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## The Impact of Corporate Governance on Capital Structure For Companies Listed on The IDX

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**Abstract:** This study was conducted due to the challenges in implementing good governance practices in public companies in Indonesia. Companies in Indonesia also face challenges in ownership and control of the company. Amidst the increasingly complex business world, corporate governance and decision-making regarding capital structure are becoming increasingly important. The purpose of this study is to determine how corporate governance, especially commissioner compensation, board size, and company size affect the company's capital structure. The sample of this study includes companies listed on the LQ 45 index on the Indonesia Stock Exchange (IDX) from 2021 to 2023. The research data comes from financial reports available on the IDX website. To test the hypothesis, a two-way ANOVA analysis was used. The research findings show that there is no significant difference in capital structure related to compensation and board size. Conversely, company size shows a significant effect on variations in capital structure. In addition, there is no significant interaction between board compensation, board size, and company size in their effect on differences in company capital structure.

**Keyword:** Board of Commissioner's Compensation; Board of Commissioner's Size; Capital Structure; Company Size; Good Corporate Governance.

### INTRODUCTION

One of the problems that public companies in Indonesia may face is the lack of transparency and accountability in corporate governance. According to the 2020 BUMN Governance Index Report, there are still challenges in implementing good governance in the public sector, including supervision of the board of directors and company management. The lack of transparency and accountability can have an impact on the company's financial decisions, including in choosing the optimal capital structure.

In addition, companies in Indonesia also often face challenges related to company ownership and control. Complex ownership structures that are often concentrated in certain groups or individuals can affect corporate governance mechanisms and financial decisions

taken. Conflicts of interest between shareholders, management, and majority shareholders also play a role in shaping a company's capital structure.

Amidst the ever-growing complexity of the business world, corporate governance and decisions related to capital structure are becoming increasingly crucial for public companies. Corporate governance is a form of effort made by management in carrying out its responsibilities. This study replicates a similar study by (CD Cole, 2019). Corporate governance is an effort made by the company's management to carry out its duties. As an agent for shareholders, of course, the company's management has an obligation to fulfill all that is expected by the owners or principals as well as other parties such as consumers, workers, suppliers and also the community. Thus, the main objective in managing the company is to protect stakeholders (Madhani, 2017).

In carrying out these obligations, agents (company management) and also owners (shareholders) must realize a balance, both parties benefit each other. For this, effective corporate governance is needed. Effective governance at least has rules, practices or processes that can be carried out by company management and can be supervised by shareholders or owners. This is as conveyed by Nasem et al., a set of rules, practices and processes are mechanisms that function to monitor the behavior and actions of management (Naseem et al., 2017). One of the internal mechanisms is the board of directors which is used by shareholders to oversee the actions and activities of the management team (Adams et al., 2010). One of the important tasks of the management team is to make decisions about the type of funding to be used in the company / organization. This funding decision is the main one for determining the optimal mix of debt and equity for current operational funding and also for potential future growth potential (C. Cole et al., 2015; shahzad et al., 2017). Most companies obtain financing from bond issuance and for capital financing obtained from share issuance or from retained earnings in the previous period (C. Cole et al., 2015). However, in practice in the field there are different views on corporate governance based on the theory and objectives of the board of commissioner's or board of commissioners. In this regard, there are three basic theories that can explain the objectives and rules regarding the board of directors, including agency theory, stewardship theory, and resource dependence theory (Madhani, 2017).

Based on the three theories above, the capital structure owned by the company will be analyzed accordingly. These three theories will ultimately be associated with the type of compensation level of the board of commissioner's, the size of the board of commissioners, and also the size of the company. The size of the company is added according to the recommendations given (C. Cole et al., 2015).

The researcher assessed that there is a potential difference in capital structure associated with various types of board of commissioner compensation, and various types of board of commissioner sizes. Based on this assessment, there are 4 study questions that are asked:

1. What are the differences in capital structure when associated with various levels of board of commissioner compensation?
2. What are the differences in capital structure when associated with different board sizes?
3. What are the differences in capital structure when associated with different company sizes?
4. What is the relationship between various levels of board of commissioner compensation and various levels of board size and company size when determining capital structure?

This study is important to be conducted considering that good and effective corporate management is crucial for corporate management to carry out its obligations in managing the company well. Management is responsible for meeting the expectations of owners and other parties. Meanwhile, the board of commissioner's is tasked with overseeing management performance, one of which is regarding funding decisions related to the optimal mix of debt and equity for current operational funding and potential future growth.

The purpose of this study is to investigate the impact of corporate governance on capital structure selection in the context of listed companies. Through this study, it is expected to reveal how corporate governance factors, such as shareholder composition and the role of the board of directors, interact with the company's capital structure decisions. It is expected that this study can provide in-depth insights into corporate governance related to company management, the board of commissioners, and its main stakeholders in terms of company funding or the company's capital structure. This study can later serve as a basis for consideration in making company decisions regarding capital structure, especially related to the implementation of good corporate management. In addition, this study can also be a source of literature and new references in the academic field, especially in the context of capital structure and corporate governance.

## **METHOD**

This study adopts a quantitative method to analyze the differences between existing variables. The focus of this study is on companies listed or registered on the Indonesia Stock Exchange (IDX). The sample comes from companies included in the LQ 45 index during the 2021-2023 period, totaling 135 companies. Secondary data were collected from annual reports and financial reports available on the IDX and company websites. The independent variables analyzed include board of commissioner compensation, board of commissioner size, and company size, while capital structure is used as the dependent variable. The data analysis process was carried out using SPSS with hypothesis testing through two-way analysis of variance (two-way ANOVA).

### **Operational Description of Variables**

#### **Compensation of the board of commissioner's**

Board of commissioner compensation is a description of how board of commissioner compensation is obtained. In this study, a dummy variable is used, if the company provides stock-based compensation, then the value is 1, if the company does not provide stock-based compensation, then the value is 0.

#### **Size of the board of commissioner's**

The size of the board of commissioner's is a description of the number of board of commissioner's. In this study, the description of the size of the board of commissioner's is categorized into three, namely a small board of commissioner's if it has 5-7 members, a medium board of commissioner's if it has 8-9 members, and a large board of commissioner's if it has more than 10 members (Coles et al., 2008; Ning et al., 2010).

The board of commissioner's size criteria scores are:

1. indicates small size
2. indicates medium size
3. indicates large size

#### **Company size**

Company size reflects the total net worth of the company. In this study, company size is represented by stock price calculated based on market capitalization. In his study, Roosmawarni et. al.(2023) states that market capitalization is categorized into 3, namely large if the market capitalization is more than \$10 billion or more than 162.1305 trillion rupiah, medium if the market capitalization is between \$2 - 10 billion or equivalent to 32.4261 trillion rupiah - 162.1305 trillion rupiah, small if the market capitalization is less than \$2 billion or equivalent to 32.4261 trillion rupiah.

$$\text{Market capitalization} = \text{outstanding shares} \times \text{Stock price}$$

The company size criteria scores are:

1. 1 for small company size
2. 2 for medium sized companies
3. 3 for large company size

### Capital structure

Capital structure is used to assess the different ways a company chooses to finance assets or future growth. In this study, capital structure is proxied by the market leverage ratio (MLR) (Chang et al., 2014; Hermassi et al., 2017).

$$MLR = \frac{\text{Total debt}}{\text{Total debt} + \text{market value}}$$

## RESULTS AND DISCUSSION

### Normality Test

The normality test was conducted to determine the suitability of the data in this study with a normal distribution. Data is considered normal if the significance value is  $\geq 0.05$ . Here are the test results:

**Table 1. Normality Test Results**

|                                  |                | Standardized Residual for MLR |
|----------------------------------|----------------|-------------------------------|
| N                                |                | 135                           |
| Normal Parameters <sup>a,b</sup> | Mean           | .0000                         |
|                                  | Std. Deviation | .93442                        |
| Most Extreme Differences         | Absolute       | .066                          |
|                                  | Positive       | .055                          |
|                                  | Negative       | -.066                         |
| Test Statistic                   |                | .066                          |
| Asymp. Sig. (2-tailed)           |                | .200 <sup>c,d</sup>           |

Source: Processed Data (2024)

Based on the table, the standard residual significance value is recorded at 0.200, exceeding 0.05. Thus, the data can be considered normally distributed.

### Homogeneity Test

**Table 2. Homogeneity Test Results**

**Levene's Test of Equality of Error Variances<sup>a</sup>**

Dependent Variable: MLR

| F    | df1 | df2 | Sig. |
|------|-----|-----|------|
| .760 | 17  | 117 | .734 |

Source: Processed Data (2024)

Levene's test was conducted to test the homogeneity of the data, which aims to determine whether each variable has a similar variance. The results of the Levene's test show the data significance value is 0.734,  $> 0.05$ . Therefore, the data is stated to have the same variance, thus meeting the homogeneity test criteria.

## Hypothesis Testing

**Table 3. Two-way ANOVA Test Results  
Tests of Between-Subjects Effects**

Dependent Variable: MLR

| Source                                 | Type III Sum of Squares | df  | Mean Square | F       | Sig. |
|--|-------------------------|-----|-------------|---------|------|
| Corrected Model                        | 6209.480 <sup>a</sup>   | 17  | 365.264     | .895    | .581 |
| Intercept                              | 353857.890              | 1   | 353857.890  | 867.007 | .000 |
| Kompensasi_DK                          | 1.649                   | 1   | 1.649       | .004    | .949 |
| Ukuran_DK                              | 274.865                 | 2   | 137.432     | .337    | .715 |
| Ukuran_PR                              | 3064.254                | 2   | 1532.127    | 3.754   | .026 |
| Kompensasi_DK<br>Ukuran_DK             | *1005.065               | 2   | 502.532     | 1.231   | .296 |
| Kompensasi_DK<br>Ukuran_PR             | *60.989                 | 2   | 30.495      | .075    | .928 |
| Ukuran_DK * Ukuran_PR                  | 1128.681                | 4   | 282.170     | .691    | .599 |
| Kompensasi_DK<br>Ukuran_DK * Ukuran_PR | *757.733                | 4   | 189.433     | .464    | .762 |
| Error                                  | 47752.046               | 117 | 408.137     |         |      |
| Total                                  | 448486.000              | 135 |             |         |      |

Source: Processed Data (2024)

Based on the two-way ANOVA test, a significance value of 0.715 was obtained for the size of the board of commissioner’s, which exceeded the threshold of 0.05. This indicates that the size of the board of commissioner’s does not have a significant effect on variations in capital structure. The two-way ANOVA test obtained a significance value of 0.949 related to the compensation of the board of commissioner’s, which also exceeded the critical value of 0.05. This indicates that the type of compensation given to the board of commissioner’s does not have a significant impact on changes in capital structure. The two-way ANOVA test obtained a significance value for company size of 0.026, smaller than the limit of 0.05. This finding indicates that there is a significant difference in capital structure influenced by company size. The test showed a significance value of 0.762 for the interaction between the compensation of the board of commissioner’s, the size of the board of commissioners, and the size of the company exceeding the threshold of 0.05. Thus, no significant interaction was found between the three variables on changes in capital structure.

### Board of Commissioner’s Compensation for Capital Structure

The results of the hypothesis test show no difference in capital structure proxied by MLR based on the type of compensation received by the board of commissioners. This is contrary to agency theory and also resource dependency theory, but in accordance with stewardship theory. In agency theory, there is a possibility of a conflict of interest between managers or agents and company owners. Stock-based compensation (equity) can reduce conflict and align the interests of managers with owners. In resource dependency theory, the board of commissioner’s provides important resources for the company in the form of formal and informal relational capital. The results of this study may contradict agency and resource dependency theories because few companies provide compensation in the form of shares or equity, so there is no incentive for the board of commissioners to make decisions in the capital structure. In addition, the role of the board of commissioner’s may be more about supervising management than as an operational decision maker. While in stewardship theory, the board of directors should not be a guarantee for the company owners. The results of the study are in accordance with stewardship theory because it is the obligation of the board of commissioners

to do their best in managing company resources, regardless of the type of compensation received. The results of the hypothesis test are in accordance with the study found by (Bulan et al., 2014) that board of commissioner compensation has no significant effect on capital structure decisions in the financial sector. On the contrary, this finding is inconsistent with the findings (Kusumo & Hadiprajitno, 2017; Rachmawati & Sari, 2017) that shows a positive relationship between board of commissioner's compensation and the decision to use debt in the capital structure.

### **Size of the Board of Commissioner's Against Capital Structure**

The results of the hypothesis test show that the capital structure proxied by MLR is not affected by the size of the board of commissioners. This study indicates that the size of the board of commissioners does not affect the company's financing decisions. This finding is contrary to agency theory and also resource dependence theory. In agency theory, the board of commissioner's is tasked with supervising management to align the interests of shareholders and managers. Meanwhile, in resource dependence theory, board members provide an external network that helps reduce uncertainty, increase the value and strength of the company. This may occur because the board of commissioners supervision of the company's operations is less effective, so that financing decisions are more influenced by the board of directors. In addition, the expertise of the board of commissioner's has more influence on decision-making related to the company's capital structure compared to the number of board members. However, this finding supports the stewardship theory, which states that the board of commissioner's, even though the number of members varies, is still responsible for acting in the interests of the company. This finding is in line with the study of (Gustyana & Hanari, 2022; Thesarani, 2017), concluded that the capital structure is not influenced by the size of the board of commissioners. This is in contrast to the study of (Alabdullah & Mohamed, 2023; Balagobei, 2020; Javaid et al., 2023; Novitasari et al., 2020; Uddin et al., 2019).

### **Company Size Against Capital Structure**

The results of the hypothesis test indicate a significant difference in capital structure, as proxied by MLR, related to firm size based on market capitalization. Large firms tend to require more operating funds, thus utilizing external capital as a source of funding. Management theory explains that large firms have more funding options and can determine an efficient capital structure. Meanwhile, resource dependence theory highlights better access to capital markets and the ability to obtain low-cost financing as factors that influence the capital structure of large firms. In addition, large firms tend to be more flexible in issuing new shares because their shares are widely distributed, so that corporate control is not greatly affected. This finding is consistent with research that shows that firm size has an effect on capital structure in the manufacturing sector. However, this result is in line with (Aruan et al., 2022; Hutabarat, 2022; Noliviasari & Siswantoro, 2022) who found a positive effect of company size on capital structure, but contradicted (Annisa et al., 2020; Purnasari et al., 2020) which states there is no significant influence.

### **Board of Commissioners Compensation, Board of Commissioners Size, and Company Size on Capital Structure**

The results of the hypothesis test show no significant interaction between the type of board of commissioner's compensation, the size of the board of commissioners, and the size of the company on changes in capital structure. Variations in the type of compensation, the number of board of commissioner's members, and the size of the company do not have an effect on the decision to change the capital structure. This indicates that the three variables are not the main factors that can influence decisions related to the company's capital structure. This is because

agency theory focuses on the potential for conflicts of interest between owners and agents. While in stewardship theory, the role of the board of commissioners focuses more on the company's long-term goals regardless of compensation or company size and the size of the company. In resource dependency theory, board members provide an external network that is able to provide information, skills, and reduce company uncertainty that can increase the value and strength of the company regardless of the size of the company.

## CONCLUSION

This study aims to analyze the differences in capital structure influenced by the type of board of commissioner's compensation, the size of the board of commissioners, and the size of the company. The results of the study show that there is no difference in capital structure proxied by MLR based on the type of board of commissioner's compensation or the size of the board of commissioners. However, there is a difference in capital structure proxied by MLR based on company size as measured by market capitalization. The limitation of this study is that the objects used are limited to companies listed in the LQ 45 during the 2021-2023 period. In addition, there is also the use of dummy variables for the board of commissioner's compensation variable. Further researchers are advised to consider companies from other sectors and add additional variables.

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