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The Moderating Effect Of Earnings Management And Dividend Policy On Relationship Between Corporate Governance And Institutional Foreign Ownership

Arin Pranesti[1*], Indra Wijaya Kusuma[2]

Affiliation:
[1]Accounting Department, Universitas Negeri Yogyakarta, Yogyakarta, Indonesia
[2]Accounting Department, Universitas Gadjah Mada, Yogyakarta, Indonesia

ABSTRACT

This study aims to examine the effect of corporate governance on institutional foreign ownership with earnings management and dividend policy as moderating variable. Previous research tends to be done in developed countries. In addition, prior research that examined the relationship between corporate governance and foreign institutional ownership is relatively inconclusive. Although some prior studies have found a correlation between corporate governance and institutional foreign ownership, there has been no research that explains the causality relationship. This study uses a corporate governance index that formed through the results of factor analysis test. The results of statistical tests indicate that corporate governance can be used as a good signal to pursue external parties that imply the company that has a good oversight mechanism. Interaction testing results between earnings management and corporate governance imply that foreign institutional investors tend to rely on corporate governance signals. In contrast, the interplay of dividend and corporate governance policies shows significant results. Therefore, it can be concluded that companies that have good corporate governance and dividend policies can reduce the conflict of interest between agents and principals tend to attract foreign institutional investors to invest in the company.

KEYWORDS: Corporate governance; earnings management; dividend policy; institutional foreign ownership.

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***Correspondence:**
arinpranesti@uny.ac.id

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Department of Accounting
University of
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INTRODUCTION

Limited equity funding factor for domestic investors predicted to become the strongest factor in encouraging a country to liberalize its capital markets to foreign investors (Giannetti dan Koskinen 2010). The previous literature has documented that foreign investor investing in developing countries (including Indonesia) will face inherent characteristics in the country such as low minority investor protection (Leuz, Nanda, dan Wysocki 2003), the degree of fraud and corruption with political connections that relatively high (Leuz dan Oberholzergee 2006; Faccio 2010; dan Chen, Ding, dan Kim 2010), as well as low levels of disclosure (Leuz dan Oberholzer-Gee 2006). The reason for the limitations in knowledge and outreach on local conditions makes foreign investors highly sensitive to information relating to companies due to the high level of information asymmetry (Cao, Du, dan Hansen 2017).

The results of a survey conducted by McKinsey & Company (2002) showed that corporate governance plays an important role in global investor investment decisions. Although there is an agreement that there is a role of corporate governance and corporate accounting disclosure in consideration of investment decisions of institutional investors, there is a little research that requires further study of it (Chung dan Zhang 2011). In addition, Kim (2015) concluded that although some previous studies have found a correlation between corporate governance and foreign institutional ownership, there has been no research that explains the causality relationship.

Some studies that examine the relationship between corporate governance and foreign institutional ownership are mostly conducted in developed countries (Giannetti dan Koskinen 2010; Chung dan Zhang 2011; dan Bushee, Carter, dan Gerakos 2014) and in international contexts (Leuz et al., 2009). In the context of developing countries, research on corporate governance and institutional ownership have been undertaken in Malaysia (Wahab, How, dan Verhoeven 2008) and Jordan (Al-Najjar 2010) but has not been conducted in Indonesia.

When viewed from the institutional conditions in Indonesia, Indonesia has the characteristics of countries that support this research. According to Indonesia Stock Exchange (2015), the opportunities and benefits of investing in the Indonesian capital market had increased the attention of foreign investors which is marked by net purchases of foreign investors which reached the highest record in the history of 42.60 trillion rupiah in 2014. The fact is in contrast to the governance environment manage the company in Indonesia as the survey conducted by Gill, Allen, dan Powell (2010) on corporate governance in Asian countries (including Indonesia). The survey results report that Indonesia ranks 10th out of 11 countries on the overall indicator of corporate governance. It explicitly explains that Indonesia has poor corporate governance despite its efforts to improve enforcement by establishing an organization aimed at improving corporate governance (Kurniawan & Indriantoro, 2000).

If viewed from an accounting standpoint, the means used by firms to attract investors can be linked to signaling theory. The signaling theory explains how information asymmetry in the market can be reduced by providing more information as a signal from the insider to those who do not have more information or outsiders (Morris 1987). In the context of the capital markets, the company can choose the tools that are used as a signal to investors to invest their shares in the company. In this study, the signal predicted by institutional investors to consider investment decisions is through the disclosure of corporate governance (Chung dan Zhang 2011 dan Bushee, Carter, dan Gerakos 2014), earnings management (Leuz, Lins, dan Warnock 2009) and dividend policies to suit institutional investors (Bhattacharya 1979; Grinstein dan Michaely 2005; dan Chang, Kang, dan Li 2016).

Previous studies that examined the effect of corporate governance on the number of institutional ownerships showed relatively inconclusive research results. Research conducted by Chung dan Zhang (2011) dan Wahab, How, dan Verhoeven (2008) showed a positive correlation between corporate governance and institutional foreign ownership. On the other hand, there are other studies that showed opposite results such as research conducted by Bushee, Carter, dan Gerakos (2014) which found no significant evidence on the amount of institutional ownership with corporate governance mechanism. The inconclusive results of previous research motivated this study to offer an alternative factor influencing the ownership of foreign institutions, namely the existence of profit management and dividend policy in terms of agency theory and signaling theory.

From the above description, it can be concluded that this study is different from previous research which is to test whether there is the role of internal characteristics and corporate policies that can affect the decision of institutional foreign investors to invest in the company. Previous research that is not conclusive opens research opportunities to provide another opinion to explain the phenomenon with other explanations of earnings management and dividend policy. In addition, this study contributed to fill the main empirical gap in Indonesia where there has never been any specific test.

The agency theory explains the relationship between principals and agents in terms of separation of ownership and control (Jensen & Meckling, 1976) and the separation of control and policy-making functions (Fama & Jensen, 1983). Furthermore, if each party is a party to maximize utility it is not surprising that the agent does not always act in accordance with the expectations of the principal. In addition, the agent is deemed to have more information about the condition of the company than the principal causing the principal to issue an oversight board so that the agent's opportunistic actions can be minimized.

Healy dan Palepu (2001) conveyed that the challenge for every economy is how to optimize the allocation of savings on investment opportunities. Company (entrepreneur) will always try to attract investors (household saving) that are distributed widely to fund their business ideas. On the other hand, the agent is likely to act in his favor as being inefficient or choosing projects that are unprofitable to the principal (Morris, 1987). If that happens then the principal will lose confidence in the agent and cause the withdrawal of capital he gives to the agent. Therefore, a mechanism is needed to prevent agents not to act opportunistically by monitoring and controlling both internally and externally so that investors believe that the funds invested in the company are not misused.

The signaling theory is based on the assumption that insiders are more aware of the company's condition than the outsiders about the company's growth opportunities, the quality of corporate governance, and so on (Cao et al., 2017). Morris (1987) describes the capital market as a buying and selling forum. If the purchaser does not have specific information about a product, but there is a general perception of the product, then the buyer will assess the entire product at the same price-weighted from the overall common perception available in the market. It will cause a good product to be rated too low and vice versa, poor product will be overvalued (Akerlof, 1970). Morris (1987) said that the problem can be solved if the seller communicates the product information to the buyer by giving a signal which is not easily imitated by other sellers so as to increase the market price of products sold by the company.

If associated with the capital market, the company will provide a signal to potential investors in the form of information that can affect the decision of investors to buy shares offered. According to Hartono (2017), the information published by the company can be interpreted as a signal for investors in making investment decisions. Signals given by the company can be information that has been done in the past by management or information related to company activity in the period to come.

The development of foreign investment in Indonesia is marked by the issuance of legal rules that support the participation of foreign investors in the Indonesian capital market. Legal constitution that overshadowed foreign investment in Indonesia began from the issuance of the December 1987 Policy Package. Under that policy, foreign investors began to participate in the participation in the capital market, one of which is by reducing the cost of registration of emissions and also permission of ownership of maximum securities by 49% of overall emissions. In 1997 the government through the Minister of Finance of the Republic of Indonesia (1997) issued the Regulation of the Minister of Finance No. 455/KMK.01/1997 on the Purchase of Shares by Foreign Investors through the Capital Market which removes the limits of foreign investor ownership in Indonesia. The latest regulation governing the cultivation of foreign investors is Presidential Regulation No. 44 of 2016 on the List of Closed Business Fields and Opened Business Fields with Capital Investment Requirements issued by the Presiden Republik Indonesia (2016) which supports 100% foreign shareholding in certain industrial sectors. The regulation further supports the opportunities of foreign investors to invest in Indonesia.

Leuz, Lins, dan Warnock (2009) explained that the level of information asymmetry in foreign capital markets will affect investment decisions in two ways. First, information asymmetry will cause problems with adverse options when investors transact in foreign capital markets (Leuz et al., 2009). This will cause investors to tend to calculate that they will not get a comparable return when compared to the yield earned by local investors. Second, investments made in companies that do not have good governance will tend to have larger supervisory boards than companies with good corporate governance (Leuz et al., 2009).

Furthermore, Bushee, Carter, dan Gerakos (2014) conveyed that there are some incentives that encourage institutional investors to prefer companies with better corporate governance mechanisms:

1. Institutional investors have a great portfolio that straight-line to the magnitude of the boarding supervision of the companies invested.
2. There can be a relationship between corporate governance mechanism and superior corporate performance that not captured by other companies.
3. There are fiduciary responsibilities that bind to encourage institutional investors to choose companies with good corporate governance because it can reduce the possible negative impact on the actions of management fraud.
4. The reason for the liquidity of shares if at any time taken its capital contribution.
5. Institutional investors tend to look for companies that have a low risk so good corporate governance can be used as a way to reduce the risk.

The results of Bushee dan Noe (2000) also showed that institutional investors are more interested in firms with better disclosure levels so investors can predict future corporate operations. Research by Wahab, How, dan Verhoeven (2008) confirmed evidence that institutional investors choose companies with good corporate governance as measured by the corporate governance index. Kim et al. (2010) and Min dan Bowman (2015) also pointed out that improved corporate governance changes (especially in the election of foreign and independent commissioners) will increase the number of foreign ownership in South Korea.

Furthermore, McCahery, Sautner, dan Starks (2016) adding that investors will likely choose to sell off their stake in the company invested in shares does not have good corporate governance. Giannetti dan Koskinen (2010) also show that corporate governance affects investment allocation decisions of institutional investors.

From the above description it can be synthesized that foreign institutional investors will search, filter, select, and decide to invest in a company with good corporate governance because of its tendency to invest large amounts of capital in line with the amount of supervision cost incurred. Therefore, based on the hypothesis proposed in this study are as follows:

H_1 : Corporate governance has a positive effect on institutional foreign ownership

Research conducted by Sloan (1996) explicitly conveyed that the earnings consisting of the components of cash flows and accruals contain information that is reflected in the stock price. This indicated that accruals reported in the company's financial statements are the company's way of delivering to outsiders the company's future financial information. Ronen dan Yaari (2008) defined earnings management in a good sense if it can provide a signal for future value by providing a bridge of information asymmetry to external parties without having to understand the information in detail. On the other hand, earnings management is in a bad sense (truth distortion) when profit is the result of poor governance (Ronen & Yaari, 2008).

The accounting literature documented that earnings management reflects poor corporate governance (Healy dan Wahlen 1999; Klein 2002; dan Cheng, Lee, dan Shevlin 2016). Corporate governance is established to serve to control and oversee management to act efficiently. Earnings management viewed as an information conveyed to parties outside the company (outsider) and used as part of the consideration of investment decisions (Schipper 1989). Based on the signaling theory, earnings management is an accrual-shaped signal given to outside parties and can influence investors' decisions.

Accounting literature agrees that institutional investors are more capable than other investors, especially in terms of valuation of corporate activities and financial statements. This is confirmed by Balsam, Bartov, dan Marquardt (2002) which showed that institutional investors do not respond much to the discretionary accruals made by companies that are marked by low post-announcement drift. This implies that institutional investors will respond by not purchasing shares or withdraw previously invested shares at the time of the announcement or even before the earnings announcement when there is an indication of earnings management.

Based on the theory of signaling and previous research, this study argues that earnings management is one form of low corporate governance and is seen as a bad signal that is conveyed to investors. Foreign institutional investors who are sophisticated investors and face the lack of informed earnings projected by earnings management will tend to avoid investing in the company so that foreign institutional ownership tends to decline. In line with the above description, the proposed hypothesis is as follows

H_2 : Earnings management weakens the effect of corporate governance on institutional foreign ownership

The purpose of establishing corporate governance is to ensure that investors earn returns that match the performance of the company (Shleifer & Vishny, 1997). The return on investment is in the form of cash dividend. Through cash dividend payments the insider distributes the company's profits to the investor so that it can no longer use the company's profits to benefit itself (La Porta et al., 2000). Dividend payout is considered as a positive signal from the company as it describes the future earnings of the company, and the decrease of dividend payout can give a bad signal for the company (Tong & Miao, 2011).

Easterbrook (1984) argued that there is information contained in the distribution of cash dividends to investors. Management that distributes dividends is considered to meet institutional investors' expectations. In addition, dividend policy is considered to be a requirement of information content that causes the company to tend not to cut dividend payouts to signals to investors who imply that the company is committed to good corporate governance standards (Cao et al., 2017). The opinion was confirmed by Grinstein dan Michaely (2005) which indicateed that the dividend paying company is considered to comply with the prudent man rule. In addition, the company is also considered cautious and has financial stability. Therefore, based on the signaling theory, this study argues that dividend policy can be a good signal for foreign investors so that it can increase the ownership of foreign institutions in conjunction with good corporate governance. The proposed hypothesis is as follows:

H_3 : The dividend policy strenghten the effect of corporate governance on the institutional foreign ownership

METHOD

Sample Selection and Data Collection

The data used in this study is secondary data extracted and analyzed from the annual report of manufacturing companies listed on the Indonesia Stock Exchange in the 2014-2016 period. Sample selection criteria are as follows:

a. Companies that publish a complete annual report that is published officially including the financial information required by the researcher used as a measurement of research variables.

b. The Company has an accounting period ended on 31 December.

c. The Company did not announce stock split during the observation period.

d. Companies that do not stop their activities in the capital market and do not stop its operations during 2014-2016.

Operational Definition of Variables

The dependent variable of institutional foreign ownership is measured by using the ratio of the number of shares held by foreign institutional investors to the number of shares outstanding as used in the measurement of institutional foreign ownership in the research (Cao et al., 2017; Chung & Zhang, 2011).

The independent variables namely corporate governance are measured by aggregate indexes based on previous research by indexing corporate governance measures consisting of internal control mechanisms and external supervision. Internal supervisory mechanisms comprise aspects of the board of commissioners and audit committees whereas external audit mechanisms are proxied with audit quality. Prior to index aggregation, each component of corporate governance was tested first by using factor analysis to ascertain whether the element could be grouped into one aggregate index of corporate governance. The result of factor analysis will produce factors which are then grouped into one or several variable names to form an aggregate index of corporate governance. The higher the aggregate index of a company then it reflects the higher the quality of corporate governance.

The first moderating variable, namely earnings management, is measured using the conditional revenue model approach developed by Stubben (2010) which is estimated using the following model:

$\Delta AR_{it} = \alpha + \beta_1 \Delta R_{it} + \beta_2 \Delta R_{it}{*}SIZE_{it} + \beta_3 \Delta R_{it}{*}AGE_{it} + \beta_4 \Delta R_{it}{*}SQ\_AGE_{it} + \beta_5 \Delta R_{it}{*}GRR\_P_{it} + \beta_6 \Delta R_{it}{*}GRR\_N_{it} + \beta_7 \Delta R_{it}{*}GRM_{it} + \beta_8 \Delta R_{it}{*}GRM\_SQ_{it} + \varepsilon_{it}$ (1)

Information:

AR	=	Year-end receivables
R	=	Year-end income
SIZE	=	Natural log of total assets
AGE	=	Natural log of company age
GRM	=	Gross margin ratio (gross profit divided by sales)
GRR_P	=	Income growth rate (= 0 if negative)
GRR_N	=	Income growth rate (= 0 if positive)
_SQ	=	The square of the variable
ε	=	error

The second moderation variable is the dividend policy followed by *dividend payer* as a proxy of dividend policy which refers to research conducted by Baba (2009), Firth et al. (2016), dan Cao, Du, dan Hansen (2017). Measurement of dividend payer is to use dummy variable, code 1 for companies that pay cash dividend and 0 who do not pay dividend. The control variables in this study consist of four variables: *Book to market* (BTM), Company Size (SIZE) , *Leverage* (LEV) , and *Return on Assets* (ROA) referring to research conducted by (Bushee et al., 2014; Chung & Zhang, 2011).

Testing of the independent variable on the independent variable in this study was done by using multiple regression analysis *(multiple regression).* Each hypothesis will be tested with different research models. Hypothesis testing model in this study are as follows:

$IFO_{i,t} = \alpha + \beta_1 CG_{i,t} + \beta_2 BTM_{i,t} + \beta_3 SIZE_{i,t} + \beta_4 LEV_{i,t} + \beta_5 ROA_{i,t} + \varepsilon$ (2)

$IFO_{i,t} = \alpha + \beta_1 CG_{i,t} + \beta_2 EM_{i,t} + \beta_3 CG_{i,t}{*}EM_{i,t} + \beta_4 BTM_{i,t} + \beta_5 SIZE_{i,t} + \beta_6 LEV_{i,t} + \beta_7 ROA_{i,t} + \varepsilon$ (3)

$IFO_{i,t} = \alpha + \beta_1 CG_{i,t} + \beta_2 DP_{i,t} + \beta_3 CG_{i,t}{*}DP_{i,t} + \beta_4 BTM_{i,t} + \beta_5 SIZE_{i,t} + +\beta_6 LEV_{i,t} + \beta_7 ROA_{i,t} + \varepsilon$ (4)

Variable definitions:

IFO	=	The ownership of a sing institution is the proportion of shares owned by foreign institutions (in the form of percentages).
CG	=	Corporate governance is an aggregate index of the four proxy for corporate governance that is the proportion of independent board, the proportion of shares held by top management, the proportion of the audit committee, and audit quality proxied by the size of the external auditor.

EM	=	Earnings management is estimated by the conditional revenue model developed by Stubben (2010).
DP	=	dummy variable for company dividend policy (1 for those who pay cash dividend, 0 who do not pay cash dividend)
BTM	=	Ratio of book value of equity to market value of equity
SIZE	=	The total natural logarithm of the company's assets
LEV	=	Debt ratio to total assets
ROA	=	The profit-after-tax ratio before the exceptional component of an asset

RESULTS AND DISCUSSION

General Description of Sample

This research uses 3 years observation period that is from the year of 2014-2016. The reason for the 2014 election as the initial period of observation is due to consider the issuance of a good corporate governance *roadmap* by the Financial Services Authority, one of which is to suggest the entity to disclose the composition of share ownership in the company. Based on these rules, companies listed on the Indonesian Stock Exchange (IDX) disclose the proportion of ownership, including institutional ownership data required in this study. This study uses manufacturing company data because manufacturing companies are the largest companies listed on the IDX so that it is expected to reflect the general conditions of all companies on the IDX. Data were obtained through *hand collected* from company annual reports and BvD OSIRIS *database*. The following are details of the sample selection used in this study:

Table 1. Company Sample Selection

Criteria	Number of Company			Number of Observation
	2014	2015	2016	
IDX-listed manufacturing company	172	172	172	516
Manufacturing companies that do not publish financial reports during the year of observation	(20)	(20)	(20)	(60)
Companies that stop their operating activities in the capital market	-	-	-	-
Companies that declare stock splits during the observation period	1	1	7	(9)
Companies that do not have complete data regarding the variables used	(73)	(62)	(73)	(208)
Final Observation Total	78	89	78	245

Measurement of Corporate Governance Through Factor Analysis

Table 2. The value of KMO, Barlett, and Measure of Sampling Adequacy (MSA)

The to-		1	2	3	4
KMO value		0.613	0.640	0.648	0.659
Sig. Barlett		0,000	0,000	0,000	0,000
MSA value (*)	X1	0.323	0.283	-	-
	X2	0.576	0.590	0, 593	0.599
	X3	0.584	0.613	0.617	0.617
	X4	0.872	0.867	0.871	.898
	X5	0.745	0.735	0.749	0.776
	X6	0.410	0.411	0.410	-
	X7	0.160	-	-	-
Conclusion		X7 deleted	X1 deleted	X6 deleted	**Qualified**

(*) Description: X1 is the proportion of independent commissioner, X2 is the size of the board of commissioners, X3 is the proportion of the audit committee, X 4 is audit quality, X 5 is the board of commissioner of foreign board, X 6 is the meeting of the board of commissioners, and X7 is the expertise audit

By making an empirical estimate of the structure of the variables formed, factor analysis can be an objective basis for establishing aggregate indices or summations of several scales (Hair Jr. et al., 2014). Santoso (2017) and Hair Jr. et al. (2014) stresses that in the early stages of factor analysis, the most important consideration is the minimal value of the Kaiser-Meyer-Olkin (KMO) test of 0.50; significance in Bartlett test is $p \leq 0,05$, and the value of Measure of Sampling Adequacy (MSA) is more than 0.50. Summary of significance value of KMO test, Bartlett and MSA are shown in table 1.

The next factor analysis test is looking at the number of factors formed based on the eigenvalue. The factor analysis test showed that the eigenvalue exceeding 1.00 was only one factor with the eigenvalue of 2,454 with the variance percentage of 61.34%. Based on the factor analysis test above, it can be concluded that from 7 (seven) variables forming the proposed corporate governance, there are only 4 (four) variables that can be formed into a proxy of corporate governance in accordance with statistical tests. The variables in question are the size of the board of commissioners, the proportion of the audit committee, the quality of the audit, and the proportion of the board of foreign commissioners. Furthermore, the measurement of corporate governance is done by summing the multiplication of factor values loadings and Z-score each of these variables. Here is a common measurement of corporate governance:

$$CG_{i,t} = 0,921X1_{i,t} + 0,864X2_{i,t} + 0,618X3_{i,t} + 0,691X4_{i,t} \quad (5)$$

Variable Definitions:
X1: The size of the board of commissioners

X2: Proportion of audit committee
X3: Audit quality
X4: Proportion of foreign board of commissioners

Table 3. Descriptive Statistics

Panel A: Descriptive Statistics

Variables	**Min**	**Max**	**Mean**	**Std. Dev**	**N**
IFO	0.0008	0 , 975	0 , 449	0.284	245
CG	-4.06	8.45	0.01 0	2.47	245
EM	0 , 00	0 , 22	0.033	0.039	242
BTM	-94,724	18,181	0.611	8,742	245
SIZE	9,3001	26,291	19,162	4,274	243
LEV	-92,28%	96.13%	51.07 %	2 6.11 %	245
ROA	-54,87%	41.50%	3.38%	9.80%	245
Valid N (*listwise*)					240

Panel B: Sample Frequency of Dividend Policy

Dividend Policy	**Frequency**	**Percentage**	**Cumulative Percentage**
No (0)	146	59.6	59.6
Yes (1)	99	40.4	100.0
Total	245	100.0	-

Hypothesis Testing Results

Table 4. Regresian results

Variables	Predicted sign	Model 1		Model 2		Model 3	
		β	Sig.	β	Sig.	β	Sig.
Const		0.467	0,000 ***	0.429	0,000 ***	0.490	0,000 ***
CG	+	0.026	0,000 ***	0.023	0.015 **	0.009	0.419
BTM	-	0.007	0.483	0.005	0.586	0.007	0.463
SIZE	+	0.001	0.890	0.002	0.695	-0,001	0.856
LEV	-	-0,001	0.108	-0,001	0.170	-0,001	0.092 *
ROA	+	0.007	0.001 ***	0.007	0.002 ***	0.007	0.002 ***
EM	-	-	-	0.331	0.477	-	-
CG * EM	-	-	-	0.130	0.501	-	-
DP	+	-	-	-	-	-0.003	0.942
CG * DP	+	-	-	-	-	0.034	0,020 **
Adj. R^2		0.086	-	0.078	-	0.100	-
F Value		5,577	0,000 ***	3.907	0,000 ***	4,833	0,000 ***

Description: ***, **, * significant at 1%, 5%, and 10% level.

The regression result is showed in table 3. This study also conducts robustness check. Robustness testing in this research is done in two ways: (1) combining in one model and (2) converting the sample into balanced panel data. Table 4 shows the results of the robustness test to determine whether the model used in the study shows consistency after the change of the research model and the panel data sample changes. These results show results consistent with previous hypothesis testing. This reinforces the results of previous statistical tests which show that hypothesis 1 and hypothesis 3 are supported while hypothesis 2 is not supported.

Table 5. Robustness Testing Results

Variables	Predicted sign	Model Merged		Balanced Panel	
		β	Sig.	β	Sig.
Const		0.459	0,000	0.203	0.111
CG	+	0.062	0,000 ***	0.051	0,000 ***
EM	-	-0,032	0.925	-0.134	0.767
CG * EM	+	-0.005	0.980	-0.127	0.589
DP	-	-0,022	0.129	-0.002	0.204
CG * DP	+	0.011	0.019 ***	0.001	0.011 ***
BTM	-	0.006	0.512	0.010	0.327
SIZE	-	0.001	0.834	0.011	0,048 **
LEV	+	-0,001	0.128	0,000	0.781
ROA	+	0.006	0.006 ***	0.004	0.101
Adj. R^2		0.184	-	0.223	-
F Value		6,997	0,000 ***	5,455	0,000 ***
N		240		141	

The results of the statistical tests in Table 3 show that the first hypothesis is accepted at the level of significance of 1%. The results of this study are in line with research conducted by Wahab, How, dan Verhoeven (2008); Kim et al. 2010; Chung dan Zhang (2011); dan Min dan Bowman (2015) which shows that good corporate governance will attract institutional investors to invest in the company. As Chung dan Zhang (2011), point out, the higher the quality of corporate governance will be followed by an increase in the number of institutional investors. In additionKim et al. (2010) and Min dan Bowman (2015) also show that corporate governance designed in accordance with the interests of foreign investors will increase foreign investor confidence accompanied by an increase in the number of foreign institutions.

On the contrary, the results of this study contrast with research conducted by Leuz, Lins, dan Warnock (2009) stating that companies with poor state-level governance will tend to be avoided by foreign investors. The results of this study show that although at the country level, Indonesia has poor governance but foreign institutional investors will still consider corporate governance at the company level to invest in the company.

As Bushee, Carter, dan Gerakos (2014) explain that institutional investors will choose companies with good corporate governance primarily because of high supervisory fees. Therefore, to avoid excessive oversight board expenditure investors will tend to choose companies with good governance quality. In addition, foreign institutional investors face high levels of information asymmetry and tend to underinvest in foreign stocks as to avoid higher corporate risk compensation when compared to investing in domestic firms (Cao et al., 2017; Leuz et al., 2009; Min & Bowman, 2015).

Based on statistical test results, hypothesis 2 is not supported because the beta is positive and the significance exceeds 5% which is theoretically opposed to the proposed hypothesis. In this study, corporate governance that interacts with earnings management is not significant indicates that foreign institutional investors rely only on the signals of corporate governance mechanisms as a consideration of investment in investment companies but do not consider the earnings management undertaken by the company. This study supports the existence of signaling theory for earnings management with different explanations.

In the opinion of Schipper (1989) earnings management is seen as information that the company conveys to outsiders. It assumes that earnings management is a signal in the form of accruals over the company's cash flow conditions in the future. However, this study shows that foreign institutional investors do not consider much of the earnings management done by firms in Indonesia. This can be explained through research conducted by Siregar dan Utama (2008) which concluded that earnings management in Indonesia is a profit management with efficient rather than opportunistic type.

In addition, the study also confirmed the opinions expressed by Balsam, Bartov, dan Marquardt (2002). The accounting literature agrees that institutional investors are more capable of conducting the process of assessing the activity and financial statements of the company when compared to other investors. Discretionary accruals conducted by corporations are not much responded by institutional investors (Balsam, Bartov, dan Marquardt 2002) even up to the time of post-announcement drift. This indicates that foreign institutional investors do not respond to earnings management by firms in Indonesia because institutional investors who have better analytical capabilities than other investors can analyze that earnings management in Indonesia is efficient earnings management.

The results of this study are in line with research conducted by Baba (2009), Firth et al. (2016); Cao, Du, dan Hansen (2017). The results of this study indicate that foreign institutional investors will be interested in companies that pay dividends so as to increase foreign ownership in a company. The higher the dividend paid by the company will be the higher the number of foreign institutional ownership. Companies that distribute dividends can strengthen investors' consideration to investing in companies with good corporate governance. On the contrary, this study is not in line with research conducted by Vo (2015) which showed that foreign investors in Vietnam prefer companies that pay lower dividends. In addition, Vo (2015) also showed that when foreign investors become big shareholders, foreign investors tend to force managers to pay fewer dividends and maintain high profits to capitalize on future emerging market opportunities.

Another explanation of the relationship of dividend and corporate governance policy is explained by research conducted by Grinstein dan Michaely (2005) which showed that dividend-paying companies are considered to comply with prudent man rules. Grinstein dan Michaely (2005) explain that dividend payments made by the company suggest that the company has a cautious attitude in predicting future financial conditions. In addition, cash payer dividend companies also have a relatively stable financial history when compared to firms that do not pay dividends.

CONCLUSION

The results of this study indicate that the results are consistent with previous research that corporate governance is positively and significantly related to the ownership of foreign institutions. This shows that corporate governance is a good signal as a sign that management has managed the company in the interests of shareholders. In addition, dividend policy can strengthen the relationship between corporate governance and foreign institutional ownership. In contrast, earnings management is not statistically supported in influencing the relationship between corporate governance and foreign institutional ownership. The results of this study support agency theory and signaling theory used by companies to mitigate contractual relationships between agents and principals.

The implications of this research are expected to provide a new view of the company by making internal and external control mechanisms that can be used as a good signal to foreign investors. In addition, the dividend policy submitted by the company to investors has proven to be a mediating bridge of conflict between agents and principals. This can encourage companies to try to meet investor expectations by providing policies that are able to convince foreign investors to invest in Indonesia.

This study has several limitations that can be used as an improvement material for further research. Limitations of research and suggestions for future research are as follows: This research does not categorize institutional investors in several categories due to limited research data related to the types of foreign investors' shareholders disclosed by companies in Indonesia. Subsequent research is expected to categorize institutional investors such as those categorized by Bushee (1998) who divide investors into three types based on the period of stock ownership i.e. dedicated, quasi-indexer, and transient.

The measurement of corporate governance based on indexation of factor analysis only includes four corporate governance proxies. It may be possible that there is a lack of representation from the measurement of corporate governance. The use of corporate governance index may also use index indexation as used in the study (Brown & Caylor, 2006; Chung & Zhang, 2011). The use of earnings management estimates using discretionary revenue is a novelty in accounting research. In addition, discretionary income is only part of the income and income comprised. In further research, the use of profit management proxies such as Jones Model, Modified Jones Model, and Dechow Model can be used as an alternative to earnings management.

The measurement of dividend policy using possible dummy variable measurements cannot capture the magnitude of the dividend policy signals conveyed by the company. Further research can use other measures such as dividend yield or dividend payout ratio. The observation period used in this study is limited to three years. This is due to the limitations of research data relating to the ownership of foreign institutions disclosed by the company. The issuance of a good corporate governance roadmap by the Financial Services Authority that advises issuers to disclose the composition of shareholdings within the company was only issued in early 2014.

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