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The Moderation Effect of Corporate Governance Mechanisms on The Relationship Between Capital Structure and Company Performance (Empirical Study on Insurance Companies Listed on The Indonesian Stock Exchange 2019 – 2022)

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ABSTRACT

The significance of Company Performance extends to enhancing shareholder value, boosting employee morale, solidifying industry standing, intensifying market competition, fulfilling stakeholder expectations, and adhering to regulatory standards. Enhanced performance not only elevates the prosperity of shareholders but also augments the company's overall value. This study aims to investigate the impact of Capital Structure on Company Performance, emphasizing the moderating effect of Corporate Governance mechanisms. A quantitative approach is adopted, and the research relies on secondary data obtained from the Indonesia Stock Exchange (IDX) for this correlational analysis. The analysis encompasses annual report data from financial entities within the insurance sub-sector from 2019 to 2022, incorporating 68 datasets. The selection of these samples was conducted through a purposive sampling technique. SmartPLS 3.0 was used as this investigation's analytical instrument, employing Partial Least Square (PLS) path analysis. The outcomes indicated a minimal effect of Capital Structure on Company Performance. Moreover, the research ascertained that the effect of Capital Structure, as quantified by the debt-asset ratio (DAR), on Company Performance, assessed through the Return on Assets (ROA), remains insignificant even when considering the moderating variable of Commissioner's Size. The effect of capital structure (DAR) on company performance (ROA) with board size as a moderating variable is insignificant. 4. Capital Structure (DAR) on Company Performance (ROA) with Audit Committee Size as Moderating Variable's effect is insignificant.

***Keywords**: Corporate governance, capital structure, company performance*

INTRODUCTION

The Indonesia Stock Exchange (IDX) describes corporate governance (CG) as a framework established to guide the expert administration of corporations, adhering to the core values of transparency, accountability, responsibility, independence, fairness, and equality. Corporations must implement corporate governance to optimize their long-term value and efficacy, synchronize stakeholder interests, enhance transparency and accountability, efficiently manage risks, and adhere to pertinent laws and regulations.

The operational integrity of insurance companies is significantly influenced by effective corporate governance, which protects stakeholders' interests, including those of shareholders, policyholders, and employees. By fostering risk management, financial steadiness, and a culture of transparency and responsibility, it contributes significantly to the organization's well-being. Moreover, adherence to pertinent legislation and regulatory mandates is ensured, a mat par amount the heavily regulated insurance sector. In addition, good governance practices can help insurance companies build trust and reputation, which are essential for attracting and retaining customers.

By enhancing Corporate Governance practices, a company's value may be elevated through improved financial outcomes and diminished risks, particularly those stemming from self-serving decisions by the Board of commissioners. Strong corporate governance typically enhances investor trust and improves the company's overall performance. Governance can affect the relationship between a company's capital structure and performance in various ways.

Corporations utilize a financial strategy to obtain funding that incorporates multiple avenues, such as direct financing, contributions from external sources, and debt, collectively called the capital structure. The complex relationship between a company's operational efficiency and capital structure is influenced by several factors, among which corporate governance mechanisms are critical. Enhanced practices in corporate governance can bolster financial outcomes, subsequently impacting decisions related to the capital structure.

In light of the context above, scholars are motivated to undertake a study entitled **"The Moderating Effect of Corporate Governance Mechanisms on the Relationship Between Capital Structure and Company Performance (Empirical Study of Insurance Companies Listed on the Indonesia Stock Exchange (IDX) 2019 - 2022)"**.

LITERATURE REVIEW

Agency Theory

Agency theory is utilized to clarify and tackle disputes emerging between business proprietors and their delegates. Particularly relevant within the interaction framework between company shareholders and executives, this theory underscores the reality that alignment of interests needs to be consistently assured. Central to agency theory are the concepts of the principal-agent dilemma, which highlights the potential for agents to prioritize their interests over those of the principals and the imperative to mitigate agency loss, defined as the perceived detriment to the principal resulting from the agent's conduct. Approaches to diminish agency loss include linking compensation to performance, enhancing transparency, and implementing incentive schemes and rewards. Typical examples of principal-agent relationships encompass the interactions between shareholders and company management, special advisors and their clientele, and beets and property owners, as delineated by Eisenhardt (1989).

Company Performance

A company's achievement of predetermined objectives reflected in its performance can be quantified through diverse methodologies, notably financial ratios. Suciati (2021) emphasized the significance of various financial metrics, such as the Debt-to-Equity Ratio (DER), Current Ratio (CR), and Return on Asset (ROA).

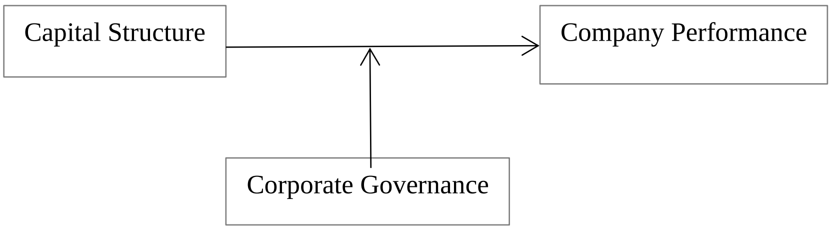
Capital Structure

Pandey (2001), a finance expert, characterizes the capital structure as the mix of sources for long-term financing, including debt securities, long-term debt, equity share capital, preference share capital, and reserves and surpluses.

Corporate Governance Mechanisms

The structure of Corporate Governance is defined by a complex network of interactions, systems, and practices put into place by a corporation's governing bodies, including the General Meeting of Shareholders (GMS), the Board of Commissioners, and the Board of Directors. These are designed with the dual aims of maximizing long-term shareholder value and considering the interests of additional stakeholders, all within the framework of existing regulations and norms (Sianturi, 2016). According to the National Audit Committee on Governance Policy's (KNKG) 2006 definitions, the Board of Commissioners plays a critical role within the corporate framework, entrusted with the collective duty of oversight and advising the Board of Directors to ensure compliance with the principles of Good Corporate Governance (GCG). However, it is explicitly stated that the Board of Commissioners should refrain from engaging in the company's daily operational activities. Article 1 of Law No. 40 of 2007 on limited companies mandates that the Board of Directors is entrusted with the governance and representation of the company, both within and outside of legal contexts, by the company's objectives as outlined in its articles of association. The directors must ensure that company operations adhere to all relevant laws and regulations, thereby establishing the company's legitimacy in the eyes of the public and its stakeholders. The "Auditing Handbook" by Davies and Parker (1995) describes an "Audit Committee" as a body primarily consisting of non-executive or independent members from the company's governing structure, charged with overseeing the auditing and financial reporting processes, among other duties. "Governing Body" denotes the assembly of directors, trustees, governors, or a comparable authority governing the organization. This delineation emphasizes the critical function of the Board of Commissioners, Board of Directors, and Audit Committee. These corporate entities are responsible for supervising and implementing robust corporate governance protocols within the firm.

Conceptual Framework



H1: Capital Structure affects company performance.
H2: The relationship between Capital Structure and Company Performance can be moderated by the size of the Commissioner.
H3: The size of the Board can serve as a moderating factor in the relationship between Capital Structure and Company Performance.
H4: The influence of Capital Structure on Company Performance can be moderated by the size of the Audit Committee.

RESEARCH METHODS

Type, Location and Time of Research

A core quantitative correlational study was cited from October 2023 through March 2024.

Population and Research Sample

1. This investigation focused on insurance companies listed on the Indonesian Stock Exchange, with information obtained from www.idx.co.id and the official websites of the respective firms.
2. Insurance companies that maintained their registration on the Indonesia Stock Exchange (IDX) between 2019 and 2022 were selected as the sample for this study.

Variable Operational Definition

Capital Structure

The metric for capital structure, known as the total debt to total assets ratio (TDTA), will be utilized by researchers, and it is determined using the following formula:

$$DAR = \frac{Total\ Liabilities}{Total\ Asset} \times 100\%$$

Description:
DAR = Debt to Assets Ratio

Company Performance

In measuring company performance, researchers use the following formula:

$$ROA = \frac{EAT}{\Sigma\ Asset} \times 100\%$$

Description:
ROA = *Return on Assets*

EAT = *Earnings After Tax*
Σ *Asset* = Total Assets

Corporate Governance Mechanisms

Several variables that can be used as indicators of corporate governance mechanisms include the amount of board size, commissioner size, and Audit Committee size. Measurement of these variables can be seen through the annual report.

Sources and Data Collection Methods

This study relies on secondary data to meticulously reassess established theories about the mechanisms of governance and the structure of capital in insurance companies listed on the Indonesia Stock Exchange. The approach to collecting data involves the documentation method, specifically employing the annual reports from the Indonesia Stock Exchange.

Data Analysis Method

Utilizing SmartPLS 3.0, the research adopts Partial Least Square (PLS) path analysis to streamline data, enhancing its interpretation and application.

RESEARCH RESULTS AND DISCUSSION

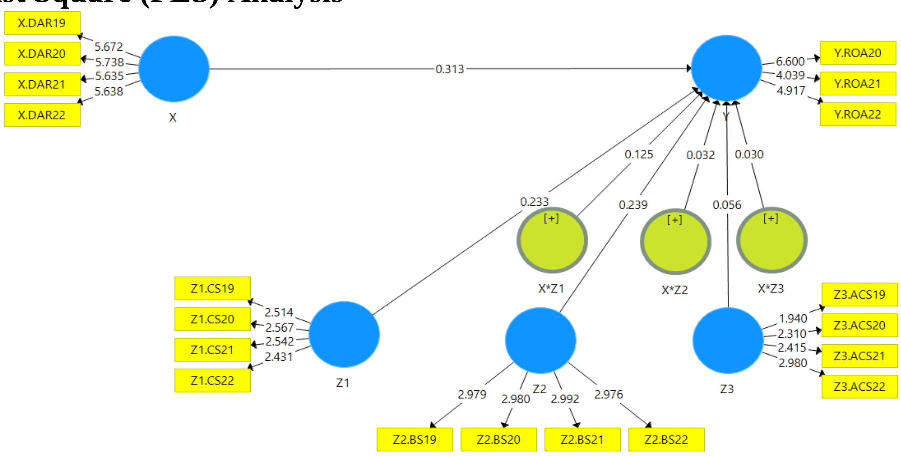
Research Results

Descriptive Statistical Analysis Results

Descriptive analysis determines the research variable's value, including capital structure, board size, commissioner size, audit committee size, and company performance.

1. The Capital Structure (X), the independent variable, is delineated by a spectrum extending from a low of 0.09 to a high of 0.91. The mean of this variable is reported as 0.5490, with a variation measured by a standard deviation of 0.208.
2. In the context of the moderating variable (Z1), the Size of the Commissioner spans from 2.00 at its lowest to 7.00 at its highest, with the calculated mean being 4.073, alongside a variability quantified by a standard deviation of 1.110.
3. For the second moderating variable (Z2), the size of the Board, the boundaries are set with a minimum of 2.00 and a maximum of 8.00. These variable averages 4.264, accompanied by a standard deviation of 1.451.
4. Audit Committee Size, which forms a composting variable (Z3), is a component marked by a minimum value of 2.00 and a ceiling of 4.00. The mean is established at 3.132, with a standard deviation of 0.453.
5. Company Performance (Y), the variable of dependence, spans a spectrum from -0.25 to 0.08 in its measurement. This parameter's average is noted, with the spread represented by a standard deviation of 0.048.

Partial Least Square (PLS) Analysis



The ventilation between variate bless is insignificant; the land value of Capitate al Structure(X) relation with any Performance(Y) is 0,313. Commissioner Size Modern capital structure is based on company performance and company performance. The Commissioner's size is ted in a value of 0.125. The relationship is also moderated by Board Size, which has an associated value of 0.032 (XZ2). Additionally, a value of 0.030 is attributed to the moderating influence of Audit Committee Size on the connection between Capital Structure and Company Performance (X*Z3).

R Square

R Square

Matrix | R Square | R Square Adjusted

	R Square	R Square A...
Y	0.421	0.208

Ghozali (2014) interprets the R^2 values of 0.67, 0.33, and 0.19 as indicative of "good", "moderate", and "weak" model performance, respectively. The R Square value of the Return on Assets variable is recorded at 0.421, indicating that factors such as capital structure, board size, commissioner size, and Audit Committee size explain 42.1% of the variation in company performance. This explanatory power is classified as "moderate". On the other hand, factors not investigated in this study account for the remaining 57.9% of the variance.

Hypothesis Test

Path Coefficients

Mean, STDEV, T-Values, P-Values | Confidence Intervals | Confidence Intervals I

	Original Sa...	Sample Me...	Standard D...	T Statistics (...	P Values
X -> Y	-0.332	-0.164	1.063	0.313	**0.377**
X*Z1 -> Y	0.316	0.243	2.534	0.125	**0.450**
X*Z2 -> Y	-0.048	0.301	1.513	0.032	**0.487**
X*Z3 -> Y	-0.052	0.023	1.704	0.030	**0.488**

Discussion of Research Result

Impact of Capital Structure on Company Performance

The research reveals a minimal impact of capital structure on corporate performance, resulting in hypothesis 1 being rejected.

Influence of Capital Structure (DAR) on Company Performance (ROA) with the Influence of Commissioner Size

The research results show that the commissioner size does not moderate the effect of capital structure (DAR) on corporate performance (ROA) Thu. Thus, thesis two is rejected.

Impact of Capital Structure (DAR) on Company Performance (ROA) Considering Board Size as a Moderating Factor

Research has been through the size of the Board needs to have the ability to moderate the relationship between capital structure (DAR) and corporate performance (ROA), leading to the dismissal of hypothesis 3.

Relationship Between Capital Structure (DAR) and Company Performance (ROA) with Audit Committee Size as a Moderating Factor

The conducted research findings indicate that the Audit Committee's size fails to act as a moderating factor in the link between capital structure (DAR) and corporate performance (ROA), which results in the rejection of hypothesis 4.

CONCLUSIONS AND SUGGESTIONS

Conclusion

This research aims to explore the moderating role of corporate governance mechanisms within the relationship between capital structure and financial performance. The outcomes of the analysis and discussion lead to several key conclusions:

1. The impact of Capital Structure on Company Performance is found to be negligible.
2. Moderate needs to be absent in Board Size regarding the relationship between Capital Structure and Company Performance.
3. No influence is observed from Commissioner Size on the link between Capital Structure and Company Performance.
4. The effectiveness of Audit Committee Size in altering the dynamics between Capital Structure and Company Performance is absent.

Suggestions

Some suggestions that researchers can convey based on the analysis that has been done are:

a. For Investors

Before making investment decisions, investors must conduct a thorough analysis of company performance. This entails a focused examination of the debt-to-asset ratio (DAR) as an indicator of capital structure alongside the mechanisms of corporate governance, which significantly influence and mirror a company's performance.

b. For Management

To optimize company performance, the primary goal is for managers to evaluate future investment prospects by contrasting closely associated internal financing options. This evaluation aids in formulating policies on how capital structure or leverage applies to company performance, considering corporate governance mechanisms as a moderating factor.

c. For Future Researchers

Future researchers are expected to deepen further the Debt Assets Ratio and Return on Asset theory, take research objects with cluster techniques, add research methods, and examine other financial variables that have a greater influence on company performance. It is hoped that future researchers can add references to this research.

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