

## GOOD CORPORATE GOVERNANCE AND HEALTH LEVELS OF SOES IN INDONESIA

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### Abstract

In this article, researchers will find out the effect of good corporate governance on the level of health of SOEs in Indonesia. Multiple regression analysis techniques were applied to a total of 139 observations in this study. Proxies are used to measure the level of health and GCG score of SOEs in accordance with regulations issued by the Ministry of SOE. The results of this study indicate that GCG measured by a commitment to the implementation of corporate governance, board of commissioners/supervisory board, information disclosure and transparency, and other aspects does not affect the level of health of SOEs Whereas, GCG measured by shareholders and GMS/capital owners and directors influences the level of health of SOEs.

**Keywords:** Good Corporate Governance, Health Level, SOEs in Indonesia.

### INTRODUCTION

The rapid development of technological advances has increased competition among companies, resulting in an increasing demand for sustainable corporate governance in a company as well as State-Owned Enterprises. Basri & Munandar (2009) stated that Indonesia has one structural problem that has long been systematically binding Indonesia to adversity, namely the weakness of the institutional framework. One of the steps chosen by the State of Indonesia to strengthen the economic institutional framework, especially in order to realize corporate governance, was the establishment of the National Governance Policy Committee (*Komite Nasional Kebijakan Governance/ KNKG*) in 1999. The basic principles and basic guidelines for implementing GCG contained in the GCG handbook were at the minimum standards to be followed up and explained in sectoral guidelines issued by KNKG (KNKG, 2006). This guideline is intended for all companies in Indonesia including state-owned enterprises. The formation of the KNKG then led to the establishment of the index of GCG measurement in SOEs.

In the ministerial regulation of State Owned Enterprises Number: PER-01/MBU/2011 article 44, it is stated that SOEs must measure the implementation of GCG in the form of an assessment. This assessment is a program carried out to identify the implementation of GCG in SOEs through both the measurement and implementation of GCG in SOEs that are conducted regularly. In addition, an evaluation (review) was also carried out to describe the follow-up to the implementation of GCG in SOE in the following year after the assessment. To be able to realize the assessment or measurement activities for the implementation of GCG, a Decree of the Ministry of State Owned Enterprises Number: SK-16/S.MBU/2012 was issued regarding

indicators/parameters for assessing and evaluating the implementation of good corporate governance in the State Owned Enterprises.

State-Owned Enterprises are the main players in the economies of countries in Asia so that the performance of SOEs has an important influence on the level of competition and economic growth of a country (OECD, 2016). SOE have a dominating role in several sectors and is a contributor to state cash, so it requires good management.

The performance of SOEs often gets unfavourable evaluations from the public. SOEs is seen as an inefficient business entity, where one of the causes is less optimal use of resources, full of involvement in corrupt practices, and low profitability (Riyanto, 2011). Even though, SOEs is one of the drivers of the national economy which has a considerable influence in realizing the welfare of society (Avianti, 2006). In Indonesia, several SOEs have succeeded in going public (listed), but other SOEs are still trying to improve their financial performance. Therefore, the proper implementation of corporate governance is expected to improve the performance of SOEs in Indonesia. One measure of SOE performance is the measurement of the level of health of SOEs whose provisions are contained in the decree of the Minister of SOEs Number: Kep-100/MBU/2002.

Research that examines corporate governance indexes on performance is Nofiyanti & Pur (2010) and Wati (2012) which use two different CG indices. Rina (2010) uses an index from FCGI (Forum for Corporate Governance in Indonesia) and Wati (2012) using the CGPI index. Rina (2010) found that there was no significant influence between good corporate governance and the financial performance of SOEs as measured by the ROI score based on the SOE Ministry regulations. Whereas, Wati (2012) found that good corporate governance had a significant effect on financial performance (ROE and NPM) in companies listed on the IDX which were included in the ranking list by the Indonesia Institute for Corporate Governance (IICG).

Furthermore, the research conducted by Nuswandari (2009) about the Effect of Corporate Governance Perception on Company Performance in Companies Listed on the Jakarta Stock Exchange produces GCG which positively significantly affect ROE and statistically does not affect market performance (Tobin's Q). Research conducted by Sayidah (2007) which examines the effect of GCG using CGPI score on company performance, states that the Quality of Corporate Governance does not significantly affect the company performance, whether measured by profit margin, ROA, ROE or ROI.

The existence of differences in the results of previous studies provides an opportunity for researchers to examine the effect of corporate governance on the performance of SOEs. This study will use good corporate governance as an independent variable which is then divided into 6 measurement indicators and the health level of SOEs as the dependent variable.

Along with the background that has been explained, this research will then describe the related literature and the development of hypotheses, the research methods used, the analysis and discussion of research results, conclusions and implications.

## **RELATED LITERATURE AND HYPOTESIS DEVELOPMENT**

### **Agency Theory**

Agency theory is an approach used to develop a conception of governance (Brennan, Niamh M; Solomon, 2008). Agency theory is a theory that focuses on the relationship between principal and agent, where one or more people (the agent) act as people who are trusted by individuals or a group of other individuals (the principal) (Lukviarman, 2016). In a company, shareholders are principals while company managers are agents.

Agents who have been given the authority to make decisions on behalf of the principal then do not necessarily do things as expected by the principal (Jensen & Meckling, 1976). In this case both the principal and the agent have their own interests, and the agent will not always act in the interests of the principal. This difference in interests is known as the agency problem. For this reason, a mechanism of separation of ownership and control is needed which then raises costs in order to overcome this agency problem, namely monitoring costs, bonding costs, and residual loss (Fama, 1980; Jensen & Meckling, 1976).

### **Good Corporate Governance and SOE Health Level**

One lesson that can be taken after the economic crisis that occurred in Indonesia is the application of the principles of corporate governance. The better the implementation of corporate governance mechanisms, the company will be in a good monitoring condition, so that it will improve the performance of the company concerned and can reduce the tendency for fraud to occur in a company.

Minister of SOEs Regulation Number: PER/01/MBU/2011 concerning Good Corporate Governance in Article 1 paragraph 1 stated that corporate governance is the principles that underlie a process and mechanism for managing a company based on legislation and business ethics. The application of the principles of corporate governance to SOEs is aimed at many things, starting from optimizing the value of SOEs in order to increase national and international competitiveness while ensuring the sustainability of the company, creating professional, efficient and effective SOEs governance, enhancing the function and independence of the company, prioritizing moral values and compliance with laws and regulations in every decision making, and having a sense of social responsibility towards the surrounding environment, contributing to the national economy, and developing a conducive investment climate. Improving the quality of the application of corporate governance means that the company has good monitoring activities, so that it can improve the performance/health level of the company which in turn can minimize the tendency for fraud to occur in a company.

The establishment of SOE is aimed at several things such as as a major contributor to national economic growth and State revenues, pursue profit, provide public benefits in the form of the provision of goods and / or services for the lives of many people, as a pioneer or take over for

sectors that cannot be managed by the private sector and cooperatives, and provide active guidance and assistance to weak economic entrepreneurs, cooperatives and communities.

To be able to fulfill the above objectives, a system is needed that can assess the ability of SOEs to achieve these goals. Therefore, the Minister of SOEs issued Decree Number: Kep-100/MBU/2002 concerning the assessment of the state of SOE's health, then the SOE minister set a regulation Number: PER-10/MBU/2014 concerning indicators of the rating of the state-owned financial services and fields insurance business and assurance services. The assessment carried out covers the assessment of financial, operational, and administrative aspects. These three aspects are considered to be able to describe the overall performance of the company. This assessment will be determined annually in the General Meeting of Shareholders (GMS) (or the minister of SOEs specifically for public companies (*perusahaan umum/Perum*)).

The assessment of this level of health is deemed necessary in knowing the condition of the company appropriately and measurably so that it can be determined whether the SOEs have competitiveness and conduct its business activities efficiently.

The existence of good corporate governance is expected to be able to increase the level of health, protect the interests of stakeholders and improve compliance with laws and regulations as well as generally accepted ethical values (Taruno, 2013). Indicators of GCG Assessment based on the decree of SOE Ministry of secretary Number: SK-16/S.MBU/2012 consists of 6 indicators that will be used as proxies in this study, namely 1). Commitment to sustainable implementation of good corporate governance; 2). Shareholders and GMS / capital owners; 3). Board of Commissioners / Supervisory Board; 4) Directors; 5). Information disclosure and transparency; 6). Other aspects. The following is the hypotheses that can be formulated for this study:

H1: Good corporate governance that is proxied by a commitment to the implementation of good corporate governance on an ongoing basis affects the level of health of SOEs.

H2: Good corporate governance that is proxied with shareholders and the GMS / capital owners affect the level of health of SOEs.

H3: Good corporate governance that is proxied by the board of commissioners / supervisory boards influences the level of health of the SOEs.

H4: Good corporate governance that is proxied by the directors influences the level of health of the SOEs.

H5: Good corporate governance that is proxied by disclosure of information and transparency influences the level of health of SOEs.

H6: Good corporate governance that is proxied with other aspects influences the level of health of SOEs.

**METHOD**

This study will examine the effect of good corporate governance on the level of health of SOEs. In this study will test the hypotheses that have been formulated in order to be able to explain the causal relationship between the available variables called the hypothesis testing method

**Population and Samples**

The population taken for this study is SOEs in Indonesia. Data on the number of SOEs that are listed on the Ministry of SOEs website is 115 so the population in this study is 115 SOEs. The sample in this study was taken from the Annual Report of SOEs which was published through the Ministry of SOE website and from the website of each SOE.

Sampling in this study uses a purposive sampling method, where researchers use the terms or criteria that have been adjusted, so that samples can be appropriate for the research objectives (Sekaran and Bougie, 2013). The conditions specified in this study are as follows:

- a. SOEs in Indonesia that have published financial reports during 2012-2016 are listed on the website of the Ministry of SOE or the website of each SOE.
- b. Financial statements that present all data and information such as GCG score and health level score of SOE that will be used in measuring variables and analyzing data for testing hypotheses in research.

This study uses secondary data sources, namely data that has been collected by data collection agencies and published to the data user community (Kuncoro, 2009). Secondary data used in this study consisted of financial statements of SOEs in Indonesia in 2012-2016, laws, and other regulations related to research objectives, especially those related to SOEs in Indonesia. The sampling technique uses purposive sampling method.

**Table 1**  
Sample Determination

Sample Criteria	Total
Number of SOEs in Indonesia until 2016	115
Number of SOEs that do not fit the criteria	(72)
The number of SOEs that fit the criteria	43
Data being sampled (43 SOEs x 5 years)	215
Incomplete data	(29)
Outlier	(47)
Number of final observations	139

**Measurement of Variables**

The dependent variable in this study is the level of health of SOE, while the independent variable is good corporate governance. The following is an explanation of the definitions of each research variable and its measurement basis.

The level of health of SOEs is assessed based on the performance of financial aspects, operational aspects and administrative aspects. The procedure for evaluating the state of health of the SOE is based on the decree of the Minister of SOE Number: Kep-100/MBU/2002 concerning the assessment of the health level of state-owned enterprises. SOEs in the performance assessment process are then differentiated into SOEs that are engaged in financial and non-financial services. SOE distribution is carried out because the valuation between SOEs engaged in financial services and non-financial services has a different valuation method. Non-financial SOEs are then differentiated into SOEs that are engaged in the infrastructure and non-infrastructure sectors.

The results of the performance assessment are in the form of SOE health level scores ranging from 0-100 which are attached to the SOE financial statements. The higher the level of health score, the better the level of health of SOE.

SOE Health Level = Total SOE health score

The obligation to measure the implementation of GCG in SOEs is contained in the Minister of SOE Regulation Number: PER-01 / MBU / 2011 dated August 1, 2011 article 44 paragraph 6. Subsequently, the Decree of the Ministry of SOE secretary Number: SK-16 /S.MBU /2012 is issued concerning indicators/parameters for assessing and evaluation of the implementation of good corporate governance in SOEs. Assessment is carried out on 6 aspects, namely 1) commitment to the implementation of good corporate governance in a sustainable manner, 2) shareholders and GMS / capital owners, 3) board of commissioners / supervisory board, 4) directors, 5) information disclosure and transparency, 6) other aspects. Each aspect consists of several indicators and parameters which will then be tested for application and each given a weight as the maximum score/score in each parameter, indicator, and GCG aspect. The sum of the weights from the six aspects will produce a score of GCG implementation between 0-100. The following are indicators of the GCG parameters tested:

**Table 2**  
Indicator of GCG Assessment

<b>Testing aspects / parameter indicators</b>	<b>Weight</b>
1. Commitment to the implementation of good corporate governance in a sustainable manner	7,00
2. Shareholders and GMS/capital owners	9,00
3. Board of commissioners/supervisory board	35,00
4. Directors	35,00
5. Information disclosure and transparency	9,00

6. Other aspects	5,00
<b>Total Score</b>	<b>100,00</b>

Measurements for each indicator that was used as proxy in this study were carried out by measuring the performance of each parameter indicator as follows:

$$GCG = \frac{\text{realization of weight achieved}}{\text{maximum standard weight to be achieved}} \times 100\%$$

### Research Design

To test the level of significance regarding the relationship between good corporate governance on the level of health of SOEs, multiple regression analysis is used with the following equation:

$$TK_{it} = \alpha + \beta_1 \text{Commit}_{it} + \beta_2 \text{GMS}_{it} + \beta_3 \text{Com}_{it} + \beta_4 \text{Dir}_{it} + \beta_5 \text{Trans}_{it} + \beta_6 \text{Other}_{it} + \varepsilon$$

Where:

HL = Health Level

Commit = commitment to the implementation of good corporate governance

GMS = shareholders and GMS / capital owners

Com = board of commissioners/supervisory board

Dir = directors

Trans = information disclosure and transparency

Other = other aspects

## ANALYSIS AND DISCUSSION

### Descriptive statistics

The results of table 1 present that the average health level of SOE (HL) has a score of 80.57 with the lowest score of 33.03 and the highest score of 97.22. These results indicate that the average level of health of SOEs is in the category of "Healthy", although there are several SOEs which a small portion are included in the unhealthy category as listed in the minimum value.

**Tabel 3**  
Descriptive Statistics

	N	Min	Max	Mean	Std. Deviation
<b>HL</b>	139	33,03	97,22	80,57	14,335
<b>Commit</b>	139	45,00	100,00	85,86	12,082
<b>GMS</b>	139	0,00	99,00	89,60	9,694
<b>Com</b>	139	0,00	99,00	86,83	12,477
<b>Dir</b>	139	69,00	100,00	89,34	5,842

<b>Trans</b>	139	38,00	99,00	82,37	10,927
<b>Other</b>	139	-20,00	100,00	32,10	40,905
<b>Size</b>	139	15,47	30,86	24,51	3,700
<b>ROA</b>	139	-0,09	0,51	0,06	0,076

Meanwhile the standard deviation of the health level of 14.335 means that the distribution of data varies considerably. For almost all GCG score variables, all indicators have an average of > 82%, where only the GCG score variable with other aspect indicators (Other) has a fairly low average value of 32.10 with the highest achievement of 100%, the lowest of -20% and standard deviation of 40,905.

### Regression Result and Discussion

Test the hypothesis in this study using multiple linear regressions. The regression results show the magnitude of the coefficient of determination adjusted R<sup>2</sup> which is 0.168. This figure shows that 16.8% of the variation in the level of health of SOEs in Indonesia is explained by the dependent variable of the good corporate governance, while the remaining 83.2% is explained by other reasons outside the model.

The F test results produce a significance level of 0,000. This probability value smaller than 0.05 implies that the regression model can be used to predict the health level of SOEs at a 5% significance level, which in other words good corporate governance is proxied by a commitment to the implementation of good corporate governance in a sustainable manner, shareholders and GMS / capital owners, board of commissioners / supervisory board, directors, disclosure of information and transparency, and other aspects jointly influence the level of health of SOEs.

**Table 4**  
Hypothesis Testing

<b>Dependent Var. : Health Level of SOEs</b>		
<b>Independent Var</b>	<b>Coefficient</b>	<b>Prob.</b>
<b>Commit</b>	-0,013	0,624
<b>GMS</b>	0,074	0,013
<b>Com</b>	0,186	0,195
<b>Dir</b>	-0,114	0,024
<b>Trans</b>	0,009	0,769
<b>Other</b>	-0,001	0,294
<b>Control Var.</b>		
<b>Size</b>	-0,026	0,905
<b>ROA</b>	-1,884	0,000
<b>Adj R Squared</b>	0,168	
<b>Prob (F stat)</b>	0,000	
<b>Observations</b>	139	

The results of the t test show the relationship of each independent variable to the dependent variable. The results for the first hypothesis, namely commitment to the implementation of good corporate governance in a sustainable manner, affect the level of health of SOEs rejected. This can be seen from the probability value of 0.624 where the value is above the 5% significance level. The results of this study do not support the results of previous studies stating that organizational commitment positively influences good corporate governance (Manik, 2014). Pratolo (2008) stated that the commitment of managers in the organization will support the application of the principles of good corporate governance and support the improvement of company performance. The results of this different study are due to the fact that in the five years period the implementation of GCG in SOEs which was sampled in this study has not consistently increased the level of health of SOEs.

Furthermore, the second hypothesis which states that shareholders and GMS / capital owners influence the level of health of SOE is accepted. This can be seen from the probability value of 0.013, which is smaller than the 5% significance level. The results of this study indicate that the GMS / shareholders / owners of capital that implement good corporate governance in SOEs dominated by the government influence the level of health of SOEs. The results of this study are not in line with the research conducted by Avianti (2006) which states that the disruption of the enforcement of the principles of Good corporate governance is caused by the dominance of government ownership in SOEs and this dominance can also lead to business decisions that are not profitable.

Likewise, the third hypothesis which states that the board of commissioners / supervisory board influence the level of health of SOE is also rejected. This can be seen from the probability value above 5%, which is equal to 0.195. Pujiningsih (2011) stated that the composition of independent commissioners had no effect on company performance and Rochman (2016) found that the frequency of board of commissioners meetings, the board of commissioner's background had no effect on company value and the composition of board of commissioners had a negative effect on firm value. The results of this study are not in line with previous studies that measured corporate governance mechanisms concerning independent commissioners judged by the size, proportion and frequency of board of commissioners meetings and stated that they were positively and significantly related to the performance and value of the company (Sarafina & Saifi, 2017).

The fourth hypothesis which states directors influence the level of health of SOEs is accepted. This can be seen from a small significance value of 5% which is equal to 0.108 with a negative coefficient. This finding supports the results of Nurulita (2015) which states that directors have a negative influence on the profitability of SOEs in Indonesia. The findings of this study imply that directors who work in accordance with the principles of GCG will increase the level of health of SOEs. The Board of Directors is one of the most important organs in making decisions for upholding GCG in a company.

The fifth hypothesis which states disclosure of information and transparency affects the level of health of SOEs rejected. This can be seen from the significance value of 0.769 which is of

greater than 5%. The results of this study do not support the findings of Siagian, Siregar, & Rahadian (2013) who found that there is a negative effect of disclosure on company value, where companies with low corporate value try to improve the company's image by providing good information disclosure. The results of this study did not prove the existence of a relationship between transparency and health levels. This is partly due to the obligation for SOEs to disclose information transparently by the government regardless of whether the SOE is healthy or not, because this is related to the decision making by the government in treating the SOE. Some SOEs that have low performance can be given funding support by the government in order to sustain the operation of these SOEs or other decisions to maintain the existence of SOE especially if the SOE has an important role for national economic development.

The sixth hypothesis which states that other aspects affect the health level of SOEs is rejected. This can be seen from the significance value above 5%, which is equal to 0.294. Other aspects of the indicators are assessed from whether the GCG practices of SOEs are examples or benchmarks for other companies or in fact the practice has violated the principles of GCG as stated in the general guidelines for GCG in Indonesia. The results of this study found that other aspects did not affect the level of health of SOE. Previous research has tried to examine the effect of corporate governance quality by taking a sample of companies included in the top 10 CGPI ratings (Corporate Governance Perception Index) but found no evidence that GCG quality had an effect on company performance (Sayidah, 2007). In addition, there are still many SOEs that score 0 on other aspects. This happens because the practice of GCG applied to SOEs cannot yet be used as a benchmark for other companies, especially SOE, in the form of companies that have not gone public.

Finally, the control variable in this study, ROA having a value of 0,000, has a negative effect and is significant at the 5% level. These results indicate that SOEs with healthy predicate have lower ROA values and vice versa. While the size control variable proved to have no effect on the level of health.

## **CONCLUSIONS AND IMPLICATIONS**

This study examines the effect of good corporate governance on the health level of SOEs whose measurements are based on regulations issued by the Ministry of SOE. The results of this study indicate that the first, third, fifth and sixth hypotheses are commitment to the implementation of corporate governance, board of commissioners / supervisory board, disclosure of information and transparency, and other aspects do not affect the level of health of SOEs. Meanwhile, the second hypothesis is that shareholders / GMS and capital owners have a positive influence on the level of health, besides that the directors have been shown to negatively influence the level of health of the SOE.

The implications of the results of this study are for regulators that it is necessary to develop or reconsider existing policies so that they can improve the efficiency and competitiveness of SOEs in the future.

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