Family Control, Board of Directors and Bank Performance in Indonesia

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Abstract

This study examined the effects of family control and board of directors on bank performance in Indonesia. There are 362 observations were conducted in all national banks in Indonesia during 2007-2009. Performance is proxied by ROA, ROE, and NPL. The findings showed that banks controlled by family and private institutions were more likely to have lower performance which indicates that the entrenchment effect is stronger than alignment effect. Owner involvement in the board of directors and in management had a negative effect on performance. This indicates that expropriation leads to performance downgrade. The independence of the board of direction had no effects on performance. This showed that board of directors could not function in concentrated and controlled ownership. Control variables such as number of branch, supporting branch, cash office, and automated teller had no significant effect on performance.

Key Words: Family Control, Board of directors, and Performance.

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Introduction

The case of the Century Bank[1], that is suspected to make Indonesia suffering from a loss of 6,7 trillion rupiahs[2], has emphasized the possibility of expropriation of the controlling shareholders on the minority shareholders, the depositors and the Republic of Indonesia as the insurance institution. The indication of family ownership expropriation also happened in the case of Eddy Tansil[3], the Summa Bank case[4], and the liquidation of several banks during the economic crises[5]. These kinds of cases always involved a family as controlling shareholders and have terrible effects on the performance. They can even cause a take-over or liquidation of the bank.

Previous research showed that a high level of concentration of the shareholders' voting rights and domination of the controlling shareholder is related to a high level of expropriation on minority shareholders, a low performance level and a low value of the company (Claessens *et al.* 2000, La Porta *et al.* 2002, Zhu and Ma, 2009). The risk of expropriation will be higher if family's control rights have more influence than cash flow rights, for instance, through dual class voting shares or ownership structure pyramid (Almeida and Wolfenzon 2006; Claessens *et al.*, 2002; La Porta *et al.*, 1999; Morck dan Yeung, 2003; Villalonga dan Amit 2006).

[1] The Century Bank was declared as a fail bank that has systemic effects, based on the Indonesian Bank Governor Decree No 10/232/GBI/Rahasia on 20th November 2008 (BPK RI, 2009).

[2] The Century Bank received a short term financing from the Indonesian Bank to the amount of 689 billion rupiahs and investment participation from the deposit insurance institution to the amount of 6,76 trillion rupiahs which were given in several tranches between 24th November 2008 and 24th July 2009 (BPK RI, 2009).

[3] The Eddy Tansil case has caused a loss of 1,5 trillion rupiahs or 565 million US Dollar for Indonesia.

[4] The Summa Bank was liquidated by the government based on Banking Rules 1992 on 14th December 1992. It experienced a difficult time due to the increasing amount of nonperforming loan since the credits are mostly transferred to its own companies in which the financed projects are not working. http:businessknowledges.blogspot.com/2009/10/kasus-bank-summa.html.

[5] on November 1997, 16 banks were liquidated and the operation of 7 banks was stopped on April 1998 due to complicated banking problems, low level of corporate governance implementation (Asian Development Bank, 2000) and credits that are mostly transferred to related groups.

Result of previous research showed that there is a significant negative relationship between family ownership concentration and firm's performance (Oswald, 2009; Achmad *et al*., 2009, Giovannini, 2010).

Based on the phenomenon of expropriation conducted by controlling shareholders and the results of previous researches, there is a debate on whether family control negatively affects banking's performance in Indonesian or not. On the other hand, the board of directors has a crucial role in upholding *corporate governance*. It is obligated to ascertain the conduct of *good corporate governance* in every single banking service in any level or organization structure, to control directors' performance and responsibility, to direct, observe and evaluate the conduct of strategic banking policy (BI, 2006). Jaggi *et al.* (2009) mentioned the importance of board of directors' independency in 1) monitoring management's activities, 2) providing control on initiative effectiveness and managerial activities, 3) protecting investor's business, and 4) avoiding the power misuse of power by insiders.

The previous research about the relationship between board of directors and performance showed inconsistent results. Positive effects of board directors on performance can be found in research conducted by Ibrahim and Samad (2011), Giovannini (2010) and Filatotchev *et al.,* (2005), while Prabowo and Simpson (2011), Prabowo (2011), and Zhu and Ma (2009) found no significant relationship between the board of directors and performance. The requirements to be a member of the board of directors in banking industries are different from the requirements in the other industries. The members have to be elected by the shareholders and need to successfully pass the fit and proper test conducted by Indonesian Bank as the regulator (BI, 2007). Thus, this research suggests that boards of directors in banking industries will have a positive effect on performance.

The purpose of this research is to test the effect of family control and two certain characteristics of a board of directors (size and independency) on banking performance in Indonesia. This research is important because 1) there is a phenomenon of companies controlled and dominated by family in East Asia, including Indonesia(Fan and Wong, 2000; Claessens *et al.,* 2000; Lukviarman, 2004; Siregar, 2006; Achmad *et al.,* 2007; dan Sanjaya, 2010). This phenomenon might cause agent conflict since family control will give a strong motivation to the family to conduct expropriation on company's resources at the expense of non family minority shareholders (Vilalonga and Amit, 2006). 2) Big banking cases in indicate Indonesia the existence of withdrawal of resources by families as the owner and controller[6]. 3) a bank is an institution which has to comply to strict rules; nevertheless these kinds of cases keep on happening, suggesting that the policy of corporate governance fail to limit the expropriation by the controlling shareholder.

The differences between this study and previous ones are the following: 1) the research setting is in Indonesia, a country that has unique agency conflicts, including conflicts between controlling shareholders and non controlling ones, depositors and Indonesian Bank as insurance institution in the banking sector. 2) This research tries to analyze the practice of family control in Indonesian banking industries that is rarely subject to analysis. 3)

There are banking cases in Indonesia indicating the conduct of expropriation by controlling shareholders that cause loss for several parties, even in some cases the Indonesian government need to take over those banks. All of those facts have made Indonesia to be a perfect setting to scrutinize the complicated relationship between family control and bank performance thus, so that motivated this study.

Theoretical Background and Development Hypothesis

The conceptual framework of this research is based on the agency theory (Jensen and Meckling, 1976). Agency theory assumes the principal and agent are involved in a specific agreement and will try to maximize their utility. This condition will create an agency conflict among them. Agency conflict between the shareholders and management happens in companies in which the shareholders are located in many different areas, for example in companies in the US (Morck and Steier, 2007). While agency problems happened in companies with concentrated share ownership, for instance companies in Indonesia (Lukviarman, 2004), are involving the controlling shareholders and minority shareholders. Agency conflict happening in the banking industry is more complex since it involves controlling shareholders, minority shareholders, depositors (Palenzuela and Mariscal, 2007) and in Indonesian banking industries, also conflict with the Indonesian Bank as the insurance institution.

[6] Look at footnote 1-5

Family Control and Performance

Several previous studies showed different results about the effect of family control on performance. Filatotchev et al. (2005) showed that family control does not affect performance of the multi-industrial companies listed in Taiwan. A positive relationship between family control and performance can be found in Maury (2006), Andres (2007), Ibrahim and Samad (2011), and Silva and Majluf (2008). Maury (2006) showed that the value of Tobin's Q and ROA of companies controlled by family are 7% and 16% higher than those without family control. Maury (2006) used 1672 non-financial companies from 13 Western European Countries as the sample. While Andres (2007) showed that firms owned or controlled by family are more profitable compared to those owned by several groups of shareholders, if only the successor still have the control power.

He observed family companies and performance on 1.701 listed companies in Germany. The findings of Andres (2007) were supported by Ibrahim and Samad (2011) who studied 290 listed companies in Malaysia with 2030 observations in total . Furthermore, Silva and Majluf (2008) showed that family ownership had positive effects on performance as long as their voting rights are not more than 67,8%, which is the case in 48,5% of companies owned by a family. For their research, they used 330 observations on the economic emergency in Chile. Research results that showed a positive effect on the performance of family control was consistent to the argument that the control ability of the family reduces the classic agency conflicts between owner and management (Maury, 2006).

Concentration of ownership can be related to the possibility to force the owners to monitor management so as to reduce cost and agency conflicts. Firms controlled by a family are also associated with low agency cost and can help reduce the information asymmetry with external funding providers (Andres, 2008).Negative relationship between family control and performance was found by Oswald et al. (2009) for companies in the U.S., whereas Ahmad et al. (2009), Prabowo (2011) and Prabowo and Simpson (2011) had the same results for Indonesia, Reyes and Zhao (2010) for France, and Giovannini (2010) for Italy. This Negative relationship is consistent with the theory of entrenchment (Oswald et al., 2009), which says that family control provides an incentive to expropriate corporate resources for their private benefits.

The use of the entrenchment theory offers a new theoretical perspective that is deemed more appropriate to explain the relationship between performance and ownership, especially within firms owned by families. This research suspects that family control will tend to move to entrenchment effect which at the end will have a negative impact on the performance of banking industry in Indonesia. This assumption is based on: 1) the results of previous research which showed that family control has a negative impact on company's performance (Oswald *et al.*, 2009; Achmad *et al.*, 2009; Giovannini, 2010, Prabowo and Simpson, 2011). 2) The ownership structure of companies in Indonesia, including the banking industry, is concentrated on specific groups (Claessens *et al.*, 2000; Lukviarman, 2004; Siregar, 2006; dan Sanjaya, 2010), this condition might motivate the controlling shareholders to conduct expropriation on company's resources to gain individual benefit. 3) The Banking cases, which happened in Indonesia[7], indicated the occurrence of the expropriation of resources of controlling shareholders on the costs of other stakeholders. So, the hypothesis of this research can be formulated as follows:

H1: Family control has a negative effect on the performance of the banking industries in Indonesia.

Board of Directors and Performance

Previous research related to the relationship between board of directors and performance showed inconsistent results. A positive relationship between corporate governance (CG) and performance can be seen in Ibrahim and Samad (2011), Giovannini (2010) and Filatotchev *et al.*, (2005). A negative relationship between board of directors and performance was found by Prabowo and Simpson (2011), Prabowo (2011) and Zhu and Ma (2009). Ibrahim and Samad (2011) showed that the size and independency of the board of directors will significantly affect company's performance. Giovannini (2010) showed that board's independency is improved as there is investment withdrawal conducted by family during IPO, existence of an equity venture owner in the firm, an establishment of a big and active board of directors and of a compensation committee.

Furthermore, he found that the existence of an independent board of directors has positive impact on company's performance even though statistically the significance is quite small. Filatotchev *et al.*, (2005) showed that board's independency from the successor's family and board member's financial business have positive impact on the performance of listed companies in Taiwan.

[7] Take a look at foot note 1-5

Prabowo and Simpson (2011) observed the relationship between the structure of the board of directors and company's performance of family controlled companies by using 152 non financial companies in Indonesia for the sample.

The result showed that directors' independency does not have significant effects on the company's performance. Furthermore Prabowo (2011) broadened governance mechanism by testing the effect of control in the family ownership. The result showed that directors' independency has a negative impact on performance of companies with family's ownership and involvements in the board of directors are too strong. This finding is supported by Zhu and Ma (2009) which not found evidence for the effect of board of directors' independence on companies' value in capital market in China during 2002 until 2006. This finding strengthened previous findings that boards' independency is invalid in protecting minority shareholders in China.

There are several requirements that have to be fulfilled in order to be a member of the board of directors in the Indonesian banking industry. has Additionally to the election by the shareholders, every member has topass the fit and proper test conducted by the Indonesian Bank. The Fit and proper test is conducted in order to ensure that the candidate has the integrity, competency and financial reputation to handle his responsibility as a member of the board of directors appropriate. Integrity represents his good moral and behavior, a high commitment to improve good operational activities of banking and assurance that he is not listed in the fail applicants list. A candidate must have a good understanding and experience in banking industries to be categorized as competent (BI, 2003). Thus, this study believes that the existence of board of directors in banking industries will have a positive impact on performance. The second hypothesis of this study therefore can be formulated as follows:

H2a: Board of directors has a positive effect on performance of the banking industries in Indonesia.

Research Method

This research uses data of public national banks in Indonesia during 2007 until 2009. There are 362 observations conducted in this research. The data of the financial reports and financial ratio from 2007 to 2009 are obtained from Direktori Perbankan Indonesia (DPI) issued by Indonesian Bank and other financial information is collected from Info Bank, while data about family and non-family ownership are gathered from the Indonesian Bank.
The dependent variable is bank performance, measured by using ROA (Return on Assets), ROE (Return on Equity) and NPL (Non Performing Loan).

The first independent variable is family control measured by using 1) dummy variable for family and non-family ownership. Non-family ownerships consist of ownership by government, foreign institution and private institution. 2) Family involvement in the board of directors and 3) family members involvement in the management. The second independent variable is board of directors' independency that is measured by using 1) the independence of the board of directors, 2) the size of the board of directors, 3) the existence of an independent chief director. The control variables consist of 1) the number of branch offices, 2) the number of ATMs, 3) the establishment year, 4) the total amount of assets, and 6) the extend of family ownership (in percent) .
The criteria of family controlled bank are as follows:

1. The family has 20% or more ownership on the company. 20% cut off was used in several studies, for instance La Porta *et al.*, (1999) abd Claessens *et al.*, (2000). La Porta *et al.*, (1999) mentioned that 20% cut off is enough to effectively control a company. Besides, based on capital market rules year 1995, it is mentioned that someone is categorized as primary shareholder if he owns directly or indirectly at least 20% of the company's voting rights. (UU RI Number 8 year 1995).
2. The family has less than 20% direct ownership on the company but, it is involved in the company's board of directors. Thus, it will have the authority to control the company (Giovannini, 2010).
3. The family has less than 20% direct ownership on the company but, it's involved in company's management. So, the family is able to control the company indirectly. (Givonannini, 2010).
4. The family has less than 20% direct ownership on the company, but the Indonesian Bank declares it as the ultimate shareholder. Thus, there is a possibility that it owns a big portion of shares through indirect ownership.

The data analysis techniques used in this research are the Wallis Kruskal test and multiple regressions. The Wallis Kruskal test is used to analyze the difference between the performance of the banks controlled by a family and non family controlled banks. The equation for the multiple regressions can be formulated as follows:

$$ROA = \alpha + \beta_1 DFam + \beta_2 DGovt + \beta_3 DPrivInst + \beta_4 DForeign + \beta_5 BrdInd + \beta_6 BrdSize + \beta_7 HeadDirInd + \beta_8 Brch + \beta_9 SubBrch + \beta_{10} ATM + \beta_{11} Cash + \beta_{12} Age + \beta_{13} TA + \beta_{14} OwnCon + \beta_{15} BrdOwn + \beta_{16} MgtOwn + \varepsilon_{it.}$$

$$ROE = \alpha + \beta_1 DFam + \beta_2 DGovt + \beta_3 DPrivInst + \beta_4 DForeign + \beta_5 BrdInd + \beta_6 BrdSize + \beta_7 HeadDirInd + \beta_8 Brch + \beta_9 SubBrch + \beta_{10} ATM + \beta_{11} Cash + \beta_{12} Age + \beta_{13} TA + \beta_{14} OwnCon + \beta_{15} BrdOwn + \beta_{16} MgtOwn + \varepsilon_{it.}$$

$$NPL = \alpha + \beta_1 DFam + \beta_2 DGovt + \beta_3 DPrivInst + \beta_4 DForeign + \beta_5 BrdInd + \beta_6 BrdSize + \beta_7 HeadDirInd + \beta_8 Brch + \beta_9 SubBrch + \beta_{10} ATM + \beta_{11} Cash + \beta_{12} Age + \beta_{13} TA + \beta_{14} OwnCon + \beta_{15} BrdOwn + \beta_{16} MgtOwn + \varepsilon_{it.}$$

Note:

D-Fam	: Bank controlled by family (excluded group).
D-Govt	: Bank controlled by government .
D-PrivInst	: Bank controlled by private institutions.
D-Foreign	: Bank controlled by foreign Institutions.
BrdInd	: the amount of independent directors divided by the total amount of directors
BrdSize	: the size of board of directors.
HeadDirInd	: Independent head of board of directors
Brch	: The amount of branch offices
SubBrch	: The amount of sub branch offices
ATM	: The amount of ATMs
Cash	: The amount of cash offices
Age	: Age of the firm
TA	: The logarithm of total assets.
OwnCon	: Ownership Concentration: The largest percentage of ownership
BrdOwn	: Owners' involvement in the board of directors.
MgtOwn	: Owners' involvement in the management .

Results and Discussion

This research is conducted on public national banks in Indonesia for 3 years from 2007 until 2009. The yearly samples are up to 123 companies, summing up to 373 observations in total. The effect of family control and board of directors on the performance is tested by using regression analysis. In conducting this analysis, abnormal and incomplete data must be expelled from the samples to fulfill classical assumption test. Thus, the sample size is 362 observations.

Banking Control Structure in Indonesia

Mapping the control structure is important because controlling shareholders might use their controlling authority to gain private benefits causing loss for the other shareholders (Denis and McConnell, 2003). Besides, control is one of the internal mechanisms of corporate governance (Denis and McConnell, 2003) aiming to influence company's operations and policy directly or indirectly (BI, 2003).Based on the collected data, the study found that banking control structure in Indonesia during 2007 until 2009 consists of control by family (33,24%), local and central government (26,54%), private institution (18,77%) and foreign institution (21,45%).

Most banks are controlled by a family or by individuals. Control by private institution might be actually be control by a family through indirect control, a phenomenon also found in Lukviarman (2004). He mentioned that 71,5% companies in Indonesia are controlled by a family. Unfortunately, this interesting phenomenon cannot be described completely because of the limited information about indirect ownership. Companies controlled by family might change their ownership structure from individuals into private institutions. Thus, banks that are controlled by private institutions are possibly actually controlled by family.

Ownership Concentration Level in Indonesian Banking

In this section, the study will describe the concentration of ownership structure to know the normal level of ownership percentage in Indonesian banking industries. Ownership concentration level is classified into the following groups: 1) 0 – 10% ownership. 2) ownership of more than 10% up to 20%. 3) ownership of more than 20% up to 40%. 4) Ownership of more than 40% up to 60% . 5) ownership of more than 60% up to 80%. 6) Ownership of more than 80% up to 100%.

In the sample has not been any observation with an of less than 10% is not found, this finding indicates that the ownership structure is not well spread. Two percent of the sample had an ownership concentration of 10% up to 20%, 13 percent had a concentration between 20% and 40%. 29 percent of the observations are in the category of 40 % to 60% of ownership, and the category of 60% to 80% includes 19% of all observations. The biggest share of the sample (37%) is found to have an ownership concentration between 80% and 100%. This result indicates that the level of banking ownership concentration in Indonesia is very high. Besides, there is no big difference between ownership concentration from 2007, 2008 and 2009. Based on these findings, it can be conclude that 40% or more ownership concentration is dominating the ownership structure in Indonesian banking (85%).

The Impact of Family control and Board of Directors on ROA

The result of tests conducted to explore the impact of family control and board of directors on ROA can be seen in table 1. Previously this test have passed classic assumption test with normal distribution, and there is no multicollinearity among the variables and there is no auto correlation. This test used 362 observations. The regression result shows that the amount of adjusted R^2 is 0.237, it means that 23.7% of ROA can be explained by the 15 independent and control variables in the model, while the rest of it can be explained by other factors outside the model. The amount of the calculated F-Test is 7.918 with 0.000 probabilities. Since the amount of the probability is less than 0.05, it means that this regression model can be used to predict ROA or in other words that all the variables used in this study affect ROA at the same time.

Table 1
The Impact of Family Control and Corporate Governance on ROA, ROE and NPL

Independent variables	***The impact of family control and corporate governance on***					
	ROA		ROE		NPL	
	B	t-statistic	B	t-statistic	B	t-statistic
(Constant)	-1.545	-3.581	-3.722	-10.418	-2.267	-4.235
D-Govt	.308	3.343***	.345	5.642***	.067	.742
D-PrivInst	.089	0,931	-.016	-.262	.241	2.721***
D-Foreign	.271	2,610***	.052	.798	.150	1.550
BrdOwn	.007	0.108	.001	.011	.113	1.438
MgtOwn	-.336	-2.618***	-.327	-3.001***	.082	.458
HeadDirInd	-.184	-2.176**	-.069	-.929	.140	1.283
TA	-.018	-0.512	.223	7.614***	.027	.612
BrdInd	-.030	-0.399	-.104	-1.619	.149	1,283
OwnCon	.005	0.055	-.197	-2.991***	.194	2.021
FamOwn	-.144	-1.296	-.026	.053	-.003	-.250
BrdSize	-.014	-1.028	.001	.045	-.040	-2.358**
Brch	.000	-0.051	.000	-1.105	.000	-.307
Subbrch	.000	0.296	.001	.089	.000	.367
Cash	.000	-0.542	.000	-.472	.000	-.098
ATM	.000	1.313	.000	-1.097	.000	.206
Age	.001	.994	.001	1.219	.003	2.172**
	Adj. R^2: .237		*Adj.* R^2: .495		*Adj.* R^2:.081	

, **, * Indicate significance at the 10, 5, and 1 percent levels, respectively*

Based on this research model in which 15 independent and control variables are included, it is found that ROA for banks controlled by government is 30.8% bigger than for banks controlled by families and for banks controlled by foreign institution is 27.1% bigger than for banks controlled by families. This result has a level of significance between 0.001 and 0.009 in sequence. Meanwhile there is no significant difference of the ROA between banks controlled by private institutions and families. This finding supports the previous assumption that private institutions who become controlling shareholders are actually family. Owner's involvement in the management variable has a significant negative impact (0.009 significant level) on ROA. Meanwhile, the controlling variables company's size, biggest ownership percentage, company's age, number of branch offices, sub branch offices and the number of ATMs are not significantly affecting ROA.

Based on this testing, it can be concluded that controlling factors influence the performance stronger as the board of directors. This might be caused by concentrated ownership and the controlling structure in banking industries, which lets controlling owners dominate in running the company. Thus, the board of directors' (which were elected based on the fit and property test) central function, integrity and competency, do not have significant effect on the performance. Controlling owner's involvement in the board of directors and management has negative influence on the performance. This finding is in accordance with the formulated hypothesis which stated that family ownership has a negative influence on the performance and is describing controlling owner expropriation. Besides, the indication of expropriation by controlling owners is supported by the research result which shows that the performance of banks controlled by families or private institutions is significantly lower than those controlled by government and foreigners.

The Impact of Family control and Board of Directors on ROE

The result of this research shows that banks controlled by government have significantly higher ROE (34,5%) than those controlled by family. Meanwhile banks controlled by foreigners and private institution have a 5,2% and 1,6% higher ROE than those controlled by family. Thus, it can be concluded that banks controlled by government and foreign institutions or foreigners are having higher ROE compared to those controlled by family and private institutions. Family involvement in the management has a negative impact on ROE. Meanwhile, the size of board of directors, the percentage of independent directors and the head of director independency are not significantly affecting ROE. Company's size has positive effects on ROE and ownership concentration has negative effects on ROE. The more concentrated the ownership, the lower the ROE.

This analysis has also considered classical assumption test. The results of this research show that family ownership has a negative impact on ROE. Also owners' involvements in the management and board of directors have negative impacts on ROE though not too significant.

The size of board of directors has a positive significant effect on ROE but, head of director's independency and the percentage of directors' independency do not affect ROE. The results of test on family control and board of directors on ROE are supporting previous findings mentioned about the impact of family control and board of directors on ROA.

The Impact of Family control and Board of Directors on NPL

The test for the impact of family control and board of directs on NPL shows that the amount of adjusted R^2 is 0.081, it means that 8.1% of NPL can be explained by 15 independent variables in this model. Meanwhile the rest of them (92.9%) are explained by other factors which are included in this model. Based on the result, the amount of calculated F is 2.827 with 0.000 probabilities thus, it means that this regression model can be used to predict the NPL or in other words those 15 variables are all together affecting NPL.

NPL in banks controlled by family is not significantly different to those controlled by government or foreigners. It means that banks controlled by family, government and foreigners have the same awareness to control their NPL. NPL in banks controlled by private institutions is 24,1% significantly higher than the one in banks controlled by family. It means that banks controlled by private industries have bigger courage to handle troublesome credits. Their courage to handle troublesome credits is reasonable since they have to handle greater risk compare to banks controlled by family.

It is reasonable because the risk of owners in banks controlled by private institution (in which there is possibility that those banks are controlled by individuals or family) is indirect one, while in banks controlled by family the risk is direct risk. From these results, it can be concluded that concentrated ownership of banks on private institution in founding previous researchs (Abbas, Rahman, Mahenthiran, 2009, and Bhattacharya and Graham, 2009) can bring good effect, unfortunately in Indonesia this condition has the opposite effect since the controlling shareholders can get protection from their indirect ownership due to litigation risk in banking industries. Ownership concentration has significant positive effects on NPL, it means that the more concentrated the ownership the more non performing loans are in a bank.

The age of a company has a significant positive effect on NPL but, the coefficient is very small (0,003). It means that the older the bank is, the less courage it has to handle non performing loans. The board of directors' size has significant negative effect on NPL; the bigger the size of board of directors is, the smaller the NPL. This finding indicates that the bigger the size of the company the smaller the risk of nonperforming loan within a bank. Findings of this research show that boards of directors can contribute to reduce nonperforming loan in particular banks but, they do not have any effect on ROA and ROE. The other control variables, which are branch offices, sub branch offices, the amount of cash and the number of ATMs, and the size of the bank, do not have significant effect on NPL.

Conclusion

This study is conducted with data of national public banks in Indonesia for 3 years, namely from 2007 until 2009. For each year there is the data of 124 banks in the samples, so in total the observations count to 371. From this sample, observations with incomplete or abnormal data are deducted in order to fulfill the classical assumption test and thus, the final sample size is 362 observations. The controlling structure in Indonesian banking during 2007 up to 2009 is consisting of four kinds of ownership: family control (33, 24%), government and local government (26,54%), private institutions (18,77% and foreign institutions (21,45%). Banks controlled by family and individuals are dominating the structure (33,24%). The ownership structure of Indonesian banks is concentrated 85% of the Indonesian banks show a concentration of ownership of more than 40%. Besides, there are no significant changes in the ownership structure between 2007 and 2009.

Owners who are involved in the banks' board of directors have significant negative impact on ROA and insignificant negative impact on ROE. The size of the board of directors brings significant negative impact on NPL. It means that the bigger the size of the board of directors, the smaller the amount of nonperforming loan within a particular bank.This research found that family ownership has significant negative effects on ROA and ROE. Board of directors' independency does not significantly affect ROA, ROE and NPL. This result is in accordance to Zhu and Ma (2011), because in their study they did not find any evidence on the effect of board of directors' independence on the companies' value in China between 2002 and 2006. It also supports the findings of Prabowo (2011) in which the samples were non financial institutions in Indonesia.

This research indicates that a board of directors is less functional in a institution with a structure of high control. Meanwhile, the head of director's independence has a positive impact on the NPL. The control variables, which are the number of branch offices, sub branch offices, cash office and ATMs, do not significantly affect ROA, ROE and NPL. The size of the company has a positive significant effect on ROE, meaning the bigger the company the higher the ROE. But, those control variables do not have significant effects on ROA and NPL. Ownership concentration has a significant negative impact on ROE, which means that the more concentrated the ownership, the smaller the amount of ROE. But, it does not have a significant effect on ROA. Ownership concentration is also having a positive effect on NPL, which means that the more concentrated the ownership, the bigger the amount of the nonperforming loan.

Contribution

Practical Contribution

The phenomenon of high ownership concentration in Indonesian banking during 2007 until 2009 indicates that for more than 10 years since Claessen *et al.*, (2000); La Porta *et al.*, (1999) and Lukviarman (2004) conduct their research, there is no big difference in ownership concentration and ownership structure in Indonesia from year to year.

This findings prove that high ownership concentration and family ownership indicate the occurrence of controlling shareholders, who are happen to be family at the same time, and expropriation on the other shareholders. Based on these findings, the researcher suggests the Indonesian Bank to establish rules which oblige banks to be more transparent in revealing indirect ownership, and its magnitude and distribution. Currently, those kinds of rules are not available and voluntary disclosure about the ownership details are rarely found in annual reports of banks. Giving disclosure about indirect ownership will reduce expropriation risk.

Theoretical Contribution

The findings of this study give important theoretical contributions to prove that controlling factors are more influencing on banks' performance while the factors of boards of directors are not really influencing the performance. Foreign banks, which do not have board of directors in their structure, can perform better than banks controlled by family and having a board of directors. The existence, independence, and number of heads of a board of directors and an independent head of the board are not really well working in an entity in which the ownership structure is very concentrated.

Though findings in this research are contrary to research conducted in countries where the ownership structure is well spread, these findings support the agency theory which mentioned that each party will maximize its private utilities even if it has to sacrifice other's utilities. It means that controlling owners will maximize their utilities even they have to sacrifice the other's utilities. This finding can be explained as follows: in a well spread ownership structure, family controlling reduces the agency cost and improve the company's performance, while, in a concentrated ownership structure family ownership might lead to actions to gain private advantage and thus reducing the company's performance.

The existence and independence of board of directors in well spread ownership structure and in a company which upholds legal aspects will bring improvement on the performance but, board of directors in a concentrated ownership structure does not have any impact in the limitation of controlling owners expropriation and at the end it does not affect the performance. Varied result related to the effect of family control and board of directors on the performance indicates that the result will easily changed if the performance indicator used in the analysis is changed. The use of different performance indicator will produce different results.

Limitations and Implications for Future Research

The limitation of this research is its performance indicators. This research uses ROA, ROE and NPL as the performance indicators. Mean-while there are other financial ratio indicators such as capital, assets, management, earnings and liquidity (CAMEL) ratio and market indicators such as tobin's Q that can be used in the research. The use of other indicators is feasible because previous research use other indicators too. This research uses board of directors as the corporate governance mechanism proxy thus, future research can include other comprehensive governance mechanisms.

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