Family Control and Good Governance: Does It Affect Firm's Performance?

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Abstract

This paper aims to analyze whether family control and good governance affect firm performance. This model is developed based on the agency view and stewardship perspective. It uses a sample of 71 manufacturing companies listed on the Indonesia Stock Exchange (IDX) for 2017-2019, resulting in 213 observations. The data is analyzed based on panel data regression and moderated regression analysis. Our findings suggest that there is a positive and significant effect of corporate governance on a company's performance. These effects are weaker when firms have a higher level of family control. It might be indicated that the selected directors are not based on competence and only on family relationships which will negatively affect the management's decision.

Keywords
Corporate Governance, Family Control, and Firm Performance.

1. Introduction
Financial performance is one of the critical factors that must be maintained by the company so that investors are interested in continuing to invest in that company. Management's ability to increase shareholder value will go hand in hand with rising share prices. In addition, cooperation between agents and principals in making decisions will increase company value (Onasis and Robin, 2016). In many developing countries, owners of family companies will choose people from their own families or relatives to be appointed board members in their companies, including in Indonesia, where most companies are owned by families (Rashid, 2018). Based on a survey from Price Waterhouse Cooper (PwC) published in CNN Indonesia, it is stated that more than 95% of companies in Indonesia are family-owned businesses (Supriadi, 2014).

In applying the concept of good corporate governance in the Indonesian state, institutional elements are expected to provide a maximum contribution, namely independent commissioners and independent directors. The existence of an independent board brings objectivity in ensuring interests beyond the interests of shareholders (Bohorquez, Ferrero and Sánchez, 2018). The function of the audit committee that assists the board of commissioners in overseeing the company running on an ongoing basis can improve the integrity of financial reporting. The existence of an audit committee can also reduce illegal actions in the form of fraud or falsification by management in financial reporting (Hundal, 2013). Onasis and Robin (2016) concluded that independent commissioners positively affect company performance and the audit committee has a positive effect on financial performance.

1.1 Objectives
This study aims to analyze the effect of governance on company performance by using the ratio of independent commissioners and the number of audit committees. In addition, this study adds family control as a moderating variable of the relationship between governance and company performance because most companies in Indonesia are family companies.

2. Literature Review
Agency theory is a corporate governance concept that regulates the relationship between principals and agents (Anand, 2007). Principal in managing his company assigns duties and responsibilities to agents. Jensen and Meckling (1976) define the agency relationship as a contract between the principal and the agent, emphasizing that the agent should make each decision on behalf of the principal's interest. Rashid (2018) argue that there will be unavoidable conflicts

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between principals and agents. Conflicts arise due to differences in interests between the two parties. Motivations to achieve individual prosperity, lifestyle, and private facilities, are sometimes the triggers. The principal is often disadvantaged as a result of this difference in interests. This agency conflict between the principal and agent is called type I agency conflict, which assumes management takes advantage of shareholders because of scattered ownership (Nurim et al., 2017). It can be overcome in a family business by placing family members in strategic positions in top management.

Agency conflicts also might arise between shareholders. This conflict occurs in companies with concentrated ownership. This difference in interest occurs between the majority and the minority shareholder. Majority shareholders have greater rights in making decisions, such as choosing the board of commissioners and the board of directors at the shareholders' general meeting, known as type II agency conflict (Nurim et al., 2017). The problem that arises from type II agency conflict concerns the issue of moral hazard because majority shareholders can influence the board in making decisions in their favor (Atmaja, Haman, and Tanewski, 2011). Moreover, if some of the board are affiliated with the company's owner, they get greater control in determining policy in the company.

According to Hayat et al. (2018), companies sometimes need to incur agency costs to reduce agency conflicts. It includes the costs of making a sound information system, auditing financial statements so that fraud does not occur, and cost of management supervision (Jensen and Meckling, 1976). Theoretically, management is responsible for maximizing the value of a company (Hayat et al., 2018). Stewardship theory explains that management will act in the best interests of company owners because managers are not always motivated by individual goals and do not tend to abuse company resources for personal gain (Rashid, 2018). Stewardship theory focuses on harmonization between principals and stewards. The role of managers in management is expected to increase the company's profitability. As stewards in the company, the manager's actions must align with the company's owner's goal to achieve mutual success. In this theory, managers should act in the best company's interests and put aside their egos.

The implementation of Good Corporate Governance (GCG) is essential to support the success of sustainable economic growth and economic stability (Anand, 2007). Regarding GCG, Indonesia adopts a two tiers system, in which the board of commissioners and directors have apparent authority and responsibility under their respective functions based on the articles of regulations. Both have the same responsibility in maintaining the company's long-term sustainability. According to Khameswary (2019), four other organs are needed to complete the implementation of GCG, including the Independent Commissioner, Independent Director, and Independent Audit Committee. In the structure of the board of a family company, it is usually found that family members occupy strategic positions as commissioners or directors.

According to Yolanda and Utama (2021), family ownership can positively and negatively impact the company's performance. The existence of family members who occupy strategic positions can benefit the family business itself and reduce agency problems (Komalasari and Nor, 2014). However, according to Rashid (2018), family control can bring losses to the company. It happens when family members who occupy strategic positions are chosen not based on their abilities or competencies (Komalasari and Nor, 2014). Independent commissioners will improve corporate governance quality through the supervisory function (Fadillah, 2017). The existence of an independent commissioner can reduce agency conflict and prevent opportunistic actions from management that will increase the company's performance (Candradewi and Sedana, 2016). Moreover, the audit committee plays a significant role in assisting the board of commissioners carries out their duties, especially in checking the company's financial statements and internal control to ensure that the company is run effectively and efficiently to increase its value (Leung et al., 2014). Therefore we propose the following hypothesis:

H1: Good corporate governance will positively affect the firm performance.

Several studies state that family control harms company performance. Prabowo and Simpson (2011) conclude that family ownership is more detrimental to firm performance when families are highly involved in decision-making. According to Ariani and Fitdiarini (2016), family-owned businesses generate a smaller market value than non-family businesses. Allegations of nepotism make the board unable to manage the company effectively and efficiently, so they can make wrong decisions that reduce company profits. Family-controlled companies tend to prioritize the family's interests so that they may conflict with other parties not part of the family (Laely and Yana, 2018). With the family on the company's board, it is likely to weaken the implementation of good corporate governance because there will be potential conflicts in the management. It happens because the monitoring process from the family commissioner becomes less effective and can increase opportunistic actions on the part of the family (Limbago and Sulistiawan,

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2019). Although public companies in Indonesia require that every company has an independent board of commissioners and an audit committee, fraudulent practices still occur. The transparency of companies' financial statements in Southeast Asia, including Indonesia, is still considered unsatisfactory because of the company's control from the family (Saputra, 2010). According to Haddad et al. (2015), the presence of families on the company's board brings various effects on the board's effectiveness in exercising control.

H2: Family control weakens the positive influence of corporate governance on firm performance

3. Methods

The firm's performance as the dependent variable is measured through Return on Assets (ROA), and Tobin's Q. Corporate governance as the independent variable is proxied by the ratio of independent commissioners and audit committees. The ratio of independent commissioners is measured using a comparison between the percentage of the number of independent commissioners divided by the entire board of commissioners in the company. The board of commissioners formed the audit committee to assist and strengthen the supervisory function of the board of commissioners who work professionally and independently. The audit committee is measured using the total members of the audit committee in a company (Widyati, 2013).

In addition, family control is used as a moderating variable. We measure the level of family control based on public information that provides information related to family relationships by analyzing whether there is a match between the names of the directors and commissioners with the founders of the company (Ulupui, Utama and Karnen, 2014). For some companies, information related to family relationships between directors, commissioners, and shareholders is presented in sentences or tables. Family directors are measured using a comparison between the percentage of family members serving on the board of directors divided by the total directors in a company (Idris et al., 2018; Komalasari and Nor, 2014). Family commissioners are measured using the proportion of families on the board of commissioners (Setiawan and Putri, 2019).

Several control variables included in the model are:

- Firm size is measured by the natural logarithm of total assets (Rashid, 2018). In the context of a family business, the more generations involved, the more potential for conflict of interest.
- Company age is measured by the period since the company was founded (Buallay, Hamdan, and Zureigat, 2017).
- The board size shows the number of directors (Buallay et al., 2017). More members of the board of directors in the company are expected to improve the company's performance by dividing tasks and responsibilities in business management.
- The liquidity ratio is measured by the current ratio (Putri and Santioso, 2019), and
- The debt ratio is measured by total debt divided by total assets (Hayat et al., 2018). Companies with low debt ratios have the opportunity to increase company profitability.

Then the model is analyzed using panel data regression with common effects approach as the analysis tool. The common effects model approach assumes that the behavior of data between companies is the same in various periods.

4. Data Collection

This study uses manufacturing companies listed on the Indonesia Stock Exchange during 2017-2019 as the sample. All the data are collected through the company's annual report and financial reports published on the IDX website. Based on the predetermined sample criteria through the purposive sampling method, we found 71 manufacturing companies from 2017-2019.

5. Results and Discussion

The findings show that independent commissioners significantly affect company performance, as proxied by return on assets and Tobin's Q. It indicates that independent commissioners, through their supervisory roles, can monitor manager's performance and prevent opportunistic actions that can harm the company (Candradewi and Sedana, 2016). Independent commissioners as neutral parties will be more flexible in conducting supervision without any intervention. Onasis and Robin (2016) strengthen the notion that independent commissioners positively influence company performance in Indonesia. A competent board of commissioners will be able to supervise the company's

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directors and management in making strategic policies that can improve company performance (Aprianingsih and Yushita, 2016).

There are interrelated roles between the independent commissioner and the audit committee because an independent commissioner holds the chairman of the audit committee. Just like independent commissioners, the audit committee also consists of neutral people who are parties outside the company. The audit committee's duties include reviewing financial statements, the audit process, and internal control to ensure that the accounting information contained in the financial statements is not biased (Leung et al., 2014). The results show that the audit committee significantly improves company performance as proxied by return on assets. These results are supported by Putra and Fidiana (2017) and Aprianingsih and Yushita (2016). The audit committee is beneficial in optimizing the supervision that will have an impact on the influence of the company's performance. They focus on supervision, especially in the company's accounting and internal control (Hermiyetti and Katlanis, 2017). It indicates that more audit committee members will have a good impact on the supervision carried out.

The Moderated Regression Analysis (MRA) results show that family control weakens the positive influence of governance proxied by independent commissioners on company performance. It is supported by Komalasari and Nor (2014) and Prabowo and Simpson (2011), who explain that family control negatively impacts company performance. The existence of family control that participates in company management will weaken the influence of good governance as the family members can change the direction of policies and strategic decisions that will be implemented (Yopie et al., 2018). Families who have voting rights through their ownership can intervene in the direction of the decisions to be taken.

We also found that the interaction models between independent commissioners and family control will weaken the positive influence of corporate governance on company performance. This can happen because the independent commissioner only has the authority to supervise and provide suggestions or advice on the management of the company (Fadillah, 2017; Putra, 2015). A director who comes from the family makes an intervention in decision-making easier. This happens because the company's management decisions are entirely in the hands of the board of directors (Ridwan and Afriyenti, 2019). The role of the family commissioner will also assist the family in supervising the decision-making that has been made.

Although stewardship theory assumes that family control can reduce agency conflicts, it may lead to agency conflicts in other forms that can reduce company performance. A family company tends to have a type II agency conflict risk because there is a majority shareholding owned by the family, which can cause conflict when the decisions made by the company are considered beneficial to the family. The involvement of families who participate in managing the company and being placed on the board, both as directors and commissioners, can decrease the company's value. The selection of families to be included in the company's board without special abilities and expertise can decline the company's performance (Pranata et al., 2019).

On the other hand, this study finds that family control can strengthen the positive influence of corporate governance proxied by the audit committee on company performance. The interaction between the audit committee and the two family control proxies, namely family directors and family commissioners, will strengthen governance's positive influence on company performance (Hundal, 2013; Onasis and Robin, 2016). The audit committee has an essential role in maintaining the credibility of preparing financial statements to implement good corporate governance (Sumantri and Mardianto, 2018). The existence of directors and commissioners with family relationships with owners or majority shareholders is believed to reduce agency problems (Makhlouf et al., 2018). The reduction in agency problems within the company can improve company management. Therefore, family control is likely to strengthen the positive influence of the audit committee on company performance.

5.2 Graphical Results

Statistic Descriptive is stated in Table 1 and Pearson Correlation is presented in Table 2., The Regression Results of Corporate Governance on Firm’s Performance is shown in Table 3.

Table 1. Statistic Descriptive

Variable	Obs	Mean	Dev. Std	Min	Max
ROA	213	0,06	0,12	-0,40	0,92
TOBINSQ	213	1,92	2,93	0,17	23,29
Ind. Commisioner	213	0,44	0,13	0,20	1,00
Audit committee	213	3,03	0,39	2,00	5,00
Family's Director	213	0,24	0,25	0,00	0,75
Family's Commisioner	213	0,20	0,23	0,00	0,67
SIZE	213	28,82	1,57	25,22	33,49
AGE	213	40,31	16,38	3,00	101,00
BoDSIZE	213	5,31	2,35	2,00	14,00
Liquidity	213	2,22	1,64	0,27	13,04
Debt ratio	213	0,45	0,25	0,07	1,95

Table 2. Pearson Correlation

		1	2	3	4	5	6	7	8	9	10	11
1	ROA	1.00										
2	TOBINSQ	0.47	1.00									
3	Ind. Commisioner	0.35	0.21	1.00								
4	Audit committee	0.07	-0.11	0.11	1.00							
5	Family's Director	-0.10	-0.15	-0.17	-0.09	1.00						
6	Family's Commisioner	-0.05	-0.07	-0.23	-0.18	0.54	1.00					
7	SIZE	0.08	0.17	-0.03	0.31	-0.31	-0.25	1.00				
8	AGE	0.25	0.55	-0.05	-0.12	-0.13	-0.04	0.14	1.00			
9	BoDSIZE	0.05	0.16	-0.06	0.24	-0.28	-0.22	0.65	0.17	1.00		
10	Liquidity	0.16	-0.11	0.07	-0.08	0.01	0.19	-0.24	-0.06	-0.15	1.00	
11	Debt ratio	-0.10	0.11	0.06	0.01	0.02	-0.12	0.01	0.06	0.04	-0.65	1.00

Table 3. The Regression Results of Corporate Governance on Firm's Performance

	ROA		**TOBINSQ**	
	I-A	**I-B**	**II-A**	**II-B**
C	-0,38**	-0,38**	-4,39**	-3,18**
	(-17,68)	(-15,16)	(-15,47)	(-4,49)
Ind. Commisioner	**0,19****		**2,56****	
	(9,69)		**(8,65)**	

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Audit committee		**0,02****		**-0,10**
		(4,23)		**(-0,98)**
SIZE	0,01**	0,01**	0,08**	0,04**
	(16,54)	(11,89)	(8,47)	(2,25)
AGE	0,00**	0,00**	0,04**	0,07**
	(20,60)	(28,04)	(65,23)	(62,52)
BoDSIZE	-0,00**	-0,00**	0,05**	0,11**
	(-3,74)	(-9,34)	(5,01)	(8,21)
Liquidity	0,01*	0,01**	-0,00	-0,00**
	(2,81)	(5,82)	(-0,44)	(-2,69)
Debt Ratio	-0,04**	-0,01*	0,73**	1,10**
	(-2,91)	(-1,88)	(8,32)	(12,74)
N	213	213	213	213
F-statistic	39,12	72,12	25,57	202,66
Prob(F-statistic)	0,00	0,00	0,00	0,00

** $p < 0,05$ dan * $p < 0,10$
Nilai *t-Statistic* disajikan dalam kurung

The Regression Results of Corporate Governance and Family Control Interation on Firm's Performance is presented in Table 4.

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Table 4. The Regression Results of Corporate Governance and Family Control Interation on Firm's Performance

	ROA				**TOBINSQ**			
	I-A	**I-B**	**I-C**	**I-D**	**II-A**	**II-B**	**II-C**	**II-D**
C	-0,46**	-0,42**	-0,28**	-0,29**	-3,75**	-6,65**	-1,96**	-1,44**
	(-20,56)	(-11,14)	(-7,69)	(-19,63)	(-15,63)	(-32,92)	(-15,73)	(-22,32)
Ind. Commisioner (IC)	0,22**	0,20**			5,26**	3,38**		
	(-16,29)	(-5,55)			(-11,05)	(-7,74)		
Audit Committee (AC)			-0,04**	-0,03**			-1,43**	-1,07**
			(-5,41)	(-4,85)			(-207,24)	(-19,22)
Family's Director (FD)	0,08**		-0,44**		4,98**		-11,23**	
	(-8,03)		(-12,41)		(-13,71)		(-52,06)	
Family's Commisioner (FC)		0,02		-0,58**		3,41**		-10,94**
		(-0,45)		(-7,35)		(-7,21)		(-10,43)
IC*FD	**-0,13****				**-10,71****			
	(-5,47)				**(-14,62)**			
IC*FC		**0,04**				**-5,32****		
		(-0,41)				**(-3,72)**		
AC*FD			**0,15****				**3,80****	
			(-13,67)				**(-42,59)**	
AC*FC				**0,20****				**3,90****
				(-7,49)				**(-12,7)**
SIZE	0,13**	0,01**	0,01**	0,01**	0,02**	0,14**	0,18**	0,13**
	(23,25)	(14,96)	(11,90)	(16,09)	(7,40)	(37,94)	(-32,15)	(-41,45)
AGE	0,00**	0,00**	0,00**	0,00**	0,05**	0,04**	0,04**	0,04**
	(29,41)	(20,05)	(13,68)	(16,01)	(30,47)	(29,71)	(-17,77)	(-13,86)
BoDSIZE	-0,00*	-0,00**	-0,00**	-0,00**	0,09**	0,07**	0,03**	0,05**
	(-1,95)	(-2,49)	(-14,08)	(-7,60)	(26,37)	(17,10)	(-2,32)	(-6,53)
Liquidity	0,01**	0,01**	0,01**	0,01**	-0,07**	-0,03	0,03**	-0,01*
	(2,09)	(2,36)	(4,53)	(5,09)	(-12,27)	(-1,40)	(-2,45)	(-1,67)
Debt Ratio	-0,05**	-0,05**	-0,02**	-0,03**	0,36**	0,57**	0,93**	0,73**
	(-2,60)	(-3,54)	(-2,03)	(-2,84)	(4,44)	(4,25)	(-6,01)	(-5,29)
N	213	213	213	213	213	213	213	213
F-statistic	32,07	30,94	101,00	46,98	41,30	27,28	20,19	58,50
Prob(F-statistic)	0,00	0,00	0,00	0,00	0,00	0,00	0,00	0,00

** p < 0,05 dan * p < 0,10

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6. Conclusion
This study aims to determine the effect of corporate governance on company performance with family control as a moderating variable. The main findings are that corporate governance positively and significantly influences the company's performance. Independent commissioners and audit committees are essential in creating good corporate governance by reducing agency conflict. Family control proxied by family directors weakens corporate governance's positive influence on firm performance. It indicates that if the selected directors are not based on competence and only on family relationships will negatively affect the company's management.

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