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INFLUENCE OF FINANCIAL PERFORMANCE, VALUE OF COMPANY, CORPORATE GOVERNANCE MECHANISM FOR EXECUTIVE COMPENSATION

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***Abstract*—This study explains the effect of corporate performance, corporate values and corporate governance mechanisms on executive compensation. The sample is 16 firms listed in the manufacturing company for the period of 2010-2016 (112 research data).**

Results of F test show that the regression model used to determine the ROA variable (X_1), Tobin's Q (X_2), Institutional ownership (X_3) on Executive Compensation (Y) is jointly influential, so the proposed hypothesis is proved true. Result of F test 20,275 with p value (sig.) Equal to 0.000 which is much smaller 5% (0.05). The regression model in this study indicates that the independent variables are able to explain the Executive compensation by 36%. Based on t test result, it is found that ROA (X1) variable has no effect on execitive compensation, Tobin's Q (X2), Institutional Ownership (X3), which significantly influence Executive Compensation (Y).

Keyword—Return on Asset (ROA); corporate values (Tobin's Q); Mechanism of Corporate Governance (Institutional Ownership); Executive Compensation

I. INTRODUCTION

Compensation makes the attraction for a company, because it can improve company performance. One of the problems is the salary given to the executive. The high salary received by the executive but not matched by the rewards received by the shareholders over the invested capital is not as expected. One of the conflicts is the separation of ownership and management of the company. [1] The purpose of bringing the differences of interests between shareholders and managers.

The provision of compensation should be offset by a good performance or high, while the company's performance down the compensation obtained directors will decline. Company performance is one tool to measure compensation. Compensation is obtained from the company if the resulting performance is high. If the target performance is achieved, then the reward will be given. Performance measurement tools companies in this study using profitability ratios. A commonly used profitability ratio is Return on Assets (ROA). Return on Assets function to calculate the ratio of net income to total assets [2]. The return on asset (ROA) is higher then the more efficient the company's operation and the low return on asset (ROA) result can be caused by the number of unemployed company's assets. The company's success in improving its profitability can provide a positive signal for investors in making investment decisions.

Investors invest capital into the company by looking at the financial statements that the company's performance from year to year increase. Increased performance will also increase the value of the company and increase the company's profits. High corporate value affects high stock prices too, is considered an indicator for the market in assessing the company as a whole. High corporate value will make the market believe not only in the company's current performance but also on the future prospects of the company.

Increased profit and value of the company one of them with the supervision of investors.

There are no sources in the current document. [3] Argue that companies with good corporate governance mechanisms can resolve agency conflicts. Corporate governance mechanism that can monitor the performance of the company is the existence of institutional ownership. [4] Argue that institutional ownership enhances oversight of management and reduces managerial decisions. High supervision affects the ability of the executive to influence the compensation contract. Institutional ownership is the ownership of shares owned by institutions or institutions such as insurance, banks, investment companies and other institutional ownership [5]. The greater percentage of shares held by institutional ownership will make monitoring efforts more effective as they can control the opportunistic behavior of managers. Monitoring measures reduce agency costs because it allows firms to use lower debt levels. Research related to executive compensation in Indonesia until now is still kept confidential in the publication of financial reporting. In this study to see the compensation earned executives using short-term salaries include through total wages, salaries, benefits and bonuses. This study uses manufacturing companies because almost 30% of the total companies listed

on the Indonesia Stock Exchange is a company that originated in the manufacturing sector [6]. Manufacturing industry sector consists of basic industry and chemical sector, various industries and consumer goods industry.

II. TEORY STUDY AND HYPOTHESIS

Agency theory is used as the main basis explaining the relationship of performance, corporate value, corporate governance mechanisms, with executive compensation. According to [7] the agency theory explains the agency relationship between the owner of the economic resource and the manager who takes care of the use and control of resources within a company. Shareholders hire executives and wish to act on what shareholders want. The challenge that must be faced is to motivate agents to work as well as owners who want a profit. Principals want high profits and agents want high salaries or compensation [8].

[9] Argues: Company performance is one that is used to measure achievement in a certain period. In the agency theory revealed that the company's performance is positively related to the level of remuneration. [10] Explain that adequate compensation makes the agent (management) act in accordance with the wishes of the principal (shareholder). Compensation provided by the owner based on performance is as expenses incurred in the hope that the company's performance can experience an increase and vice versa compensation will be reduced if the company's performance decreases.

Return on Asset (ROA) is used in assessing whether or not a company is affecting investors to make decisions. The high ROA depends on the management of the company's assets by management that illustrates the efficiency of the company's operations. [11], [12] where this year's ROA is expressed as a significant factor in determining executive compensation.

Hypothesis: Return On Assets (ROA) have a positive effect on executive compensation

The point of view of the agency theory of the relationship between firm value and executive compensation is important to provide an incentive mechanism for a company that compensation has a direct effect as an appeal and executive retention. The relationship of executive compensation to company value because of this relationship gives executives an incentive to create wealth for shareholders [13]. [14] Argues that CEO compensation raises company value. According to research [15], [16] found that the higher the value of the company the greater the compensation of the CEO. [17], [18] revealed that firm value positively affects executive compensation.

Hypothesis: Corporate value positively affects executive compensation

From the point of agency theory according to [19], [20], institutional ownership can reduce agency conflict by monitoring managerial action. Institutional ownership is not only motivated and tasked to monitor CEO compensation and also has the expertise and resources [21]. Distribution of shares from institutional ownership can reduce agency costs as it encourages more optimal supervision of management performance [22]. In contrast to research [23], [24] states institutional ownership has a negative effect on executive compensation. Institutional ownership plays an active role in determining executive compensation [25]. A large degree of institutional ownership, the higher the level of compensation (Institutional ownership provides and establishes a better compensation policy.

Hypothesis: Institutional ownership positively affects executive compensation

III. RESEARCH METHODS

A. *Executive Compensation*

Compensation is salary plus bonus used as a compensation measurement tool. CEO compensation in Indonesia is not published, so the researcher uses CEO compensation data from compensation data provided to the board of directors through short-term rewards covering through total wages, salaries, benefits, bonuses. Thus executive compensation can be formulated as follows

Executive compensation = Salary + Bonus + Benefits

B. *Return on Asset (ROA)*

Return on Asset is used to measure the ratio that shows the company's ability to generate net profit after tax based on total assets owned by the company. The higher the ROA the higher the company's ability to generate profits. Return on Assets can be formulated as follows:

$$\text{ROA} = \frac{\text{Net profit}}{\text{Total Assets}}$$

C. *Company Value*

If Tobin's Q value is more than one (Tobin's Q> 1), the market value of the firm is greater than the value of the company's assets recorded in the financial statements means that the market judges both the firm and the company has an opportunity to increase its trading volume. If Tobin's Q is equal to one (Tobin's Q = 1), the firm's market value equals the value of the listed company's assets. If Tobin's Q value of less than one (Tobin's Q <1) means the cost of replacing assets is greater than the market value of the company. Company value is measured through Tobin's Q, which is formulated:

$$\text{Tobin's Q} = \frac{\text{(number of shares outstanding x Closing Price) + DEBT}}{\text{Total Assets}}$$

DEBT = (Total Debt + Inventory - Current Assets)

D. *Institutional Ownership/ IO*

Institutional Ownership (IO) is the majority shareholding of a company owned by an institution or institution (insurance company, bank, investment company, asset management and other institutional ownership). Institutional ownership can be formulated:

$$\text{Institutional Ownership} = \frac{\text{Shares owned by the institutional}}{\text{Total number of shares outstanding}}$$

E. Population, Sample and Sampling Method

The population used in this study is a manufacturing company listed on the Indonesia Stock Exchange (BEI) in 2010-2015. The data of Manufacturing Sector financial report from 2010-2015 amounted to 148 companies. Sampling method in this research using purposive sampling method that has a sample based on certain criteria. Data using cross section (one of the incomplete variables removes the whole sample year 2010-2016). The final data shows the sample per year of 16 companies x 7 Years. The data of this research are 112 sample.

F. Data Analysis Method

Data analysis method used regression was is the study of the dependence of the dependent variable with one or more independent variables. Data processor is assisted by using SPSS 19 [26].

The regression model in this study are as follows:

$$COMP = \alpha + \beta_1 \text{ ROA} + \beta_2 \text{ Tobin's Q} + \beta_3 \text{ INS} + e$$

IV. RESULT AND DISCUSSION

A. Descriptive statistics

Descriptive statistics used in this study are mean, median, maximum and standard deviation. The following table presents descriptive statistics for ROA, Corporate Value, Institutional Ownership and Executive Compensation

TABLE 1. DESCRIPTIVE STATISTICS

	N	Minimum	Maximum	Mean	Std. Deviation
Compensation	112	21.46	27.37	23.9247	1.28173
ROA	112	.00	.42	.1350	.10053
Tobin's Q	112	25.15	35.88	29.4307	2.64049
Institutional Ownership	112	.00	.98	.6054	.20615

B. Normality Test

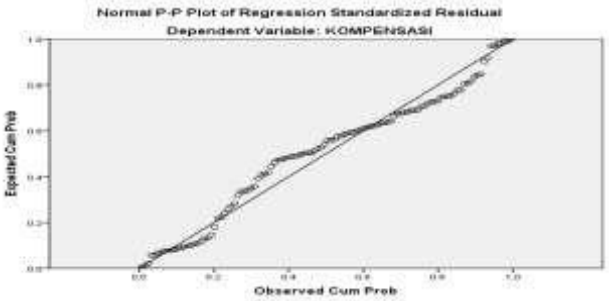

Fig 1. Normal P-P Plot of Regression Standart

Fig. 1 shows that the research data is normally distributed, that is spread along the diagonal line by not forming a certain pattern. It can be stated that the data of the research is normally distributed.

C. Hypothesis Test Results

TABLE 2. HYPOTHESIS TEST RESULTS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.600[a]	.360	.343	1.03930

The value of R Square is 0.343, which means that independent variables (ROA, Value of Enterprise, Institutional Ownership) are able to explain 36% of the dependent variable (Executive Compensation), while the rest of 64% is explained by other variables not included in the model investigated in this study).

D. Test Simultan (Statistic Test F)

TABLE 3. TEST SIMULTAN (STATISTIC TEST F)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	65.698	3	21.899	20.275	.000[a]
	Residual	116.655	108	1.080		
	Total	182.354	111			

F value of 20.275 with p value (sig.) Of 0.000 which is much smaller 5% (0.05). It means that there is a significant influence simultaneously (together) between independent variables to the dependent variable.

Based on the simultaneous test results above, can be formulated empirical model of test results as follows:

Y= 12,822 + (-4,394) ROA + 0,36 (Tobin's Q) + 1,540 (Institutional Ownership) + e

The direction (slope) of the relationship between Return on Assets (ROA) to CEO compensation shows negative, that is -4.394. The slope of Tobin's Q relationship to CEO compensation is positive, at 0.36. The direction (slope) of the relationship between institutional ownership of CEO's compensation shows Positive, that is 1.540.

E. Tests of Parsial (Statistical Test T)

Partial test is intended to provide confirmation and verification accepted or rejected testing the research hypothesis.

Table 4. TESTS OF PARSIAL (STATISTICAL TEST t)

Model	Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1 (Constant)	12.822	1.480		8.665	.000
ROA	-4.394	1.389	-.345	-3.164	.002
Tobins Q	.366	.050	.753	7.355	.000
Institusional Ownership	1.540	.539	.248	2.856	.005

Based on the table obtained value of ROA regression coefficient of -4.394, this proves that ROA has no effect on executive compensation. ROA data do not give high compensation to executive compensation ROA variable significance is equal to 0.002> 0.05 this proves that ROA has no effect, thus the hypothesis is rejected.

Based on the table obtained value of regression coefficient variable Value Company 0,36, this proves that the value of the Company does not affect the executive compensation. the value of the significance of the Company's Value variable is 0.000> 0.05 This proves that the Company Value has a positive effect, thus the hypothesis is accepted.

Based on the table obtained value of regression coefficient variable of institutional ownership of 1,540, this proves that the value of the Company does not affect the executive compensation. the value of the significance of the Company Value variable is 0.005> 0.05 This proves that institutional ownership has a positive effect, hence the hypothesis is accepted.

V. CONCLUSION AND RECOMMENDATION

This research explains about the influence of company performance, corporate value and corporate governance mechanism towards executive compensation in manufacturing industry company in 2010-2016.

1. Based on the table obtained value of ROA regression coefficient of -4.394, this proves that ROA has no effect on executive compensation. ROA data do not give high compensation to executive compensation ROA variable significance is equal to 0.002> 0.05 this proves that ROA has no effect, so **H1: hypothesis rejected**
2. Based on the result of hypothesis testing about the influence of Corporate Value (Tobin's Q) on Executive listed in Indonesia Stock Exchange can be concluded that variable of company value have positive and significant influence to Executive compensation. This is indicated by a significance level smaller than 0.05, so **H2: is accepted**.
3. Based on the result of hypothesis testing about the influence of corporate governance mechanism on Executive Compensation listed in Indonesian Stock Exchange, it can be concluded that the variable of corporate governance mechanism has positive and significant impact on Executive compensation. This is indicated by a significance level smaller than 0.05, so **H3: is accepted**.
4. Based on the test results simultaneously, the independent variables that exist together affect the dependent variable. This is indicated by a significance level of 0,000 that has met the criteria of being under 5%.
5. Based on the estimation results from the regression model in this study indicates that the independent variables are able to explain the executive compensation by 36%. While the rest is explained by other factors outside the model that is not included in this model that is equal to 64%. Other factors affecting Executive compensation are ROE, ROI, business segment, Dividend Payout Ratio, Dividend Yield, Company Size.

Suggestions for further research look for variables that have more influence than executive compensation. in this study is still less accurate because the variables used proxy from the calculation is almost the same then the result that affects together only 36%. Use other variables with different calculations such as ROE, ROI, business segment, Dividend Payout Ratio, Dividend Yield, Company Size and research data using all financial statements in BEI.

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