CHAPTER II

REVIEW OF RELATED LITERATURE

2.1.Theoretical Review

2.1.1. Agency Theory

According to the agency theory, the separation between ownership and management of a company can bring to a conflict. The occurrence of agency conflict is because, by the related parties, namely the principal (who gives the contract or shareholders) and the agent (who receives the contract and manages the principal fund) has conflicting interests (Bodroastuti,2009). According Jensen and Meckling (1976) agency relationship is a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. The purpose of the agency theory is to create efficiency and effectiveness to design the most cost-effective information systems.

To achieve company goals, the principal instructs the agent to manage the company as principal wants, but sometimes management as the agent does not do as the principal instructed. The principal can limit the divergences from his interest by monitoring costs designed to limit the activities of the agent. In some situation, the principal will pay the agent to avoid the agent does not take certain actions which harm the principal and to ensure the principal will be compensated if he does take such

actions. Agents will be more concerned with achieving better results than always obeying the orders of principals, thus there is agency conflict. Agency conflicts that arise between various parties that have various interests can complicate and hinder the company from achieving positive performance.

One of the causes of agency problems is the existence of Asymmetric Information. Asymmetric information is a condition when the agent and principle do not understand their decision. Furthermore, if the agent has information which supposed to inform to principal to take a decision, but the agent only keeps by themselves. Thus, agents and principals cannot decide by one of the two. There are 2 problems caused by information asymmetry, namely adverse selection, and moral hazard. Moral hazard is a problem that arises if the agent does not carry out things agreed upon in the employment contract. It occurs because of inappropriate decision making by the management on controlling the financial condition so then the use of money is not following company needs so financial distress will occur. Managers have negative impacts on the company because managers make decisions that are not based on the interest of shareholders. While Adverse selection is a condition where the principal cannot know whether a decision is taken by the agent is based on the information that has been obtained or occurs as an omission in the task. The managers try to manipulate the information that will provide to investors. Thus, the investors are not convinced with the quality of the

company because of not reliable and accountable information provided by managers then investors will give stock at a low price.

Good corporate governance is the tool for minimizing the conflict between agents and principals. Good corporate governance will regulate and control the company for adding the values to the company then interested parties or stakeholders can change the behavior of management. And good corporate governance will overcome the lack of information between agent and principal. Good corporate governance will give an impact on financial distress. The management better manages the company, financial distress will decline. While, if management cannot manage the company, financial distress will occur.

2.1.2. Financial Distress

Financial distress is a decline in financial condition as shown in negative profit or even bankruptcy. According to Platt and Platt (2002), financial distress is less precise than the legal actions that define proceedings such as bankruptcy or liquidation. Financial distress is a situation where cash flow is insufficient to cover current obligations (Altman, 1998). These obligations can include unpaid debts to suppliers and employees, actual or potential damages from obligation, and missed principal or interest payments under borrowing agreements (default). Technical default, the violation of debt covenant other than one specifying principal and interest payments, can be warning that distress is imminent. Brigham and Daves, (2002) they conclude that a company experiencing

financial distress is when the company's business conditions deteriorate to the point where the company cannot fulfill its financial obligations that begin when the company cannot meet the payment schedule or when cash flow projections indicate that the company will soon not fulfill its obligations. Elloumi and Gueyie (2001) Niarachma (2012) stated Companies that have experienced negative earnings per share (EPS) in the long term are included in financial distress.

Financial distress starts from liquidity difficulties (short term) as an indication of the lightest financial distress. And to know whether financial distress occurs when the company giving the negative operating profit, negative sales profit, merger, even bankruptcy.

There are several conditions of companies experiencing financial distress, as defined from the previous research by Emery & Finnerty (1997); Brigham (1997); and Gitman (1994) in Suciati (2008) cited by Niarachma (2012) as follows:

1. **Economic Failure**

   This condition happens if the company:

   1. It does not have enough income to cover the cost of production as well as its cost of capital
   2. The rate of return is lower than the level of the capital investment that can be generated from an outside party, e.g the deposit rate is greater than the return of investment (ROI)

3. The rate of return is lower than the cost of capital that needs to be paid by the company. The rate of return here is increasing the applicable credit interest rate.

2. Business Failure

The condition that represents a company or business which has a negative or low on their return of investment (ROI). In other words, when the company suffers an operating loss continuously, then the market value of the company will decrease. So, the cost of capital is larger than the return that supposed to be a company get. And it can be concluded the company is experiencing failure.

3. In Default

A company is considered in default if it is violated in terms of the loan agreement. Two different terms related to this condition as follows:

a. Technical Default

This condition happens if the debtor, in this case, the company, violates the loan agreement. The company experiencing a technical default does not always lead to a state of bankruptcy because the company is still able to continue its operation if the company tries to renegotiate with the debtor.

b. **Payment Default**

When a company is declared to be in payment default condition, they fail to fulfill the obligation to pay the interest or loan. The failure here is not the company unable to pay the debt, but the company is late to pay its obligation during its due date even though only passing one day. If the agreement is equipped with a grace period agreement (extension of the period), then the payment default condition occurs after that grace period.

4. **Insolvent**

Insolvent condition is a condition where the company is unable to fulfill its short-term obligations caused by the liquidity deficiency or they are unable to obtain net profit (loss)

a. **Technical Insolvency**

The condition where the company can not pay its liabilities during the maturity date because the company has a cash shortage. On the other words, a condition where the company's total asset is still greater than its total liabilities which means the company has problem on liquidity crisis. Technical insolvency is a temporary condition if the company can convert its assets in a certain period to increase cash to pay its obligation so the company will survive or able to get out of the threat of failure.

b. Bankruptcy Insolvency

The condition where the company has the book value from total liabilities is greater than the market value from total assets so the value of the company is negative. It means the values of assets are insufficient to pay back its debts. Bankruptcy insolvency also gives an indication of financial distress which is more serious than technical insolvency so it can be concluded as economic failure which leads to the liquidation of the company.

5. Bankruptcy

This condition is where the company already has a negative capital. The creditors can not do claims to the company unless the property of the company has been able to be liquidated. Making a declaration of bankruptcy is giving information to the stakeholders where the company is already bankrupt.

According to Almilia and Kristajadi (2003) cited in Niarachma (2012), the prediction of financial distress becomes the attention of many parties. The parties that use the model are:

a. Lenders

Research related to the prediction of financial distress has relevance to the institution lenders, both to decide whether to grant a loan and determine policies to monitor loan that has been granted.

b. **Investors**

The prediction model of financial distress can help investors during the assessment of the possible problem of a company in making payments of loans and interest.

c. **Regulators**

Regulators institution has the responsibility to monitor the ability of a company in paying debt and stabilizing the company. This led to the need for an applicable model to determine those aspects.

d. **Government**

The financial prediction model is also important for the government to formulate antitrust regulation.

e. **Auditor**

The financial distress prediction model is a tool for the auditor in making a going concern value of a company.

2.1.3. Good Corporate Governance

To overcome the economic crisis such as financial distress in Indonesia developing corporate governance. Good Corporate Governance (GCG) is needed to encourage the creation of an efficient, transparent and consistent market with laws and regulations. Corporate Governance (CG) was introduced by the Cadbury Committee in 1992 in a report known as the Cadbury Report. According to the Organization of Economic Cooperation and Development (OECD), GCG is a group of relationships

between the management of the company, the board, shareholders, and other parties that have shares in the company. Good corporate governance is a system to create good corporate management to raise value-added for stakeholders. And to achieve GCG in a company, there are five good corporate governance principles:

1. Transparency

To keep the objectivity of the company, Company has to give relevant information and easy to be accessed for taking decisions by stakeholders in the exact time that have been agreed between managers and stakeholders. Financial reports, company position reports, and institution ownership must be included in that information. Two indicators of transparency, information and company policies.

2. Accountability

Accountability is the one principle of corporate governance. Accountability is about the responsibilities of the managers as a result of managing the company and the performance of the company. The company has to give the information of structure, and company internal control as transparency and fairly. Furthermore, the company needs to be managed, measured, and the interest of shareholders.

3. Responsibility

Companies must comply with laws and regulations and carry out responsibility for society and the environment so that it can be maintained long-term business continuity and recognition as a good corporate citizen.

4. Independency

To achieve good corporate governance, the company must be managed independently and professionally without regulation which does not suitable for the company so each company does not intimidate by others. Independency needs to avoid conflict between stakeholders. The decision that made me need to be objective without interfered with others.

5. Fairness

Treatment fair and equal in fulfilling rights stakeholders arising from the agreement and applicable laws and regulations.

2.1.3.1. Managerial Ownership

Managerial ownership is the proportion of company ownership by management. In other words, managerial ownership is the percentage of share owned by the manager or director of the company. Managerial ownership is used to know how many shares that owned by the management in the certain company.

Jensen and Meckling (2017) stated that the greater the proportion of ownership by management, it will decline the using of resources as well as declining agency cost because of the different opinions between agent and principal and also the greater the responsibility of management in managing the company. This happens because managers who have involvement in the company through managerial ownership will also feel they own the company (sense of belonging) so that all decisions taken by managers will be carried out more carefully considering all the

consequences that occur due to decisions taken will also affect the manager. Therefore, management who owns shares in the company tends to develop strategies to improve company performance, especially long-term corporate performance such as integrating company with another company that considering improving long term sales. Thus, managerial ownership can increase the effectiveness of management working as well as decreasing financial distress that can make damage the company.

2.1.3.2. Institutional Ownership

Institutional ownership the proportion of stock owned by the institution. Several shareholders which are foreign companies, BUMN, insurance, bank or others that have big control over management and giving motivation for management to the optimization of company value so it will increase company performance and decrease financial distress. According to Setiawan et al (2017) on Kurniasati et al (2018), Institutional ownership is the total shares owned by an institution. Bodroastuti (2017), that institutional ownership will support control more optimal towards management's performance. It is because stock ownership represents a source of power that can be used to support the existence of management so with institutional ownership, agency cost can be minimized.

The higher institutional ownership shows the ability to control the management and the more efficient the utilization of assets so the potential of financial distress can be minimized.

2.1.3.3. Audit Committee

Ananto et al (2017) Audit Committee is a committee which has responsibilities to supervise financial report, control external audit, and also control the internal control system which can decrease the misconduct by the management. Audit committee competency is one factor that influences company performance. Audit committee help management about financial report and explanation, internal control system, and independent auditor.

Based on the Decision of the Directors of the Jakarta Stock Exchange No. Kep-315 / BEJ / 06/2000 stated that the membership of the audited committee at least 3 (three) members, the independent commissioner of the company and also as chairman of the committee audited, and another member is independent parties where at least one of them have the ability in the field of accounting and finance.

2.1.3.4. Independent Commissioner Board

Independent commissioner as *controveiling power,* which means the existence of an independent commissioner as supervisor of the long-term strategies decided by commissioner board for the future company. According to Kurniasati et al (2018), the Independent commissioner board is a board that has to supervise the company that is headed by the board of directors. An independent commissioner board is established to control and supervise the directors of the company so it will

raise appropriate decisions and keep the company safe from the possibility of financial distress.

2.1.4. Firm Size

Firm size describes assets owned by the company in a certain period. According to Rajan and Zingales (1995) in Putri and Merkusiwati (2014), Companies with large total assets indicate that the company is easier to do diversification because in this stage the company's cash flow has been positive and it is considered to have good prospects in a relatively long period. Besides, this also reflects that companies are relatively more stable and able to generate profits than companies with small total assets. The companies with small total assets indicated financial distress.

2.1.5. Sales Growth

The main goal of companies is to maximize the revenue and always increase the sales, in both the short and long-term (Baumol, 1959) cited by (Mohd Sam & Hoshino, 2013).

Sales growth affecting firm growth in the next future. Every company has to keep their finance in good condition in avoiding financial distress. Predicting financial distress is important for the company in order to preparing the company to control the finance in safe condition when facing financial distress. Sales growth will be showing the percentage of entire sales and previous sales

Bigger sales is better because the sales increase from year to year. It shows company activities have a good mark and company can

continuing their activities as well as decreasing the risk of financial distress.

2.2.Review of Previous Research Results

Some previous research have previously researched some studies related to good corporate governance, firm size, and sales growth towards financial distress.

Nindita & Moeljadi & Indrawati (2014) did a study entitled "Prediction on Financial Distress of Mining Companies Listed in BEI using Financial Variables and Non-Financial Variables". This study was conducted to examine if financial variables and non-financial variables can be used to predict the condition of financial distress in public mining companies listed in Bursa Efek Indonesia during period 2008-2009. The study population was all public mining companies listed in Bursa Efek Indonesia and there is no delisting during research period. The total sample used in this study were 13 companies. The financial variables used were current ratio, cash ratio, debt ratio, ROA, day sales in receivables ratio. This study used saturated sampling technique. The result of this study was, (i) current ratio, cash ratio, and debt ratio have significant effect on negative correlation coefficient in predicting financial distress of companies. (ii) non-financial ratios, managerial and institutional ownership do not give significant effect in predicting financial distress of companies.

Fathonah (2016) entitled "Pengaruh Penerapan Good Corporate Governance Terhadap Financial Distress". This study aimed to determine the impact of good corporate governance towards financial distress of property, real estate, construction companies listed in Bursa Efek Indonesia on 2013. The indicators which are institutional ownership, managerial ownership, Independent Commissioner Board, and Audit Committee. This study used purposive sampling and analyze using regression. The result of this study which are (i) independent commissioner board has significant negative effect towards financial distress. (ii) Institutional ownership has negative effect on financial distress. (iii) Managerial ownership has positive effect on financial distress. (iv) audit committee has positive effect on financial distress but not significant.

Sastriana & Fuad (2013) did a research entitled "Pengaruh Corporate Governance and Firm Size Terhadap Perusahaan Yang Mengalami Kesulitan Keuangan (Financial Distress)". This study aimed to examine the effect of corporate governance and firm size for firms experiencing financial distress at non-financial companies. The variables that used are: the number of board of directors, the number of independent board, institutional ownership, managerial ownership, and the number of audit committee members, and firm size. The research uses all firms that listed in Indonesia Stock Exchange (IDX) and the Indonesian Capital Market Directory (ICMD) period 2009 – 2012. The data were analyzed

using logistic regression model. And the result of this research showed the variable number of board of directors and audit committee members are significantly influence the company experiencing financial distress. While independent board, institutional ownership, managerial ownership and firm size do not have significant effect of companies financial distress.

Jamal & Shah (2017) entitled "The Impact of Corporate Governance on the Financial Distress: Evidence from Pakistani Listed Companies". The study intends to assess how corporate governance affects the financial distress in non-financial listed companies in Pakistan. It used sample of 53 companies was obtained from non-financial institutes listed in Pakistani Stock Exchange. To analyzed used regression model to explain these variables which are size of board, composition of board, audit committee independence and duality of CEO. And the findings showed the size of board, composition of board and CEO duality has positive effect on companies.

Witiastuti & Suryandari (2016) did a research entitled "The Influence of Good Corporate Governance Mechanism on the Possibility of Financial Distress". This research aimed to determine the effect of good corporate governance mechanism on the possibility of financial distress. In this research, the variables used managerial ownership, institutional ownership and independent commissioner. The sample contains 121 manufacturing companies listed on Indonesia Stock Exchange (IDX) period 2011-2013. Purposive sampling method was use to selecting

sample for 22 companies, so the unit of analysis was 66. The method of data analysis used descriptive statistics and logistic regression. The findings are (i) the managerial ownership, institutional ownership and independent commissioner do not influence significantly on financial distress.

Pramudena (2017) did a study which has title "The Impact of Good Corporate Governance on Financial Distress in the Consumer Goods Sector". The success or failure depends on the corporate governance of the company. So this study aimed to identify the relationship between the existence of good corporate governance and the profitability of financial distress. This study used secondary data that obtained from annual report period 2009 – 2014. The samples are consumer goods manufacturing companies that are listed on Indonesia Stock Exchange (IDX). 10 samples were use. The method of analysis used multiple linear regression. The result of this research that institutional ownership and managerial ownership adversely affect the possibility of financial distress. While, the proportion of commissioners and the number of board directors have positive effect on possibility of financial distress.

Murhadi & Tanugara & Sutejo (2018) entitled "The Influence of Good Corporate Governance on Financial Distress" which aimed to analyze the influence of good corporate governance (GCG) and to create a bankruptcy prediction model in financial distress. The sample used non-financial sector companies listed on Indonesia Stock Exchange (IDX)

period 2011-2015. This study used quantitative by using logistic regression model. The final sample used were 337 companies. The findings of this study are the proportion of independent outside directors, audit opinion, size, and ownership are significant of financial distress.

Ananto, Mustika, Handayani (2017) entitled "Pengaruh Good Corporate Governance (GCG), Leverage, Profitabilitas dan Ukuran Perusahaan Terhadap Financial Distress Pada Perusahaan Barang Konsumsi yang Terdaftar di Bursa Efek Indonesia. This study was conducted to examine the effect of Good Corporate Governance (GCG), Leverage, Profitability and Size of the Company's Financial Distress in Consumer Goods Company listed in Indonesia Stock Exchange. The indicator using Model Modified Altman Z Score and the method to hypothesis testing using multiple linear regression test. The sample were consumer goods company listed in Indonesia Stock Exchange from 2011-2015. Based on criteria, the sample obtained 22 companies. The findings showed that profitability and leverage affect financial distress. Meanwhile, institutional ownership, board size, the size of board of directors, independent board size, the size of the audit committee and the size of the company does not affect financial distress.

Rianti and Winwinyadiati (2018), did the research entitled " The Influence Firm Size on Financial Distress: A Research on Agricultural Companies Listed in Indonesia Stock Exchange. The purpose is to analysis the influence of firm size on financial distress in agricultural companies

listed in Indonesia Stock Exchange period 2012-2014. The proxy of financial distress and firm size that used were Altman Z's score, net profit margin, cash ratio and natural logarithm total assets. The sample obtained from Indonesia Capital Market Directory (ICMD) from 2012-2014. 18 companies were obtained as a sample. The method used multiple regression analysis. And the result is showed that firm size has effect but not significant towards financial distress.

Hidayat & Meiranto (2014) did the study entitled "Prediksi Financial Distress Perusahaan Manufaktur di Indonesia. This study aimed to investigate the effect of financial ratios to predict probability of financial distress in the company. The indicators that used were leverage ratio, liquidity ratio, activity ratio, and profitability ratio. The population using companies listed on the Indonesian Stock Exchange period 2008 – 2012. Based on purposive sampling method, the samples obtained 59 companies in the period 2008 – 2012. To measure the criteria of financial distress by using interest coverage ratio and analyzed using logistic regression. The result showed that leverage ratio (debt ratio), liquidity ratio (current ratio), and activity ratio (total asset turnover ratio) were financial ratios have significant value to predict financial distress in company, while profitability ratio (return on asset) is only financial ratios which not significant to predict financial distress in company.

Triwahyuningtias & Muharam entitled "Analisis Pengaruh Struktur Kepemilikan, Ukuran Dewan, Komisaris Independen, Likuiditas

dan Leverage Terhadap Terjadinya Kondisi Financial Distress (Studi Pada Perusahaan Manufaktur Yang Terdaftar Di Bursa Efek Indonesia Tahun 2008 – 2010). The purpose of his research is to prove the effect of ownership structure, board size, independent board of commissioners, liquidity and laverage with financial distress. The population was come from manufacturing sector at Indonesia Stock Exchange which published in financial report from 2008 – 2010. And the sample obtained 34 companies and obtained 102 data observation. This research used logistic regression as an analyzing instrument. The method that used consist of descriptive statistic, fit model test which used G test, Hosmer & Lemeshow's test and Cox & Snell;s R Square and Nagelkerke R Square and to test the coefficient of variables this study used wald test. The findings of this study showed that ownership structure, director size, liquidity and leverage have significant impact on the probability of firm experienced financial distressed. This research failed to prove effect of commissioners' size and independent board of commissioners with probability of experiencing financial distress.

Kurniasanti & Musdholifah (2018) entitled "Pengaruh Corporate Governance, Rasio Keuangan, Ukuran Perusahaan dan Makroekonomi Terhadap Financial Distress (Studi Pada Perusahaan Sektor Pertambangan yang Terdaftar di Bursa Efek Indonesia Tahun 2012 – 2016)". This study aimed to determine the factors that affect the financial distress companies in Indonesia mining sector. the dependent variables

which are board of commissioners, managerial ownership, institutional ownership, audit committee, and independent commissioner, financial ratios (profitability, leverage, liquidity, and efficiency) firm size. The sample using 17 Indonesian mining sectors selected using purposive sampling period 2012 – 2016. Data analysis technique using logistic regression. The result showed return on asset and asset turnover negatively asset on financial distress. While, board of commissioners, managerial ownership, institutional ownership, audit committee, independent commissioner, leverage, liquidity, firm size, inflation and interest does not affect on financial distress.

Hanifah & Purwanto (2013) entitled "Pengaruh Struktur Corporate Governance dan Financial Indicators Terhadap Kondisi Financial Distress". This study is to examine the impact of corporate governance structure and financial indicators financial distress. The indicators that used are size of the board of directors, the board size, independent commissioners, managerial ownership, institutional ownership, and the size of the audit committee and the financial indicators use liquidity, leverage, profitability, and operating capacity. The population from the manufacturing companies listed in Indonesia Stock Exchange period 2009 – 2011. Based on purposive sampling method, the samples obtained 45 companies' period 2009 – 2011 thus obtained 135 observations. This study used logistic regression as a data analysis tool. The result of the study showed the director size, managerial ownership,

institutional ownership, leverage and operating capacity have significant impact in financial distress.

Bodroastuti (2009) entitled "The Influence of Corporate Governance Structure to Financial Distress". This study was to examine the most influence variables of corporate governance structure on financial distress. The samples of 19 companies listed in Indonesia Stock Exchange. Thus, by using 95 observations during 2003 – 2007. It chosen by purposive sampling. The result of research showed that variables of corporate governance structure that influenced financial distress were the number of board of directors and the number of commissioners, and other not influenced.

Overall, the previous research shown in the Table 2.1 below

Table 2.1

No	Research Title & Researcher	Variable	Method	Result
1	Nindita & Moeljadi & Indrawati (2014) "Prediction on Financial Distress of Mining Companies	**Independent Variable:** current ratio, cash ratio, debt ratio, ROA, day sales in receivables ratio	Logistic Regression Analysis	The result of this study were, (i) current ratio, cash ratio, and debt ratio have significant effect on

	Listed in BEI using Financial Variables and Non-Financial Variables".	**Dependent Variable:** Financial Distress		negative correlation coefficient in predicting financial distress of companies. (ii) non-financial ratios, managerial and institutional ownership do not give significant effect in predicting financial distress of companies.
2	Fathonah (2016) entitled "Pengaruh	**Independent Variable:**	Simple Regression Analysis	(i) independent commissioner board has

	Penerapan Good Corporate Governance Terhadap Financial Distress”.	institutional ownership, managerial ownership, Independent Commissioner Board, and Audit Committee. **Dependent Variable:** Financial Distress		significant negative effect towards financial distress. (ii) Institutional ownership has negative effect on financial distress. (iii) Managerial ownership has positive effect on financial distress. (iv) audit committee has positive effect on financial distress but not significant.

3	Sastriana & Fuad (2013) “Pengaruh Corporate Governance and Firm Size Terhadap Perusahaan Yang Mengalami Kesulitan Keuangan (Financial Distress)	**Independent Variable:** the number of board of directors, the number of independent board, institutional ownership, managerial ownership, and the number of audit committee members, and firm size. **Dependent Variable:** Financial Distress	Logistic Regressio n Analysis	the variable number of board of directors and audit committee members are significantly influence the company experiencing financial distress. While independent board, institutional ownership, managerial ownership and firm size do not have significant effect of

				companies' financial distress
4	Jamal & Shah (2017) entitled "The Impact of Corporate Governance on the Financial Distress: Evidence from Pakistani Listed Companies".	**Independent Variable:** size of board, composition of board, audit committee independence and duality of CEO. **Dependent Variable:** Financial Distress	Logistic Regressio n Analysis	the size of board, composition of board and CEO duality has positive effect on companies.
5	Witiastuti & Suryandari (2016) did a research entitled "The Influence of Good Corporate	**Independent Variable:** managerial ownership, institutional ownership and	descriptiv e statistics and logistic regression .	the managerial ownership, institutional ownership and independent commissioner do not

	Governance Mechanism on the Possibility of Financial Distress".	independent commissioner. **Dependent Variable:** Financial Distress		influence significantly on financial distress.
6	Pramudena (2017) "The Impact of Good Corporate Governance on Financial Distress in the Consumer Goods Sector".	**Independent Variable:** institutional ownership, managerial ownership, the proportion of commissioners and the number of board directors. **Dependent Variable:** Financial Distress	Multiple linear regression	institutional ownership and managerial ownership adversely affect the possibility of financial distress. While, the proportion of commissioners and the number of board directors have positive effect on

				possibility of financial distress.
7	Murhadi & Tanugara & Sutejo (2018) entitled “The Influence of Good Corporate Governance on Financial Distress.	**Independent Variable:** the proportion of independent outside directors, audit opinion, size, and ownership **Dependent Variable:** Financial Distress	Logistic Regression Analysis	The findings of this study are the proportion of independent outside directors, audit opinion, size, and ownership are significant of financial distress.
8	Ananto, Mustika, Handayani (2017) entitled “Pengaruh Good Corporate Governance	**Independent Variable:** Good Corporate Governance (GCG), Leverage,	Multiple Linear Regression test	The findings showed that profitability and leverage affect financial distress. Meanwhile,

	(GCG), Leverage, Profitabilitas dan Ukuran Perusahaan Terhadap Financial Distress Pada Perusahaan Barang Konsumsi yang Terdaftar di Bursa Efek Indonesia.	Profitability and Size of the Company's **Dependent Variablel:** Financial Distress		institutional ownership, board size, the size of boatd of directors, independent board size, the size of the audit committee and the size of the company does not affect financial distress.
9	Rianti and Winwinyadiati (2018), The Influence Firm Size on Financial Distress: A	**Independent Variable:** Firm Size **Dependent Variable:** Financial Distress	Multiple Regressio n analysis	And the result is showed that firm size has effect but not significant towards

	Research on Agricultural Companies Listed in Indonesia Stock Exchange.			financial distress.
10	Hidayat & Meiranto (2014) “Prediksi Financial Distress Perusahaan Manufaktur di Indonesia.	**Independent variable:** leverage ratio, liquidity ratio, activity ratio, and profitability ratio. **Dependent variable:** Financial Distress	interest coverage ratio and analyzed using logistic regression .	The result showed that leverage ratio (debt ratio), liquidity ratio (current ratio), and activity ratio (total asset turnover ratio) were financial ratios have significant value to predict financial distress in company,

				while profitability ratio (return on asset) is only financial ratios which not significant to predict financial distress in company.
11	Triwahyuningtias & Muharam entitled “Analisis Pengaruh Struktur Kepemilikan, Ukuran Dewan, Komisaris Independen, Likuiditas dan Leverage Terhadap	**Independent variable:** ownership structure, board size, independent board of commissioners, liquidity and laverage **Dependent variable:**	Logistic regression analysis	The findings of this study showed that ownership structure, director size, liquidity and leverage have significant impact on the probability of firm

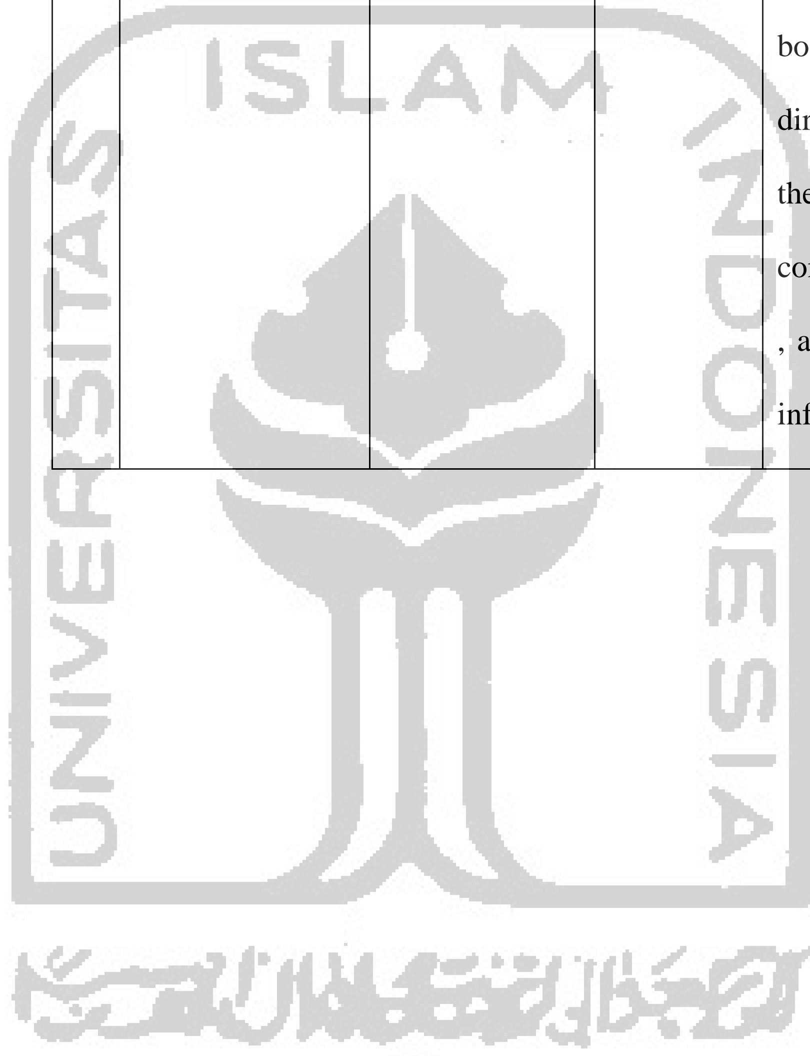
	Terjadinya Kondisi Financial Distress (Studi Pada Perusahaan Manufaktur Yang Terdaftar Di Bursa Efek Indonesia Tahun 2008 – 2010).	Financial Distress		experienced financial distressed. This research failed to prove effect of commissioners size and independent board of commissioners with probability of experiencing financial distress.
12	Kurniasanti & Musdholifah (2018) "Pengaruh Corporate Governance, Rasio Keuangan,	**Independent variable:** board of commissioners , managerial ownership, institutional	Logistic regression analysis	The result showed return on asset and asset turnover negatively asset on financial

	Ukuran Perusahaan dan Makroekonomi Terhadap Financial Distress (Studi Pada Perusahaan Sektor Pertambangan yang Terdaftar di Bursa Efek Indonesia Tahun 2012 – 2016)".	ownership, audit committee, and independent commissioner, financial ratios (profitability, leverage, liquidity, and efficiency) firm size. **Dependent variable:** Financial distress		distress. While, board of commisioners, managerial ownership, institutional ownership, audit committee, independent commissioner, leverage, liquidity, firm size, inflation and interest does not affect on financial distress.
13	Hanifah & Purwanto (2013) "Pengaruh Struktur	**Independent variable:** size of the board of	Logistic regression analysis	The result of the study showed the director size,

	Corporate Governance dan Financial Indicators Terhadap Kondisi Financial Distress". This study is to examine the impact of corporate governance structure and financial indicators financial distress. The indicators that used are size of the board of directors, the board size,	directors, the board size, independent commissioners, managerial ownership, institutional ownership, and the size of the audit committee and **the financial indicators:** liquidity, leverage, profitability, and operating capacity. **Dependent variable:** Financial distress		managerial ownership, institutional ownership, leverage and operating capacity have significant impact in financial distress.

	independent commissioners, managerial ownership, institutional ownership, and the size of the audit committee and the financial indicators use liquidity, leverage, profitability, and operating capacity.			
14	Bodroastuti (2009) entitled "The Influence of Corporate Governance Structure to Financial	**Independent variable:** Good corporate governance **Dependent variable:**	Logistic regression analysis	The result of research showed that variables of corporate governance structure that

	Distress".	Financial distress		influenced financial distress were the number of board of directors and the number of commissioners , and other not influenced.



2.3.Hypothesis Development

The hypothesis proposed as a temporary result of the research problem formulation are:

Managerial Ownership and Financial Distress

As explained in the agency theory, the theory suggests an incentive mechanism for management actions to be following the interests of stakeholders. On the other hand, management will not think like stakeholders if they are in the position of stakeholders. The position between shareholders and managers can be aligned because of managerial ownership, so that financial distress is not only the responsibility of the shareholders but also as the manager's responsibility.

Managerial ownership is assumed to be able to reduce agency problems that arise in a company. Short and Keasey (1999) cited by Triwahyuningtyas and Muharam (2012), stated that there was a linear relationship between managerial ownership with the value of the company. The linear relationship was indicating the company's performance. According to Handayani and Hadinugroho (2009) in Sastriana and Fuad (2013), the managers who have shares through managerial ownership will take the decision more carefully. It was because all the consequences will also affect the manager directly. A research conducted by Triwahyuningtyas & Muharam (2014) found that the smaller or lower managerial ownership owned by the company, the higher the possibilities of the company facing financial distress. A research conducted by Sastriana & Fuad (2013) found

that if the manager had shares through managerial ownership, the manager will take decisions more carefully considering all consequences. Thus, the agency problem will be overcome. Then the manager will maximize the value of the company.

So, it can be concluded, managerial ownership negatively affects the occurrence of financial distress, because the greater the managerial ownership of a company, the greater the management to bring the company towards a better company for the company.

Based on the explanation above, the research hypothesis is formulated as follows:

H1: ***Managerial ownership has a negative effect on financial distress.***

Institutional Ownership and Financial Distress

Institutional ownership is the total proportion of company shares owned by the institution or organization. Institutional ownership such as securities companies, insurance companies, banks, investment companies, pension funds, and ownership of other institutions will encourage more optimal of the company's management performance. Compared to managerial ownership, the institutional ownership can conduct better supervision, because the institutional ownership can get more information and analysis related to the manager.

According to the agency theory perspective, institutional ownership can improve company performance, because supervision will continue to be carried out by shareholders on overall performance in the company.

According to Bodroastuti (2009), the greater the institutional ownership, the more efficient the use of company assets, so that the potential for financial distress can be minimized because companies with greater institutional ownership indicate their ability to monitor management.

A research conducted by Kurniasanti & Musdholifah (2018) found that institutional ownership affecting financial distress. It supported by Welsbach cited Triwahyuningtias & Muharam (2012) that institutional ownership structure is one of the factors that can affect the condition of the company in the future, whether the company experiences financial distress or even goes bankrupt. Thus, the greater the institutional ownership, the financial distress can be minimized. This is because of the greater the institutional ownership, the greater the monitoring of the company, which in turn will be able to encourage the smaller potential financial distress that may occur in the company.

So, it can be concluded, the greater institutional ownership by the company, the greater control by the management, because the financial distress analysis will be better and financial distress can be overcome.

Based on the explanation above, the research hypothesis is formulated as follows:

H2: ***Institutional ownership has a negative effect on financial distress.***

Audit Committee and Financial Distress

The audit committee is a committee established by the board of directors which have to control independently on financial report and external audit. Moreover, the Audit Committee is a corporate governance mechanism that is assumed to be able to reduce agency problems that arise in a company that if it occurs continuously can cause financial distress in the company (Hanifah & Purwanto, 2013). Committee audit have to (i) ensure that financial report reported following the standard, (ii) internal control structure running well, (iii) doing audit internal and audit external following the audit standard, (iv) after the auditor has finished audit, the management have to continue to follow up on audit findings.

Based on the Decision of the Directors of the Jakarta Stock Exchange No.Kep-315 / BEJ / 06/2000 stated that the membership of the audited committee at least 3 (three) members, the independent commissioner of the company and also as chairman of the committee audited, and another member is independent parties where at least one of them have the ability in the field of accounting and finance.

The number of members of the audit committee must be more than one person so that the audit committee can held meetings and giving opinions with each other. This is because each member of the audit committee has different corporate governance experiences and financial knowledge. Oktadella (2011) in Sastriana & Fuad (2013).

Therefore, it is expected that the existence of an effective audit committee can change policies in achieving accounting profit in the next few years and to increase the company performance. Thus, the company can avoid financial distress.

Based on the explanation above, the research hypothesis is formulated as follows

H3: ***The audit committee has a negative effect on financial distress.***

Independent Commissioner Board and Financial Distress

According to Jensen and Meckling (1976) in Hanafi and Breliastiti (2016), Agency theory assesses that the independent commissioner needed on the board of commissioners to supervise and control the actions of the directors. The function of the commissioner independent in supervising performance the board of directors in terms of controlling regarding financial problems then it will avoid the detrimental action to the company, and Independent commissioner board has an important role so that the company can be spared financial difficulties. So, rate the higher proportion of independent commissioners will be very influential to the lower the probability a company experiences financial distress.

Furthermore, the independent commissioner board can reduce the problem in agency theory called agency problem. Because the existence of an independent commissioner can avoid asymmetric information between the two parties who can raise the possibility of conditions financial difficulties.

Based on the explanation above, the research hypothesis is formulated as follows

H4: ***The independent commissioner board has a negative effect on financial distress.***

Firm Size and Financial Distress

Oktadella (2011) cited by Sastriana & Fuad (2013), Firm size shows how much information contained in it, and reflects the awareness of management regarding the importance of information, both for external parties and internal parties. Firm size can describe how much the number of assets owned by the company, because the larger the size of the company, the greater the number of assets owned by the company.

This condition may occur because the larger the size of the company, the number of assets owned by the company will be even greater so that if there are urgent obligations, companies will easily meet these obligations. Likewise, with the capital condition, companies have more capital so that companies will easily expand their business to other types of businesses, if they feel that the business, they are doing is experiencing bankruptcy, for example, due to losing competitiveness with other companies.

A research conducted by Sastriana & Fuad (2013) found that in larger companies with large total assets, they will be braver to use capital from loans in spending all assets, compared to smaller companies.

Based on the explanation above, the research hypothesis is formulated as follows

H5: ***The firm size has a negative effect on financial distress.***

Sales Growth and Financial Distress

Eliu (2014) in Yudiawati & Indriani (2016), Sales Growth is a ratio that measures the company's sales by calculating the difference in the sales in a certain period. Sales growth reflects the successful application of the company’s investment in the past period and can be used as a predictor for future company growth. Pattinasarany (2010) in Widhiari & Merkusiwati (2015) explains that the ratio of sales growth is used to measure the level of sales growth in a period.

A study conducted by Yudiawati & Indriani (2016) shows the greater sales growth ratio’s company, the less the company experiences financial distress. That is because the company's high growth rate illustrates the company can maintain its position and in good condition, so financial distress can be minimized. It supported by the study conducted by Widhiari & Merkusiwati (2015), sales growth had a significant negative effect on financial distress.

Based on the explanation above, the research hypothesis is formulated as follows:

H6: ***The sales growth has a negative effect on financial distress.***

2.4.Research Model

The research model which represents the relationship among variables in this study as follows

Figure 2.1

Theoretical Framework