUBLIC LISTED COMPANIES: THE IMPACT OF IFRS' FAIR VALUE ACCOUNTING ADOPTION

BY

IMAM ZULFIAN

A dissertation submitted in fulfilment of the requirement for the degree of Master of Science (Accounting).

Kulliyyah of Economics and Management Sciences
International Islamic University Malaysia

SEPTEMBER 2021

# ABSTRACT

With studies on the impact of IFRS' fair value adoption on earnings management is sparse, this study aims to examine whether the adoption of IFRS' fair value accounting affects earnings management in terms of the accrual and real activities. In addition, this study examines whether the adoption of IFRS' fair value accounting affects the relationship between corporate governance variables and earnings management. The corporate governance variables are audit committee effectiveness (audit committee size, expertise, and meetings) and the independence of board commissioners. The variables are then regressed using panel data regression, dividing the pre- and post-period IFRS' fair value accounting adoption. Using 123 Indonesian public listed companies, by a total of 738 observations, the study finds that the adoption of IFRS' fair value accounting has significant impact on accrual and real earnings management. Moreover, when the corporate governance variables are regressed with earnings management, the result shows that the audit committee meetings and independent commissioners have a significant impact on lowering accrual earnings management after the adoption of IFRS' fair value accounting. In terms of real earnings management, the study finds that the independent commissioners fail to lower the real activities manipulation in post-adoption of IFRS' fair value accounting. This study provides an overall view of the impact of the adoption of IFRS' fair value accounting by examining its impact on earnings management and corporate governance in Indonesian firms. This study also adds knowledge to the existing literature related to earnings management and extends the understanding of the impact of corporate governance on the issue of IFRS' fair value accounting adoption. Apart from contributing to literature, this study provides recommendation for regulators to lower the earnings management practices by the adoption of IFRS' fair value accounting.

# ملخص البحث

تبعاً للدراسات حول تأثير اعتماد القيمة العادلة للمعايير الدولية لإعداد التقارير المالية على إدارة الأرباح، فإن هذه الدراسة تهدف إلى فحص ما إذا كان اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية يؤثر على إدارة الأرباح من حيث الأنشطة التراكمية والواقعية. بالإضافة إلى ذلك، تختبر هذه الدراسة ما إذا كان اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية يؤثر على العلاقة بين متغيرات حوكمة الشركات وإدارة الأرباح. متغيرات حوكمة الشركات هي فعالية لجنة التدقيق (حجم لجنة التدقيق والخبرة والاجتماعات) واستقلالية مفوضي مجلس الإدارة. بعد ذلك، يتم تراجع المتغيرات باستخدام لوحة انحدار البيانات، وتقسيم اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية قبل الفترة وبعدها. باستخدام 123 شركة إندونيسية عامة مدرجة من خلال ما مجموعه 738 ملاحظة، وجدت الدراسة أن اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية (IFRS) له تأثير كبير على إدارة الأرباح المستحقة والواقعية. علاوة على ذلك، عندما يتم تراجع متغيرات حوكمة الشركات مع إدارة الأرباح، فإن النتيجة تُظهِر أن اجتماعات لجنة التدقيق والمفوضين المستقلين لها تأثير كبير على خفض إدارة الأرباح المستحقة بعد اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية. فيما يتعلق بإدارة الأرباح الواقعية، وجدت الدراسة أن المفوضين المستقلين فشلوا في تقليل التلاعب بالأنشطة الحقيقية في مرحلة ما بعد اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية. تقدم هذه الدراسة نظرة عامة عن تأثير اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية من خلال دراسة تأثيرها على إدارة الأرباح وحوكمة الشركات في الشركات الإندونيسية. تضيف هذه الدراسة أيضاً المعرفة إلى الدراسات السابقة المتعلقة بإدارة الأرباح وتوسع فهم تأثير حوكمة الشركات على مسألة اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية. بصرف النظر عن المساهمة في الدراسات حول هذا الموضوع، تقدم هذه الدراسة توصية للمنظمين لخفض ممارسات

إدارة الأرباح من خلال اعتماد محاسبة القيمة العادلة للمعايير الدولية لإعداد التقارير المالية..

# APPROVAL PAGE

I certify that I have supervised and read this study and that in my opinion, it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Accounting.

……………………………….
Muslim Har Sani bin Mohamad
Supervisor

……………………………….
Maslina Ahmad
Co-Supervisor

I certify that I have read this study and that in my opinion it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Accounting.

……………………………….
Fatima Abdul Hamid
Examiner

……………………………….
Fatimah Mat Yasin
External Examiner

This dissertation was submitted to the Department of Accounting and is accepted as a fulfilment of the requirement for the degree of Master of Science in Accounting.

……………………………….
Zamzulaila Zakaria
Head, Department of Accounting

This dissertation was submitted to the Kulliyyah of Economic and Management Sciences and is accepted as a fulfillment of the requirement for the degree of Master of Science in Accounting.

……………………………….
Gairuzazmi Mat Ghani
Dean, Kulliyyah of Economic and Management Sciences

# DECLARATION

I hereby declare that this dissertation is the result of my own investigations, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degree at IIUM or other institutions.

Imam Zulfian

Signature……………………………… Date……………………

**INTERNATIONAL ISLAMIC UNIVERSITY MALAYSIA**

**DECLARATION OF COPYRIGHT AND AFFIRMATION OF FAIR USE OF UNPUBLISHED RESEARCH**

**CORPORATE GOVERNANCE AND EARNINGS MANAGEMENT IN INDONESIAN PUBLIC LISTED COMPANIES: THE IMPACT OF IFRS' FAIR VALUE ACCOUNTING ADOPTION**

I declare that the copyright holder of this thesis/dissertation are jointly owned by the student and IIUM.

Copyright © 2014 Imam Zulfian and International Islamic University Malaysia. All rights reserved.

No part of this unpublished research may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording or otherwise without prior written permission of the copyright holder except as provided below

1. Any material contained in or derived from this unpublished research may only be used by others in their writing with due acknowledgement.

2. IIUM or its library will have the right to make and transmit copies (print or electronic) for institutional and academic purpose.

3. The IIUM library will have the right to make, store in a retrieval system and supply copies of this unpublished research if requested by other universities and research libraries.

By signing this form, I acknowledged that I have read and understand the IIUM Intellectual Property Right and Commercialization policy.

Affirmed by Imam Zulfian

……………………………… ……………………..

Signature Date

# ACKNOWLEDGEMENTS

All praises be to the Almighty, the most Gracious and the most Merciful, Lord of the universe. I am extremely grateful that I have been blessed with strengths, patience and courage to complete my thesis as a requirement for my course, Master of Science in Accounting at the International Islamic University Malaysia (IIUM).

First of all, I would like to dedicate my greatest appreciation to my supervisors, Assoc. Prof. Dr. Muslim Har Sani bin Mohamad and Dr. Maslina Ahmad, for continuously guiding me throughout the journey with very much cooperation and patience. Besides the professional assistance on my thesis, my supervisors also have given me boundless moral supports and motivations during the process of carrying out this thesis. It is an honor to work and be supervised under such dedicated and diligent supervisors.

Next, I would like to express my gratitude to my beloved parents, Hj. Zulkifli bin Mohammad Hasan and Hjh. Fitriati binti Rusli Yusuf for their endless supports, both morally and physically towards me. They have provided me with tremendous amount of cares and also prayers in the process of my study. Not to mention my other family members who are always there whenever I need them.

Big appreciations to all the lecturers of the Department of Accounting, Kuliyyah of Economic and Management Sciences, International Islamic University Malaysia. I am very thankful for all the knowledge that has been given to me. Also special thanks to those who have spent their supports duting the writing of this thesis. These include my close friends, my classmates, my postgraduate colleagues and others. The thesis would hardly complete without everyone’s motivations especially during this pandemic.

# TABLE OF CONTENTS

# LIST OF TABLES

# LIST OF FIGURES

# CHAPTER ONE

# INTRODUCTION

## 1.1 INTRODUCTION

This chapter explains the background of the study, the problem statement, the study's objective, research questions, the significance of the study, and the motivation for the study. Finally, it ends with an explanation of the structure of the study.

## 1.2 BACKGROUND OF STUDY

Public listed companies have separated the role of ownership and control in their business operations. The owners, who are the shareholders, are the highest authority to influence the managers, who are the agents in the company. Both parties deal with agency contracts such as bonus or compensation schemes promised to the agents if they can fulfill the interest of shareholders as principals. Dealing with agency contracts in companies is not easy. The managers have to ensure that companies are performing well as shareholders expected. However, instead of providing true information, the opportunistic behavior of managers may also exist; they may alter particular information to satisfy the owners with some techniques. Eventually, managers will be compensated for good financial results or increases in stock prices (Ding, Zhang, & Zhang, 2007). To achieve those, managers tend to manage their earnings as the alternative option.

Earnings management is an activity performed by exercising discretionary choice by modifying some contracts and transactions for their benefits. For instance, the managers may engage in earnings management by altering accrual transactions or accounting methods (Braam, Nandy, Weitzel, & Lodh, 2015). A more developed way is through real earnings management, real earnings management is defined as planned actions undertaken by management that are not common from main business practices to achieve targeted earnings (Roychowdhury, 2006). The real earnings management is considered more expensive to perform, but it less detectable. This practice is conducted by manipulating the information affecting the cash flow of operations, discretionary expenses, and production costs (Braam et al., 2015).

To constrain the practice of opportunistic behavior like earnings management among managers, regulators worldwide have introduced a system to reduce misleading and inaccurate information as well as increase the shareholders' rights. This system is commonly named "corporate governance". Good corporate governance is essential to improve firms' performance (Stuebs & Sun, 2015). The establishment of good corporate governance by including boards and audit committees in the structure of a company is also one of the key points of a firm's success.

Good corporate governance is expected to reduce information asymmetry and ensure that companies' agents, the managers, will present true information (Kanagaretnam, Lobo, & Whalen, 2007). The high independence of the board and audit committee increases the quality of financial reporting (Hutchinson, Percy, & Erkurtoglu, 2008). Moreover, Hutchinson et al. (2008) added that boards and audit committee independence play important roles in decreasing the level of earnings management among companies, especially in lowering the discretionary accruals. The role of independent board commissioners is also essential in monitoring the companies to curb earnings management practices (Davidson, Jiraporn, Kim, & Nemec, 2004).

While a good corporate governance mechanism has been developed, the improvement of financial reporting quality is also conducted by regulators by developing accounting standards. The introduction and adoption of International Financial Reporting Standards (IFRS) by many countries have increased accounting quality (Hamidah, 2017; Houqe, 2018). Moreover, past studies found that IFRS adoption plays an important role in deterring earnings management (Kouki, 2018; Zéghal, Chtourou, & Sellami, 2011). One of the IFRS Standards is IFRS 13: Fair Value Measurement. The standard emphasizes the accounting treatment on how to measure some financial information using the fair-value approach, reflecting current market value. Prior literature also found that the adoption of IFRS' fair value accounting is able to improve accounting quality as well as reduce earnings management practices (Paoloni, Guido, & Elisa, 2017; Rhee, Choi, & Ryu, 2018; So & Smith, 2009).

## 1.3 PROBLEM STATEMENT

Earnings management practice is an ongoing phenomenon among firms in emerging countries, including Indonesia. Such practice is conducted by company managers by altering information in the financial statements, thereby misleading their users. The earnings management by the top management may result in low-quality earnings and may leads to fraud (Healy, 1985). Moreover, the monetary crisis that occurred in 2008 had negatively affected the economy, causing an increase in the practice of earnings management (Persakis & Iatridis, 2015).

Previous studies have discussed the efforts to improve financial reporting quality; the use of a single set of accounting standards is one of the strategies. The IFRS has been successfully accepted and adopted by majority of countries since 2005. Deloitte (2016) reported that 131 governments worldwide had announced the mandatory use of IFRS for listed firms. The adoption of IFRS should improve the quality of information disclosed to users, increasing transparency and comparability, and be more beneficial in influencing capital markets (Houqe, 2018). For instance, the adoption of IFRS has decreased the level of earnings management in countries such as France, Belgium, and Germany (Kouki, 2018 and Zéghal, Chtourou, & Sellami, 2011). Previous literature also found that the IFRS adoption has reduced earnings management among listed companies in Indonesia (Setiawan et al., 2019). Thus, the IFRS adoption is expected to lower the level of earnings management in this study. More specifically, one of the IFRS standards is dedicated to fair value measurement. The introduction of a hierarchy of fair values in IFRS should improve the quality of reported earnings with timely financial information reflecting current market conditions. The use of fair value measurement derived from IFRS may have positive impact on firms' value. For example, the fair value adoption managed to increase market prices, shown by higher earnings response of firms after using the fair value measurement (So & Smith, 2009).

Indonesia is one of the countries adopting the IFRS. In 2008, through the Indonesian Institute of Accountants (IAI), Indonesia announced the convergence of Indonesian accounting standards with IFRS. The adoption is a process with some standard changes, and the Pengantar Standar Akuntansi Keuangan (PSAK) has committed to fully adopting the IFRS in 2012 (Hamidah, 2017). There are some phases performed by such jurisdictions by minimizing the gap between the PSAK and IFRS. The adoption of the fair value measurement standard in Indonesia through the standard PSAK No. 68: Fair Value Measurement was released in December 2014. The standard defines a fair value based on an "exit price" notion and uses a "fair value hierarchy", which results in a market-based measurement. Starting from the financial year-end 2015, Indonesian listed companies fully adopted the fair value accounting on their financial statements, replacing the historical cost method.

Regardless of the benefits of IFRS, the reason for Indonesia adopting IFRS as a single set standard is to harmonize the financial reports of listed firms. Based on Hamidah (2017), it is found that IFRS standards are adopted due to the need to boost the economy and stock market performance. Moreover, Hamidah (2017) also found that the adoption of IFRS was conducted by the recommendation of accounting experts, who were also the policy makers that propose accounting regulations. However, prior studies have found that the adoption of fair value accounting lowers earnings quality (Šodan, 2015; Tutino & Pompili, 2018). Therefore, instead of deterring earnings management, there is still uncertainty as to whether the adoption of fair value accounting by IFRS would reduce earnings management level or otherwise. Previous studies also found that the principle-based accounting standards of IFRS provide greater discretion for managers to manage earnings. In line with the argument, the adoption of fair value standards would provide greater discretionary and flexibility for managers to manage earnings. The studies conducted in this area are still sparse, especially among public listed companies in Indonesia.

While the issues of corporate governance among listed companies have been discussed worldwide, the challenge of implementing corporate governance best practice is one of the issues faced specifically in emerging countries. Despite the implementation of good corporate governance, especially with the inclusion of audit committees and Board of Commissioners (BOC), some public listed companies in Indonesia are still struggling to improve their financial performance. Moreover, corruption practice in Indonesia is still high, and it places this country among the most corrupt countries in the world (Prabowo, 2016). Corruption is associated with earnings management practice in developing countries (Lourenço, Rathke, Santana, & Branco, 2018), including in Indonesia. For instance, due to a recent scandal in one of the listed companies, Garuda Indonesia, the director was fired because of illegal smuggling for personal purposes (BBC, 2019). There is a possibility that corporate governance in Indonesia seems not to be effective enough to address these endless issues. The active role of the audit committee and BOC is needed to mitigate such risk, including issues, especially earnings management among the public listed companies in Indonesia.

As the time goes by, Indonesia kept improving in terms of financial reporting and corporate governance. For instance, Indonesia has plans to adopt IFRS fully. One of the progresses is that the IFRS' fair value measurement was initially adopted in Indonesia, but the impact on earnings management is still inconclusive. Setiawan et al. (2019) examine the impact of initial IFRS adoption towards earnings management among listed companies in Indonesia. Also, the study attempts to test whether the independence of BOC reduces the incidence of earnings management. However, the study only examines the earlier period when Indonesia started to adopt IFRS, and only one variable, that is, the independence of BOC, was being tested. Since the IFRS' fair value measurement was initially adopted in Indonesia, its impact on earnings management remains inconclusive. Investigating the effect of the audit committee and BOC due to this IFRS' fair value adoption is deemed necessary since the results using the Indonesian context are still lacking, thus undetermined.

## 1.4 RESEARCH OBJECTIVES

IFRS standards are released for a better quality of financial information. As part of IFRS, the IFRS' fair value accounting is also released to achieve such a purpose. More specifically, it is expected to increase earnings quality. The earnings quality will be lower when the earnings management's practice among the managers are high; thus, IFRS' fair value is enforced to curb such practice. The researcher also expects that the adoption of IFRS' fair value also can be the benchmark to test the performance of the audit committee and BOC. Therefore, the research objectives will be stated as follows:

1. To examine the impact of IFRS' fair value accounting on earnings management among Indonesian public listed companies.
2. To examine the relationship between corporate governance characteristics and earnings management (accrual and real) before and after the adoption of IFRS' fair value accounting among Indonesian public listed companies. Specifically, the study intends:
   a. To examine the relationship of the audit committee and earnings management before and after the adoption of IFRS' fair value accounting in Indonesian public listed companies, and
   b. To examine the relationship between independent board commissioners and earnings management before and after the adoption of IFRS' fair value accounting in Indonesian public companies.

## 1.5 RESEARCH QUESTIONS

The research objectives can be answered by answering the following research questions:

1. What is the impact of IFRS' fair value accounting on earnings management in Indonesian public listed companies?

2. What is the relationship between corporate governance characteristics and earnings management before and after the adoption of IFRS' fair value accounting in Indonesian public listed companies?
    a. What is the relationship between the audit committee and earnings management before and after the adoption of IFRS' fair value accounting in Indonesian public listed companies?
    b. What is the relationship between independent board commissioners and the earnings management before and after the implementation of IFRS' fair value accounting in Indonesian public listed companies?

## 1.6 MOTIVATION OF THE STUDY

The majority of similar studies in various countries have examined the relationship between IFRS adoption and earnings management. Studies testing the impact of IFRS adoption on earnings management have also been discussed in the literature. Using the Indonesian data, the latest published study was conducted by Setiawan et al. (2019). Therefore, the main motivation of this study is due to the lack of research related to the impact of IFRS fair value accounting adoption on earnings management.

Besides limited literature, most research that links IFRS' fair value accounting adoption and earnings management use cross-country data. The latest study by Tutino & Pompili (2018) uses cross-country samples in Europe. Thus, there should also be more studies to be conducted to observe a single country level of fair value adoption and its impact on earnings management. Thus, this study is motivated to focus on Indonesia as the sample to test the effect of the adoption of PSAK N0.68: Fair Value Measurement on the earnings management using Indonesian public listed companies.

## 1.7 SIGNIFICANCE OF THE STUDY

Earnings management's practice is an important issue to be solved; at least, it needs to be minimized. The more earnings management is conducted, the more shareholders will be unprotected. The adoption of IFRS standards, specifically the IFRS' fair value accounting, is expected to be able to curb earnings management. Moreover, such adoption is expected to monitor the effectiveness of audit committee and the indpendence of BOC in lowering earnings management. Therefore, this study is expected to be beneficial as recommendation to be considered in academic and practical level. Academically, this study is expected to contribute to the literature related to financial accounting and governance, as to whether the IFRS' fair value accounting will be able to curb the earnings management and whether it will affect the audit committee and BOC in deterring earnings management from the perspective of Indonesian public companies. From a practical perspective, this study will assist in terms of improving the role of independent board commissioners and the audit committee in the adoption of IFRS's fair value, particularly in the Indonesian context. The audit committee and BOC may be able to perform better to address the intention of managers in terms of managing their company's earnings once the IFRS' fair value is adopted.

## 1.8 STRUCTURE OF THE THESIS

This study is organized as follows:

**Chapter 1:** Introduction. Chapter One consists of the background of the study. Moreover, it identifies the problem statement, followed by the Research Objectives, the Research Questions, the significance of the study, as well as the motivation of the study. The structure of the thesis is also highlighted in Chapter One.

**Chapter 2:** Literature Review. Chapter Two enriches this study with a comprehensive review of the literature and discusses an overview of corporate governance establishment in Indonesia. In addition, this chapter explains the overview of IFRS adoption in Indonesia. This chapter then highlights and discusses prior empirical research that has been conducted in areas related to this research field.

**Chapter 3:** Theory and Hypothesis Development. This chapter aims to explain the theory adopted for the study to be consequently used to explain the background of the research. In addition, this chapter took such theory to develop the hypotheses tested in this study. Lastly, this chapter provides the research model, which is referred to from the hypotheses developed.

**Chapter 4:** Research Methodology. This chapter presents the Research Methodology adopted in this study. This will include the research design, data collection method, sample design, the variables, and how data analysis will be carried out in this research.

**Chapter 5:** Analysis of Results and Discussion of Study Findings. This chapter explains the research findings. Moreover, this chapter also discusses the descriptive statistics of the variables and the test results and discussion.

**Chapter 6:** Conclusion. This chapter discusses the conclusion and summary of the study. This last chapter also mentions the contribution of the study and its limitation, followed by recommendations for further research.

## 1.9 CHAPTER SUMMARY/CONCLUSION

This chapter introduces this study briefly. It also explains the study background, problem statement, study objectives and research questions that have to be answered. The following chapter will discuss the literature review.

# CHAPTER TWO

# LITERATURE REVIEW

## 2.1 INTRODUCTION

This chapter consists of several parts. First, it provides overview of corporate governance development in Indonesia. Second, it explains the development of IFRS adoption in Indonesia. Third, it discusses prior literature that has studied the corporate governance mechanisms (audit committee effectiveness and independent board commissioners), IFRS adoption, IFRS' fair value accounting adoption, and earnings management (accrual and real). Lastly, the chapter ends with a conclusion.

## 2.2 OVERVIEW OF CORPORATE GOVERNANCE IN INDONESIA

The idea to promote corporate governance came from the issues of corporate scandals. The recent global issue related to companies using fraudulent activities to alter financial conditions has attracted the attention of regulators and accountants (Hutchinson et al., 2008). In 2002, the US government issued the Sarbanes Oxley Act (SOX) 2002 due to the bankruptcy of high-profile companies (i.e. Enron and Worldcom). The mandated act provides more corporate governance requirements that should be fulfilled by the companies (Sun, Lan, & Liu, 2014).

Corporate governance is a system providing a framework to ensure the return of the investors on their investment (Shleifer & Vishny, 1997). The establishment of corporate governance aims to control the performance of managers and protect the rights of shareholders so that misleading activities will be minimized. There are two main corporate governance mechanisms which are the board of directors (BOD) and audit committee. Such boards and committees are established to monitor managers' behavior as well as to ensure the reliability of financial reporting. The enforcement of the code of corporate governance has been discussed to address the poor performance of companies, which forces these companies to manage their earnings (Shleifer & Vishny, 1997). The Organization for Economic Cooperation and Development (OECD) in 2015 reported that lack of corporate governance was identified as one of the factors causing the economic crisis.

Indonesia also participates in establishing the code of corporate governance. Due to the 1997–1999 crisis, Indonesia was affected. One of the reasons was the inadequate corporate governance in the companies (NCG, 2006). The Indonesian government, through the Decree of the Ministry of Economics, Finance, and Industry, also established the National Committee for Governance (NCG) as an initiative to improve the practice of corporate governance (Kurniawan & Indriantoro, 2000). Established in August 1999, the NCG's main responsibility is to recommend a national framework for the implementation of good corporate governance. Since 1999, the committee has issued the Code of Good Corporate Governance (GCG) as a reference for regulating good corporate governance in Indonesian public companies. There has been high awareness and continuous improvement by the regulators to increase the rating of the governance in Indonesia. Moreover, the global corporate governance has been reformed over the years. With that, the Indonesian GCG Code has been developed and revised as well (NCG, 2006). The latest revision of the GCG Code was in 2006, and publicly listed companies, state-owned enterprises, province and region-owned companies, companies that raise and manage public funds, companies of which products or services are widely used by the public, and companies with extensive influence on the environment, are expected to become the pioneer in implementing the GCG Code. The regulator/policy makers are also expected to use the GCG Code as a reference for developing related regulations and applicable sanctions (NCG, 2006).

There is a difference in Indonesia’s corporate governance mechanism. Indonesia adopts a two-tier board system of corporate governance. A two-tier system means that there are two different boards coordinating each other to run the companies. Those boards are the Board of Directors (BOD) and the Board of Commissioners (BOC). Both have the responsibility to maintain the long-term sustainability of a company. Moreover, the BOC and the BOD must have the same