International Journal on Economics and Social Sciences
Vol.1, No. 1 January 2015
ISSN: 2442-9759 (Online)
2442-8574 (Printed)

THE INFLUENCE OF CORPORATE GOVERNANCE IMPLEMENTATION TOWARD BANK PERFORMANCE (Empirical Study on Banks Listed in Indonesian Stock Exchange)

Heriyanni Mashitoh[1]*and Irma[1#]
Faculty of Economics, Open University, Jakarta, Indonesia

Corresponding email: *heriyanni@ut.ac.id , [#]irma@ut.ac.id

ABSTRACT

This study is aimed to investigate the effect of corporate governance indicators such as the board of directors, audit committee and audit quality to the bank performance which is proxied by CAMEL ratio such as CAR, NPL, LDR, ROA, BOPO and ROE. The samples were 30 listed banks in the Indonesian Stock Exchange. Structural Equation Modelling (SEM) was used to test the influence of corporate governance indicators to the bank performance. The test results proved that the board of commissioners had a significant positive correlation to the bank performance. It means the higher the commissioners' supervision, the better the performance of the bank. Similarly, the audit quality also has a significant positive correlation to the bank performance which means the higher the audit quality, the better the performance of the bank. It has also been revealed that the audit committee, although positively related to bank performance but it is not significantly proved. The results of this study are supported by some previous studies.

*Keywords:*Corporate Governance, Performance Bank, CAMEL Ratio, the Board, the Audit Committee, and Audit Quality

1. INTRODUCTION

The banking industry has always been an object of interest to be investigated because it has two characteristics that distinguish it from other industries in general. First, as a regulation-intensive industries (highly regulated). Almost every side of the bank's activities can not be separated from the scope of regulation and monitoring of the resident agency standards or regulatory agencies, which in Indonesia is conducted by Bank Indonesia (BI). Many provisions governing banking business aims to protect the interests of the wider community. It is a consequence that is caused by the characteristics of the two banks. The banking industry is based on trust, especially the trust of its customers.

People who become customers of bank put the funds held in the bank without a full guarantee of the bank, even with the rate of return set by the bank. In accordance with its role as an intermediary and drive of the economy, the funds collected will be re-routed by the bank in the form of other investments. In carrying out its activities, the bank faces a variety of risks such as credit risk, market risk, operational risk and legal risk. To that end, the bank needs to be managed with governance (corporategovernance) by both professional management and high integrity. Without good governance, the banking industry will probably experience a collapse as it did in 1997.

It was preceded by a financial crisis in many countries in the 1997-1998. Financial crisis that began in Thailand in 1997 and was followed by the crisis in Japan, Korea, Indonesia, Malaysia, Hong Kong and Singapore which eventually turned into the Asian financial crisis. It is seen as a result of lack of practice of Good Corporate Governance (GCG). Among others, the close relationship between government and business, conglomeration and monopoly, protection, and market interventions that make these countries are not ready to enter the era of globalization and free market (Tjager et al., 2003).

However, a mild condition for the establishment of banks has a negative impact and lead to an increase in the number of banks and banking which are fairly aggressive. This increase was colored with cross-ownership issue and management of cross in the financial industry. These two things are the cause of the increased concentration of ownership in the banking industry, so the greater the likelihood of violation of the legal lending limit to a group of its own company, the greater the impact in the banking sector. After going through a period of economic crisis, the number of commercial banks in Indonesia has decreased (from 237 banks in 1997 down to 130 banks in 2006, a drop of 45.2%), resulting from the freezing of 67 bank and 40 banks merged and acquisitions. The decrease is a result of the strict standards that must be met for the establishment of a bank, such as capital structure, mergers, acquisitions and bank closures due to financial problems.

When observed from the background and the conditions,one of the main causes of the banking industry collapse experienced during the crisis is related to the poor management. Valuable lessons to be learned from the financial crisis faced by Indonesia are due to weak implementation of good corporate governance (GCG) in the banking industry. GCG implementation of the provisions on the bank aims to strengthen the internal banking system in facing of increasingly complex risks.

Organization of Economic Cooperation and Development (OECD) developed a set of corporate governance principles. The basic principles of good corporate governance include transparency, accountability, responsibility, independence, and fairness, which aim to ensure the survival and the growth of sustainable enterprises.

One of the factors needed to create effective corporate governance, especially after the financial crisis in Asia, is the role of the board of commissioners. Macey and O'Hara (2003) states that the board has a very important role in a bank because of the difference of governance at banks with non-bank firms. The main reason for the difference is due to the importance of other stakeholders such as creditors' banks and regulators. Bank directors should be responsible not only to shareholders, but also to depositors, customers, and regulators.

Skully (2002) also stated that the role of the board is very important in the application of corporate governance since the passage of oversight by the board of commissioners will reduce the risk of taxpayer funds that can be used as a mitigation or to resolve a crisis. Implementation of good corporate governance can also play a role in controlling the lending practices on the part that still has a relationship with the bank.

The studies that have been done previously on the effect of the application of corporate governance are mixed results on the relationship between the compositions of the board of management with the company's performance. Most studies find no effect or a significant relationship between the presence of the management board and the company's performance (Bhagat and Black,1999; Hermalin and Weisbach, 1991). Eisenberg et al. (1998) found a negative relationship between board size and corporate performance.

However, Rosentein and Wyatt (1990) showed a positive relationship between stock prices and the proportion of responses independent board. Large board size is more effective when compared to a small board size (Dalton et al, 1999; Nasution and Setiawan, 2007). According to Andres, Azofra and Lopez (2005) the number of board members greatly influences the control and supervision activities.Xieet. al. (2003) found that the audit committee is an important factor to management control. Number of audit committee members' influences can be given to the company,the larger size of audit committees is expected to keep the bank in better performance.

While the study examined the effect of audit committee members is independent of the performance of bank (Nasution and Setiawan, 2007; and Li et al., 2008). The results revealed that audit committee members have a positive effect on firm performance. The independent audit committee is expected to improve the company's performance.

In carrying out the obligations and responsibilities regarding financial reporting system, the audit committee should hold meetings three to four times a year (FCGI, 2001). The more audit committee meetings conducted to improve the performance of the audit committee. The holding of regular meetings of the audit committee that is expected to improve the performance of the bank.

Audit committee members have knowledge of auditing and financial reporting support to the external auditor in disputes with management. The audit committee members in resolving disagreements between management and the external auditors require the knowledge and expertise in

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

the field of accounting. The existence of a dispute between the parties management with external auditors may affect the performance of the company, so that the company is expected to perform well.

The studies that examined the effect of audit quality on the performance of banks proves that the audit is a systematic process to obtain and evaluate the evidence objectively, related to assertions of economic measures to measure the level of concordance between assertions with established criteria and then communicating the results to the parties concerned. The results of the audit process are the auditor's report (auditopinion), which is a report on the fairness of financial statements in accordance with accounting principles generally accepted.

Agency theory is the role of the external auditor as a control tool that can be used to eliminate or at least provide a signal on oportunistic practices or fraud committed by management as earnings management (Jensen and Meckling, 1976; Watts and Zimmerman, 1986). Audit will reduce the information asymmetry between company management and stakeholders by allowing outsiders to verify the validity of the financial statements.

Good audit quality should be able to detect fraud committed by management like earning management and reporting actual performance of companies that do not lie to investors. Firm size could be expected to affect the quality of the audit. Because of the size of a large accounting, firm usually will not take the risk in the financial performance of the audit client, and tend to report the actual performance of the company, as well as to encourage companies to actually improve the performance of its operations. Varying results of previous literature is caused by the endogenous relationship,i.e the things resulted from the company itself (Hermalin and Weisbach, 1991), and causality (Kole, 1997) between board composition and corporate performance management.

The inconclusive results make it quite interesting to study in Indonesia and should also research important factors that supported the GCG practices in the banking sector, especially affecting the performance of the bank. More specifically this study will use three important components in the characteristics of the GCG board, audit committee, and audit quality will be linked to the level of the banking performance which is measured by using five financial ratios included in the ratio of CAMEL.

The problems in this study is to find out the effects of the bank's board of commissioners, the audit committee, the audit quality, and the corporate governance indicators towards the bank’s performance.

2.THEORETICAL REVIEW

2.1. Good Corporate Governance (GCG)

Syakhroza (2003) assumes that managers will act opportunistically by taking personal gain before the interest of shareholders. The agency theory arises because of the development of modern management science which shifts the classical theory, namely the rule that separates the owner of the company (principal) and the managers of the company (agent). As the company expanded, especially the more dispersed shareholders, the more agency cost incurred and the owner cannot exercise effective control of the managers who manage the company.

According to Jensen and Meckling (1976) potential conflicts of interest can occur between related parties such as between the shareholders of the company manager (agency costs of equity) or between shareholders and creditors (the agency costs of debt). According to their agency, cost includes three things, namely, monitoring costs, bonding costs and residual loss. Monitoring costs are an expense that is paid by the principal to measure, observe and control the behavior of agents in order not to deviate. These costs arise because of the imbalance of information between principal and agent. In certain situations, the principal allowing agents to spend company resources (bonding costs) to guarantee the agency will not harm him. However, there is a discrepancy between the agency decision-making and decisions that maximize welfare agency. Value of money is equivalent to reduction in welfare experienced by the principal is called residual loss.

The agency theory is difficult to apply because of many obstacles.So we need a clearer concept on how to protect the stakeholders.The issues relating to conflicts of interest and cost-agency will arise, so it develops a new concept which pays attention and regulates the interests of the parties associated with the ownership and the operation of stakeholders of a company, which is known as the concept of corporate governance.

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

According to FCGI (2001) notion of Good Corporate Governance (GCG) is a set of rules governing the relationship between shareholders, management companies, creditors, government, employees and internal stakeholders and other external relating to the rights and obligations or in the other words, a system that regulates and controls the company.

According to Rahmawati et al (2006), GCG is defined as a set of rules and principles such as fairness, transparency, accountability, independency, and responsibility, which governs the relationship between the shareholders, the management, the company (directors and commissioners), creditors, employees and other stakeholders relating to the rights and obligations of each party. Based on the definition or understanding of GCG, it can be concluded that a GCGis the system, processes, and a set of rules governing the relationship between the various interested parties (stakeholders). In the narrow sense, GCG is a relationship between the shareholders, the board of commissioners, and the board of directors for the achievement of corporate objectives.

The purpose of GCG is to create benefit for all interested parties. Theoretically, the implementation of GCG to enhance corporate value, by improving their financial performance, which may reduce the risk undertaken by the board of commissioners with decisions that benefit themselves and generally GCG can increase investor confidence (Tjager et al., 2003).

Darmawanti, Rahayu, and Khomsiyah (2004) stated that issue of Corporate Governance arises because there is a separation between the ownership and the management company (agency problems). The relationship between agency problems and capital owners in the management is the owner's difficulty in ensuring that the funds are invested in profitable projects.

Organization of Economic Cooperation and Development (OECD) develops the corporate governance principles, which is known as the OECD Principles of Corporate Governance thatare:

1. Transparency (disclosure of information), namely transparency in the decision-making process and openness in expressing material and relevant information about the company.
2. Accountability (accountability), the clarity of function, structure, systems, and corporate accountability so that organs are effective enterprise management.
3. Responsibility (accountability), i.econformity (compliance) in the management of the firm to the principles of healthy corporate and applicable legislation.
4. Independency (autonomy), which is a state where a professionally managed company with no conflict of interest and influence or pressure from management that is not in accordance with regulations and legislation in force and the principles of healthy corporate.
5. Fairness (equality and fairness), the fair and equal treatment in meeting stakeholder rights a rising under the agreement and applicable legislation

The principles of corporate governance as described above are realized inthe management ofthe company attempted to implement the following matters:

1. General Meeting of Shareholders
2. Openness andTransparency
3. Existence Independent Commissioner
4. The size of the Board of Commissioners
5. Audit Committee
6. Ownership structure

2.2. The Impact of Board of Commissioners on Bank Performance

Surveillance system in the company is divided into two types, namely the system of "two-tier" system and the "one-tier". In the limited company that embraces organ systems company with "two-tier" system board as well as in Indonesia, the company's general oversight role is performed by the board of commissioners, while the firm adherents of a "one-tier" system board, the supervisory functions is performed by organs known as boards of directors.

The studies that have been done previously on the importance of the implementation of corporate governance, especially in the case studies conducted by other countries, used the term to describe the board of directors' oversight function. One of the studies referenced in this research is research conducted by Pathanet al. (2007), which examines the size and independence of the board of directors and its influence on the performance of companies on a bank in Thailand. Thailand can be an area of research, which is quite good considering like Indonesia, in 1997 the country was also experiencing

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

severe financial crisis. In a study using a fixed effect panel models, it is known that there is a significant negative relationship between board sizes with the performance of banks in Thailand. This is consistent with the hypothesis that was made and showed that the size of the smaller board would be more effective in monitoring bank managers, while the board with a larger size are more prone to agencyproblems between the owner and the company that runs the operational company (manager).

The second result obtained from the study was the discovery of positive relationship between board independence on the banks in Thailand and the bank's performance. This suggests that independent directors perform better in a monitor on the bank (especially in Thailand), as independent directors also have a market reputation that needs to be maintained. These studies suggest banks can improve their performance by reducing the number or size of the board and add a few boards that are more independent.

Eisenberg, Sundgren, and Wells (1998) also found a negative relationship between board size with the performance of the company or bank. Similarly, Hermalin and Weisbach (2003) show that the smaller board size would be more effective and can provide benefit because it is easier to coordinate in it.Large board size is more effective when compared to a small board size (Dalton et al, 1999; Nasution and Setiawan, 2007). According to Andres, Azofra and Lopez (2005), the number of board members influences and controls monitoring activities. The larger board size is expected to supervise the management better, so as to improve the performance of the bank or company.

In line with this, Adams and Mehran (2003), and Belkhir (2005) state that, the U.S. Bank Holding Companies, found that the size of the board and its performance has a positive relationship. This study suggests that surveillance conducted by the board with a large number of members or more will have an advantage that will exceed the costs incurred. Thereby,positive relationship between board size and performance of the companies in the U.S can be explained due to mergers and acquisitions in the banking industry.

2.3. The Impact of Audit Committee on BankPerformance

Another important component that supports the implementation of GCG is the audit committee (FCGI, 2001). In accordance with the Decision of the Chairman of Bapepam Number: 29/PM/2004, the audit committee is a committee established by the board of commissioners to carry out the task of supervision and management of the company.

Xieet al. (2003) found that the audit committee is an important factor in the control of management. In that study, the average audit committee, which is owned by the sample companies,is 5 members in the range of 2 to 12 members. Number of audit committee members influences the level of influence that can be given to the company, the size of the larger audit committees are expected to keep the bank with better performance.

While the study is examining the effect of independent audit committee members towards the performance of the company or bank by Nasution and Setiawan (2007) and Li et al. (2008). From the results of their study it is revealed that independent audit committee members have positive effect on firm performance. With the independent audit committee is expected to improve the company's performance.

On the other hand, Alijoyo (2003) states that the audit committee must be transparent, must be in line with audit charter and annual programs of the audit committee which are then supported with regularity of audit committee meeting. In carrying out the obligations and responsibilities regarding financial reporting system, the audit committee should hold meetings three to four times a year (FCGI, 2001). The more audit committee conducted a meeting, the more improvedof the performance of the audit committee. The holding of regular meetings of the audit committee that is expected to improve the performance of the bank. Audit committee members who have knowledge of auditing and financial reporting support to the external auditor. The knowledge and expertise in the fields of accounting and auditing is required by members of the audit committee in resolving disagreements between management and the external auditors. The existence of a dispute between the parties management with external auditors may affect the performance of the company.

2.4. The Impact of Audit Quality on BankPerformance

Audit is a systematic process to obtain and evaluate the evidence objectively related to assertions

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

of economic measures to measure the level of correspondence between the assertions and established criteria, and to communicate the results to the parties concerned. The results of the audit process are the auditor's report (audit opinion), which is a report on the fairness of financial statements in accordance with generally accepted accounting principles (GAAP).

In terms of agency theory, the role of the external auditor is as a control tool that can be used to eliminate or at least provide a signal on opportunistic practices or fraud committed by management as earnings management (Jensen and Meckling, 1976; Watts and Zimmerman, 1986). Audit will reduce the information asymmetry between company management and stakeholders by allowing outsiders to verify the validity of the financial statements. The examined of nine studies and found that the audit reduces the positive bias of the earnings and net assets before audited.

Good audit quality should be able to detect fraud committed by management like earnings management and reporting actual performance of companies that do not lie to investors. Firm size could be expected to affect the quality of the audit because of the size of a large accounting firm usually will not take the risk in the financial performance of the audit client, and tend to report the actual performance of the company, so as to encourage companies to actually improve the performance of its operations.

Based on the analysis of previous studies, the hypothesis in this study is expressed as follows:

H_1 : The Board of Commissioners has an influence on the performance of the bank.
H_2 : The audit committee has an influence on the performance of the bank.
H_3 : Audit quality has an influence on the performance of the bank.

3. METHOD

To determine the effect of the independent variables, Board of Commissioners, the Audit Committee and Audit Quality Performance Bank on the dependent variable (CAR, NPL, LDR, ROA,and ROE) then set up a model of the Structural Equation Model(SEM) to test the hypothesis1 to hypothesis 3.

Meanwhile, the measurement model in this study is using Confirmatory Factor Analysis(CFA) which indicates latent variable measured by one or more observed variables. Research model using CFA areas follows:

Latent variables in this study are Board of Commissioners, the Audit Committee, Audit Quality, and Bank Performance. Board of commissioners is abbreviated to BC. This variableis measured using four indicators, namely: BC_1, BC_2, BC_3, and BC_4. Audit Committee, is abbreviated to AC. This variable was measured using the five indicators, namely: AC_1, AC_2, AC_3, AC_4, andAC_5. Audit quality, is abbreviated to AQ. This variable is measured using two indicators, namely: $AQ_1$and AQ_2. Performance of the Bank, is abbreviated to PB. This variable is measured using the five indicators, namely: PB_1, PB_2, PB_3, PB_4, and PB_5.

Variables observed in this study consisted of sixteen indicators consisting of:

1. BC_4 observed variables. BC_1 measured using board size, BC_2 measured using the proportion of in dependent directors, BC_3 is measured by using a number of meetings of the board of commissioners, and BC_4 measured using educational background commissioner.
2. AC_5 observed variables. $AC_1$is measured by using the number of audit committee, AC_2 measured using the proportion of independent audit committee, AC_3 measured using the number of audit committee meetings, AC_4 measured using audit committee members' experience working as an auditor, andAC_5 was measured by using a background education audit committee.
3. AQ_2 observed variables. AQ_1 is measured by using a dummy the size of the Public Accounting Firm conduct an audit of the banks that the sample in this study. If companies or banks audited by Big 4 accounting firm (large) then the high audit quality, but if the bank is audited by non Big 4 accounting firm (small) then the lower the audit quantity. AQ_2 is measured by using a dummy of the audit opinion provided by the external auditor.

The population was banks and the sample was randomly selected from the banks listed in Indonesia Stock Exchange (IDX) from 2009-2010. The data used in this study are obtained from anual reports and financial statements of the banks listed on the Indonesia Stock Exchange (IDX) in 2009-2010. Data are sourced from the official website of IDX(www.idx.co.id), and the official website of each

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

company. Data on board and audit committee sourced from annual reports (annual report) that the sample banks in 2009-2010.While the ratio of data to measure the performance of the banking CAMEL sourced from financial statements (financial report) banks that were visited in 2009-2010. To test the SEM model (Hairetal., 1998), we evaluate the level off it of the data through several stages, namely: overall model fit, measurement model fit, and structural model fit.

4. RESULT AND DISCUSSION

Based on the analysis of Table 1. the descriptive statistics for each variable in this study are as follows:

Table 1. Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
BC_1	30	3.000	8.000	4.000	2.5000
BC_2	30	.667	.750	. 500	.6552
BC_3	30	4.000	43.000	10.000	1.3607
BC_4	30	.000	1.000	0.330	.48918
AC_1	30	3.000	6.000	4.000	.38824
AC_2	30	.000	.750	.500	.6801
AC_3	30	2.000	16.000	13.000	7.8925
AC_4	30	.000	.667	.330	.3423
AC_5	30	.000	.667	.330	.2197
AQ_1	30	.000	1.000	.700	.50855
AQ_2	30	.000	1.000	.600	.49827
Valid N (listwise)	30				

1. Average number of BC_1 as measured by board size is 4 people. The minimum number is 3 people and maximum is 8 people.
2. Average BC_2 as measured by the proportion of independent directors is of 0.5. It means that the number of independent directors compared to the number of commissioners has the same proportions. The minimum proportion of BC_2 is0.667, and the maximum proportion is0.75.
3. Average BC_3 as measured by the number of meetings of the BC is 10 timesa year and it is equal to the number of meetings required by the government, while the minimum meeting of 4 times means that banks only conduct meetings 4 times a year, and the maximum meetings is 43 times means that there is a bank that held 43 meeting times a year. This is more than is required by the government.
4. Average BC_4 is measured using accounting educational background is 33%.It means that the members of the commissioners who have the accounting educational background are one third of the total number of commissioners. While minimum commissioners who have an accounting educational background is 0%. It means no member of the BC in the bank that has the accounting educational background. The maximum value of $BC_4$is 1 means that each member of the board of commissioners in a bank which is a sample of accounting educational backgrounds.
5. Average AC_1 as measured using the number of audit committee is at 4.00 means that on average most of the banks into the sample audit committee has a number of (external and internal) for 4 people, while the minimum value of sizedit at 3.00 means that there is a bank which has 3 members of the audit committee . While the maximum number of bank sizedit a sample of 6.00 means that there is a bank that has a number of audit committee members as much as 6 people .
6. Average AC_2 as measured using the proportion of independent audit committee is of 0.5 means the number of independent audits compared to the number of members of the audit committee as a whole has the same proportions. While the minimum value is equal to 0.667 means the sum of independent audit committee members compared to the number of members of the audit committee as a whole has a smaller proportion or fewer. While the maximum value of 0.75 means

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

the number of independent audit committee members as compared to the number of members of the audit committee as a whole has almost the same proportion.

7. Average AC_3 as measured by using the number of audit committee meetings are as many as 13 meetings in a year, while meeting minimum is 2 times in a year while the maximum value is for as much as 16 times more than is required by the government.
8. Average AC_4 as measured using the experience of audit committee members worked as an auditor is by 12:33 it means that the average member of the audit committee have accounting education background is 1/3 of the total number of members of the audit committee.
9. The minimum value is 0% means that no member of the audit committee of the bank that has the educational background of accounting. The maximum value is 0.667, which means that the number of audit committee members who have educational backgrounds accounting are 70% of the total number of members of the audit committee.
10. AC average 5 are measured using the educational background of the audit committee is at 33% meaning that the average member of the audit committee who has experience as an auditor is one third of the total number of members of the audit committee.While the minimum value is 0% means that no member of the audit committee of the bank who has experience as an auditor. The maximum value is 0.667 means that the number of audit committee members who have experience as an auditor 70 % of the total number of members of the audit committee.
11. Average AQ_1 is measured using a dummy the size of the Public Accounting Firm conduct an audit of the banks into the sample amounted to 0.70 means that most of the banks are being sampled in this study in audits by the Big Four accounting firm and part smaller audited by non Big Four accounting firm.
12. The average AQ_2 as measured using the audit opinion dummy is equal 0.60 meaning that most of the banks are to be sampled in this study obtain audit opinion "unqualified" of the external auditor.

4.1. Stages and Testing Results

1. Overall Suitability Model. Structural model in SEM analysis begins with testing the overall model goodness of fit is statistics from LISREL output (Hair et al., 1995). Overall summary of the critical value of the test match the overall model can be seen from the summary in Table 2 (attached).By looking at the overall results of estimation based on existing criteria, the overall values obtained are marginal. Therefore, from the above analysis to test the reliability of the overall model output is at marginal fit.
2. Compatibility of Measurement Model. To test the measurement model fit performed on each construct separately through the evaluation of the construct validity and reliability (Wijanto, 2006). The aim of this testing phase to ensure that the constructs used in this study met the criteria valid and reliable. The validity and reliability of each construct of the observed variables are shown in Table 3 (attached).Based on the data in the table it can be concluded that the standard factor loading of each observed variable is greater than 0.70 then the validity of each variable is good.
3. Compatibility of Structural Model. This analysis was conducted on the structural equation coefficients by specifying a certain level of significance. Analysis of the structural models test the hypotheses proposed in this study. For a significance level of 0.05, the value t of structural equation must be greater or equal to 1.96 or greater for a practical equal to 2 (Wijanto, 2008).

4.2. Structural Equation Models (SEM):

To prove H_1, H_2, and H_3 are as follows:

BP= 0.56*BC + 0.033*AC + 0.44*AQ,Errorvar.= 0.066 , R^2 = 0.93
(0.13) (0.100) (0.10) (0.057)
4.40 0.33 4.26 1.17

All coefficients have significant values, except for the Audit Committee of the latent variables (AC). This equation is an equation for the first hypothesis, the second and third. It can be concluded that the hypothesis of this research (H_1 and H_3) is proved significant. As for the H_2 results is proved in significant. H_2 cannot be proved from the descriptive statistics on the variables of audit committee

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

meetings. In addition ,of the results of this research shows that accounting education background and experience as an auditor does not have a significant impact on the performance of the audit committee on banking performance. To assess how well the coefficient of determination of the structural equation, it will be seen from the magnitude of R_2(Wijanto, 2006). Lisrel test results that can be seen in the Reduced Form Equation R_2 values obtained for structural equation in this study. R_2 values in our model are equal to 0.93, which means that the model is able to explain 93% of the change in the latent variable Bank Performance. Overall value to f the three hypotheses proposed in this study results can be summarized inTable 2.

4.3. Analysis of Testing Results

Based on the structural equation model, confirming that the commissioners proved significantly positive effect on bank performance. What it means is the greater control by the board of commissioners on banking operations, the higher performance produced by banks. Results of this study reinforce the results of previous studies that Rosentein and Wyatt (1990), Dalton et al. (1999), Nasution and Setiawan (2007).

Table2. T-Value forEachHypothesis

Hyp	Path	Estimation	t-value	Conclusion
1	BC→BP	0.56	4.40	Significant
2	AC→BP	0.033	0.33	Not Significant
3	AQ→BP	0.44	4.26	Significant

The followingpath diagram shows thestructuralmodelofLisrel

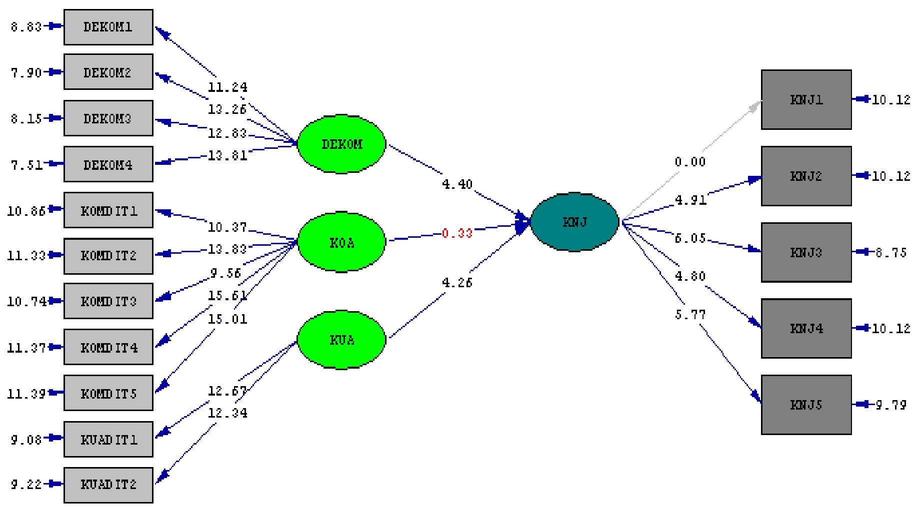

Fig. 2 SEM Diagram

The second hypothesis, which examined the effect of audit committee on banking performance results was not proven. These results are not in accordance with the results of previous studies (Herwidayatmo, 2000; Xie et al., 2003), although the direction (sign) is generated to support the results of these studies. This can be explained that the bank has a number of audit committee members very much and exceed the requirements stipulated by Bank Indonesia and Bapepam. There are also banks that conduct the audit committee meetings or gatherings up to 16 times in one year and it exceeded the meetings required by the governance.

The third hypothesis tested the effect of audit quality on bank performance results also proved positive and significant influence. It means that the greater a bank audit quality, the better the performance generated by the bank. These results reinforce the results of previous studies such as the study Jensen and Meckling (1976), and Watts and Zimmerman (1986).

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

5. CONCLUSION

This research is supported by numerous previous studies conducted related to the effect of the application of corporate governance on bank performance. The purpose of this study is to see how far the application of corporate governance can be good or bad effect on bank performance. This model uses the data of 30 banking companies. The results prove:

1. Board of Commissioners has a positive effect on bank performance. The better performance of the board of commissioners, the better performance of the bank.
2. The audit committee did not affect the performance of t he bank. Bank Indonesia and Bapepam can explain this from the bank that has a number of audit committee members that exceed the requirements stipulated. There are also banks that conduct the audit committee meetings or gatherings up to 16 times in one year and it exceeded the meetings required by the government.
3. Quality audit has a positive effect on bank performance. The better performance of the board of commissioners, the better the performance of banks.

REFERENCE

[1] Adams, R. &Mehran, H. (2003). Is corporate governance different from bank holding companies? FRBNY Economic Policy Review, 9, pp. 123-142.

[2] Alijoyo, F. Antonius. (2003). Keberadaan & peran komite audit dalam rangka implementasi GCG. Makalah dipresentasikan pada Seminar Nasional GCG–FKSPI BUMN/BUMD wilayah Jawa Timur, Surabaya-Indonesia tanggal 7 Mei 2003.

[3] Andres, P., Azofra, V., Lopez, F. (2005). Corporate boards in OECD countries: size, composition, functioning and effectiveness. Journal of Corporate Governance, 13 (2): 197-210.

[4] Belkhir, M. (2005). Board structure, ownership structure, and firm performance: evidence from banking. Available at SSRN: <http: //papers.ssrn.com/so 13/papers.cfm? paper= 604505>.

[5] Bhagat, S. & Black, B. (1999). The uncertain relationship between board composition and firm performance. Business Lawyer, 54, pp. 921-963.

[6] Dalton, Dan R., et. al. (1999). "Number of Director and Financial Performance: a Meta Analysis." Academy of Management Journal 42:6.

[7] Darmawanti, RahayudanKhomsiyah. (2004). Corporate Governance dan Manajemen Laba: Suatu Studi Empiris. Jurnal Bisnis dan Akuntansi, Vol5 No.1, 47-68.

[8] Eisenberg, T. Sundgren. D., & Well, M. (1998). Larger board size and decreasing firm value in small firms. Journal of Financial Economics. 48 (1), pp. 35-54.

[9] Forum for Corporate Governance in Indonesia. (2001). Peranan dewan komisaris dan komite audit dalam pelaksanaan corporate governance. Seri Tata Kelola Perusahaan (Corporate Governance), Jilid II. Edisi ke–2. Jakarta.

[10] Hair, J.F. Jr., Anderson, R.E., Tathan, R.L., dan Black, W.C. 1998. "*Multivariate Data Analysis*". Fifth Edition. Prentice-Hall International Inc.

[11] Hermalin, B. E. &Weisbach, M.S. (2003). Board of directors as an endogenously determined institution: a survey of the economic literature. FRBNY Economic Policy Review, 9, pp. 7-26.

[12] Jensen, Michael C. and William H. Meckling. (1976). "Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure." Journal of Financial Economics 3:4, pp. 305-360.

[13] Kole, S. (1997). The complexity of compensation contracts. Journal of Financial Economics, 43 (1), pp. 79-104.

[14] Lie, Jing, Richard Pike, danRoszainiHaniffa. (2008). Intellectual Capital Disclosure and Corporate Governance Structure in UK Firms. Accounting and Business Research, 38 (2): 137-159.

[15] Macey, Jonathan R., &O"Hara, Maureen. (2003). The corporate governance of banks. FRNBY Economic Policy Review.

[16] Nasution, MarihotdanSetiawan, Doddy. (2007). Pengaruh corporate governance terhadap manajemen laba di industry perbankan. Simposium Nasional Akuntansi X. Makassar. Ikatan Akuntan Indonesia (IAI).

[17] Pathan, Shams, Skully, Michael T., and Wickramanayake, J. (2007). *Board Size, independence and Performance: An Analysis of Thai Banks*. Asia-Pacific Financial Markets, Vol. 14, No. 3, pp. 211-227, School of Business, Bond University, Monash University – Department of Accounting and Finance.

[18] Rahmawati dkk, (2006). Pengaruh Asimetri Informasi Pada Praktek Manajemen Laba Pada Perusahaan Perbankan Publik yang Terdaftar Pada Bursa Efek Indonesia. Seminar Nasional Akuntansi 9, Padang.

[19] Rosenstein, S. & Wyatt, j. (1990). Outside directors, board independence, and shareholders wealth. Journal of Financial Economics, 26 (2), pp. 175-184.

International Journal on Economics and Social Sciences
Vol.1, No.1, January 2015, p. 25-30

[20] Skully, M.T. (2002). Banking and Corporate Governance: some prudential issues. Presented in Second International Conference on Banking and Finance in Greece.
[21] Syakhroza, Akhmad. (2003). "Teori Corporate Governance." Usahawan N0. 08 Tahun XXXII.
[22] Tjager, I. Nyomanet.el. (2003). Corporate Governance: Tantangan dan Kesempatan bagi Komunitas Bisnis Indonesia. PT Prenhallindo, Jakarta.
[23] Watts, R. L. and J.L. Zimmerman. (1986). Positive Accounting Theory. Englewood Cliffs, NJ: Prentice-Hall.
[24] Wijanto, Setyo Hari, 2006, *" Structural Equation Model (SEM) dengan Lisrel 8.7",* Catatan Kuliah, Pascasarjana Ilmu Manajemen, Universitas Indonesia.
[25] Xie, Biao, Wallace N. Davidson, Peter J. DaDalt. (2003). Earnings management and corporate governance: the role of the board and the audit committee. Journal of Corporate Finance 9: 295– 316.