# The Effect of Corporate Governance on Company Shareholder Value

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**ABSTRACT**

**Backgrounds:** Corporate governance mechanisms and firm financial characteristics are key determinants of corporate performance, with profitability proxounded by Return on Equity (ROE). Corporate performance is shaped by a constellation of governance attributes, encompassing board architecture, ownership configuration, the robustness of internal control frameworks, and the firm's leverage.

**Objectives:** This study examines the effect of corporate governance mechanisms and financial characteristics on profitability. Specifically, it investigates the roles of Non-Compliance Index, Director Share Ownership, Remuneration, Internal Controls, Extra Committees, Board Independence, Board Size, Leverage, and Liquidity in shaping ROE.

**Methodology:** A quantitatively oriented research design was implemented, utilizing archival financial disclosures as secondary data sources. The empirical estimation relied on multiple linear regression performed on a balanced panel dataset encompassing 500 firm-year observations, with classical assumption tests and hypothesis testing ensuring model robustness.

**Findings:** Simultaneously, governance mechanisms and financial characteristics significantly affect ROE. Partially, Director Share Ownership and Board Size positively influence ROE, while Board Independence has a negative effect. Non-Compliance Index, Remuneration, Extra Committees, Leverage, and Liquidity were not significant. Internal Controls could not be analyzed due to lack of data variation.

**Conclusions:** Not all governance mechanisms directly enhance profitability. Excessive board independence may constrain managerial flexibility, while effective board size and managerial ownership can improve performance. Limitations include a low $R^2$ and the use of ROE as the sole performance metric. Future studies should explore alternative performance measures and additional governance variables. Findings provide guidance for designing governance structures that promote profitability, investor confidence, and sustainable business practices.

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## 1. INTRODUCTION

Financial crises are an unforgettable aspect, including the major financial crises that hit Indonesia in 1963, 1998, and 2020/2021. In 1963, Indonesia experienced its first crisis due to hyperinflation. At that time, Indonesia's political and economic conditions were isolated from the international community due to its confrontational stance, which resulted from Indonesia's withdrawal from the United Nations (UN). This caused Indonesia's inflation rate to skyrocket to 119%, ultimately destroying the economy. There was a contraction in the national Gross Domestic Product (GDP) of 2.24%. This was followed by a contraction in household spending of 3.95% and a decline in exports and imports of 26.58% (CNBCIndonesia.com, 2024).

The 1998 economic crisis occurred as a result of the Asian financial crisis that began in Thailand. The crisis was triggered by Thailand's change in exchange rate policy from a fixed exchange rate system against the US dollar in July 1997. This policy caused many companies to default on their payments, along with a significant weakening of currency exchange rates, including the rupiah. This situation triggered the depreciation of the rupiah exchange rate from around Rp2,500 to Rp16,900 per US dollar. This prolonged economic crisis ultimately led to the collapse of President Soeharto's leadership after 32 years in power (CNBCIndonesia.com, 2024).

The economic crisis of 2020/2021 has different characteristics compared to the crises of 1963 and 1998. This turmoil was catalyzed by the Covid-19 pandemic, initially reported in Wuhan, China in late 2019, and later escalating into a worldwide phenomenon with immediate repercussions for global economic stability. These conditions forced the Indonesian government to implement various restrictive policies, such as restrictions on social, economic, business, and trade activities, in order to curb the spread of the virus. The implementation of restrictive policies materially altered the trajectory of the real and financial sectors, culminating in a sharp contraction of overall economic momentum at the national level (Pratiwi & Chariri, 2021).

In order to survive during this crisis, companies in Indonesia must implement effective measures to build resilience and increase stakeholder value during the crisis in order to survive (Pangestu et al., 2019). Therefore, there is an urgent need for research on the influence of corporate governance at the company level on shareholder value during a crisis (Farhat & Hili, 2024).

This research is grounded in Agency Theory and Stewardship Theory. Agency Theory explains the potential conflicts between management and shareholders, where ineffective governance may allow managers to act in their own self-interest, thereby harming shareholder value, particularly during periods of crisis. In contrast, Stewardship Theory argues that managers can act as stewards who are aligned with the interests of shareholders, thus potentially mitigating negative impacts during periods of instability. These theoretical perspectives provide the foundation for examining how corporate governance mechanisms influence shareholder value in financial institutions in Indonesia during times of crisis.

Financial institutions are fundamentally different from non-financial companies in terms of business models, regulations, and governance mechanisms (Ahmad et al., 2021). After the crisis, supervision of corporate governance in financial companies became more intensive, resulting in new regulations aimed at improving stability and preventing future crises. Revisions to corporate governance codes seek to improve transparency and accountability in financial institutions (Ofoeda et al., 2020). On this basis, the present inquiry explores the impact of corporate governance arrangements on shareholder value in Indonesia’s financial industry, with the crisis context serving as the empirical backdrop.

This study focuses on discussing corporate governance compliance and its relationship with shareholder value in companies, given that compliance with corporate governance codes is very important for financial companies, as it can mitigate risk and positively influence market perception (Din et al., 2022; Pratiwi & Chariri, 2021; Yusrianti et al., 2020). The analysis specifies a set of explanatory variables, including the non-compliance index, board independence, additional committee structures, internal control robustness, director ownership, and remuneration schemes, supplemented by control covariates such as board size, liquidity, capital ratios, systematic risk (beta), and financial leverage, to examine shareholder value in Indonesian financial institutions.

Prior research indicates that companies adhering to codes of conduct tend to achieve better market valuations and operational performance (Ronoowah & Seetanah, 2025). However, some scholars argue that the effectiveness of corporate governance may diminish during periods of crisis (Ariyudha & Rokhim, 2024). Governance mechanisms generally have a positive impact on firm performance (Ahmed, 2025; Al-Qudah, 2024; Arsh, 2025), yet findings regarding their effectiveness remain contradictory, particularly under unstable market conditions (Ferilli, 2024; Reis, 2022). Several studies highlight the role of board characteristics, audit committees, foreign ownership, and gender diversity in moderating firm performance in emerging markets (Azam, 2025; Gharios, 2024; Najaf, 2025), while other research emphasizes the influence of financial crises and economic volatility on the ability of governance mechanisms to remain effective (Iona, 2025; Ratmono, 2022). In this context, Kufo and Shtembari (2023) found that companies with more independent board members actually experienced lower stock returns during crises, which contradicts the assumption

that strong governance always correlates with better performance. Thus, although substantial research demonstrates the benefits of corporate governance, empirical evidence regarding its effectiveness during crises in developing countries such as Indonesia remains limited and warrants further investigation.

Based on the theoretical framework and prior findings, this study develops a conceptual model linking corporate governance mechanisms and financial characteristics to shareholder value (proxied through ROE), particularly in the context of a financial crisis. The explanatory variables include governance compliance, board independence, committee structure, internal control quality, director ownership, and remuneration schemes, while the control variables include board size, leverage, beta, capital ratio, and liquidity. This model serves as a blueprint for empirically testing the influence of governance and financial factors on firm performance during crisis conditions.

## 2. LITERATURE REVIEW

### 2.1. Definition of Dependent Variable (Shareholder Value)

Shareholder value is defined as a concept that refers to the value created by a company for its shareholders, which is measured by increases in share price and dividends paid. In this context, shareholder value is often considered a key indicator of a company's performance, where the goal of management is to increase shareholder wealth. This involves business decisions and strategies, including investing in profitable projects, managing costs efficiently, and innovating products and services that can attract more consumers. In addition, shareholder value also includes considerations of balanced risk and return, as shareholders expect to receive a fair return for the risks they take.

### 2.2. Relationship Between Variables

#### 2.2.1. The Effect of Non-Compliance Index on Shareholder Value

The NCEI serves as an indicator of the magnitude of firms' non-adherence to regulatory frameworks and good corporate governance norms. A high level of non-compliance reflects weak internal control mechanisms and increases legal and reputational risks, as well as agency costs. This condition can reduce investor confidence and negatively impact company value as reflected in shareholder value.

Extant empirical evidence points to an inverse association between departures from corporate governance standards and both firm performance and valuation. Ronoowah and Seetanah (2024) report a negative relationship between the Non-Compliance Index (NCEI) and ROA as well as ROE, albeit without statistical significance. Similar findings were also reported by García-Sánchez et al. (2020), Aluchna and Kuszewski (2020) Nguyen et al. (2020), and Fariha et al. (2022), who stated that low levels of governance compliance tend to reduce investor confidence and shareholder value. Based on this description, the following hypothesis is formulated:

**H1**: The Non-Compliance Index has a significant negative effect on Shareholder Value.

#### 2.2.2. The Effect of Board Independence on Shareholder Value

Independence at the board level represents a critical governance lever for reinforcing the effectiveness of supervisory functions. An autonomous board of commissioners is expected to attenuate conflicts of interest, promote disclosure quality, and uphold shareholder rights, while simultaneously signaling governance credibility to the investment community.

A substantial body of empirical research documents a favorable association between board independence and firm value. Alipour et al. (2019) and Kafidipe et al. (2021) found that the proportion of independent boards is positively related to firm value. Similar results were also reported by Shaikh et al. (2024), Khan et al. (2024), and Huynh et al. (2023) who stated that board independence increases investor confidence and shareholder value, although in some contexts the effect is not always statistically significant. Thus, the hypothesis proposed is:

**H2**: Board Independence has a significant positive effect on Shareholder Value.

#### 2.2.3. The Effect of Extra Committees on Shareholder Value

Extra committees, such as risk committees and sustainability committees, are additional committees that aim to strengthen the company's oversight and risk management functions. These

committees contribute to more rigorous strategic deliberation and attenuate exposure to risks that could undermine corporate and shareholder interests.

The existence of auxiliary committees in corporate governance arrangements has been shown to relate positively to firm value. Almulhim et al. (2024) found that the existence and independence of risk committees have a positive effect on financial performance. Similar results were also shown by Alodat et al. (2023), Bhat et al. (2024), Erin et al. (2020), and Ofoeda (2022), who stated that extra committees increase the effectiveness of supervision and shareholder value. Based on these empirical findings, the following hypothesis is formulated:

**H3**: Extra committees have a significant positive effect on shareholder value.

### 2.2.4. The Effect of Internal Controls on Shareholder Value

Internal controls comprise institutional mechanisms aimed at assuring the credibility of financial statements, strengthening operational performance, and ensuring adherence to regulatory frameworks. Robust control environments attenuate the likelihood of fraudulent activity and accounting irregularities, thereby elevating the decision-usefulness of financial information for investors.

Extant studies indicate that stronger internal control environments exert a favorable influence on corporate performance and firm value. Yang et al. (2020) found that the quality of internal controls significantly improves a company's financial performance. This finding is reinforced by Hamed (2023), Liu et al. (2024), and Chan et al. (2021), who concluded that strong internal controls increase investor confidence and shareholder value. Thus, the hypothesis proposed is:

**H4**: Internal Controls have a significant positive effect on Shareholder Value.

### 2.2.5. The Effect of Director Ownership on Shareholder Value

Equity participation by directors represents a conduit for incentive alignment between corporate leadership and shareholders, with the potential to attenuate agency tensions and orient strategic decision-making toward firm value maximization.

Prior empirical investigations consistently demonstrate that director equity participation is positively related to shareholder value. Rahman (2024) identifies a significant positive correlation between director ownership and firm performance metrics, namely ROA and ROE. This evidence aligns with the conclusions of Kjærland et al. (2020), Vo et al. (2025), Al Farooque et al. (2021), and Alruwaili et al. (2024), which suggest that increasing director ownership is concomitant with higher firm valuation. On this basis, the ensuing hypothesis is advanced:

**H5**: Director Ownership has a significant positive effect on Shareholder Value.

### 2.2.6. The Effect of Remuneration on Shareholder Value

Remuneration is a form of compensation given to directors and management in return for their performance. A performance-based remuneration system can be an incentive mechanism to encourage management to create long-term value for shareholders.

Empirical research shows that remuneration has a positive effect on company performance and value. Hsieh et al. (2024) and Sang et al. (2024) found that performance-based compensation increases firm value. Similar findings were also reported by Marzuki and Shukri (2019), Bezuidenhout et al. (2018) and Daruwala (2023), who stated that fair and transparent remuneration increases investor confidence and shareholder value. Thus, the hypothesis proposed is:

**H6**: Remuneration has a significant positive effect on Shareholder Value.

## 2.3. Theoretical framework

The conceptual framework functions as an analytical compass for the present study. Consistent with the research setting, it examines the influence of governance-related variables, namely the non-compliance index, board independence, extra committee structures, internal control quality, director ownership, and remuneration, while accounting for board size, liquidity, capital ratios, systematic risk (beta), and leverage as control factors in explaining shareholder value in Indonesian financial institutions, as illustrated in the subsequent figure.

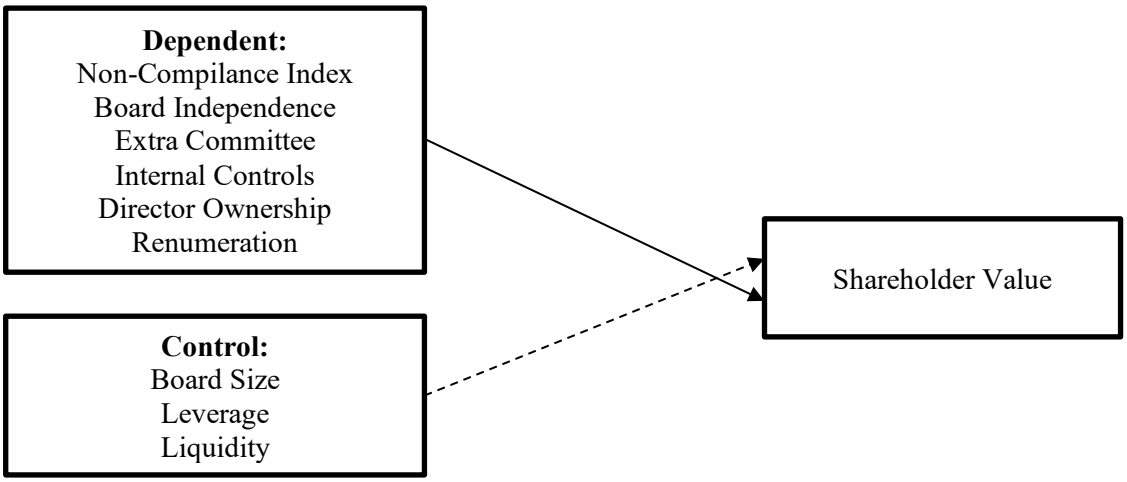


**Figure 1. Theoretical Framework**
Source: Researcher's Findings (2024)

## 3. METHOD

### 3.1. Research Design

This study employs quantitative research, which is an effort to develop theories that have been previously examined in an academic context. Furthermore, this research can be categorised as comparative causal research, which aims to investigate the causal relationship between the independent and dependent variables being tested. This research adopts a systematically designed framework to analyse the causal relationship between variables. In this context, the research paradigm applied in this study is none other than the positivistic paradigm, which emphasises the importance of data that can be measured and tested empirically. Through this approach, researchers focus on collecting quantitative data through surveys, experiments, or statistical analysis to obtain evidence that can support or reject the formulated hypothesis.

This study uses data from companies listed on the Indonesia Stock Exchange (IDX) for the period 2018–2022, in order to capture temporal variations in corporate governance practices and their influence on firm performance. To analyze causal relationships, a panel data regression model is employed. Both fixed-effects and random-effects models are considered, and the Hausman test is used to determine the most appropriate model specification.

### 3.2. Variable Operational Definition

#### 3.2.1. Non-Compilance Index

The Non-Compliance Index quantifies the degree to which a firm deviates from applicable regulatory requirements or prescribed standards. This index is calculated based on the number of violations identified in audit reports, regulations, or internal guidelines (Farhat & Hili, 2021). The formula is presented below (Equation 1):

$$\text{Non-Compliance Index} = (\text{Number of violations/total obligations}) \times 100\% \quad (1)$$

#### 3.2.2. Board Independence

Board independence denotes the extent to which directors preserve autonomy from personal, financial, or relational entanglements with the organization, enabling them to act objectively in decision-making (Altass, 2022). This metric is operationalized as the proportion of independent directors expressed as a percentage of total board membership. Nzomo (2022) formulated the relationship as shown in Equation (2):

$$\text{Board Independence} = \text{Number of independent board members/total number of board members} \quad (2)$$

#### 3.2.3. Extra Committee

Extra Committee refers to additional committees formed outside of standard committees (such as audit or remuneration committees) to address specific issues within the company. This index can

be measured by calculating the number of additional committees that exist (Yusrianti et al., 2020). The formula is presented below (Equation 3):

**Extra Committee = Total Number of Committee Types – 2 (Audit Committee & Remuneration Committee)** (3)

### 3.2.4. Internal Controls

Internal controls comprise organizational mechanisms designed to uphold the fidelity of financial disclosures and secure compliance with regulatory frameworks. Internal controls are considered to exist (1) if the company has formal policies and a clear structure for managing risk, internal auditing, and compliance with internal oversight procedures in accordance with applicable standards (e.g., COSO Framework or OJK provisions). Conversely, a value of 0 is given if the company does not have such an internal control system in place.

### 3.2.5. Director Ownership

Director ownership denotes the proportion of equity holdings held by members of the board, which indicates the extent to which directors have a financial interest in the company. This measure is expressed as a percentage (Rathnayake & Sun, 2017). According to Din et al. (2022), the relationship is expressed in Equation (4):

**Director Ownership = (Number of shares owned by directors/total outstanding shares) x 100%** (4)

### 3.2.6. Remuneration

Remuneration denotes the totality of financial and non-financial compensation awarded to directors or board members, including fixed pay, variable bonuses, and other incentive-based benefits (Kirsten & Du Toit, 2018). This measure is expressed in monetary terms. The formula according to Williams et al. (2020) is expressed in Equation (5):

**Board remuneration = Basic salary + allowances + bonuses + incentives + other benefits** (5)

## 4. RESULTS AND DISCUSSION

### 4.1. Research Results

### 4.1.1. Descriptive Statistics

The descriptive statistics table presents a summary of data for all research variables with the same number of observations, namely 500 observations for each variable. The statistics reported include measures of central tendency and dispersion, alongside the minimum and maximum observed values. The presentation and discussion of variables are carried out in accordance with the order of hypotheses proposed in this study.

**Table 1. Descriptive Statistics Results**

| Variable | Obs | Mean | Std. Dev. | Min | Max |
|---|---|---|---|---|---|
| ROE | 500 | 0.0349416 | 0.1702083 | -1.3429 | 0.6883 |
| NonComplia~x | 500 | 13.146 | 2.532491 | 4 | 19 |
| Directorsh~p | 500 | 0.008485 | 0.0419031 | 0 | 0.3151 |
| Remuneration | 500 | 1.28e+11 | 1.02e+12 | 0 | 1.35e+13 |
| InternalCo~s | 500 | 1 | 0 | 1 | 1 |
| ExtraCommi~s | 500 | 4.678 | 3.621678 | 0 | 16 |
| BoardIndep~e | 500 | 0.5267295 | 0.1394546 | 0 | 1.5 |
| BoardSize | 500 | 5.006 | 2.5272 | 1 | 13 |
| Leverage | 500 | 0.8222509 | 3.156336 | 0.0001022 | 64.65768 |
| Liquidity | 500 | 9.415633 | 27.05803 | 0 | 332.29 |

Source: Researcher's Findings (2024)

Referring to the table 1, as the dependent construct, ROE records an average of 0.0349 accompanied by considerable dispersion (SD = 0.1702). The wide span between the minimum (-1.3429) and maximum (0.6883) values underscores marked variability in firm profitability, encompassing cases of severe financial underperformance over the study period.

For Hypothesis 1, the Non-Compliance Index shows a mean of 13.146 and a standard deviation of 2.532, with a range of 4–19, indicating variability in governance non-compliance among firms, although the data distribution is relatively moderate.

Based on Hypothesis 2, the Board Independence (BoardIndep) variable has an average of 0.527, which means that around 52.7% of board members are independent members. The standard deviation of 0.139 with a value range of 0.25 to 1 indicates that the composition of board independence varies considerably between companies in the sample.

Pertaining to Hypothesis 3, the Extra Committee variable records a mean of 4.678 and a standard deviation of 3.622. The minimum value of 0 and maximum value of 16 indicate that there are quite large differences in the number of additional committees that companies have, reflecting variations in the application of additional governance mechanisms.

In the context of Hypothesis 4, Internal Controls (InternalCons) maintains a uniform value of 1 across observations, reflected in a mean of 1, a standard deviation of 0, and identical minimum and maximum values. This indicates that the internal control variable is constant across all observations, so there is no variation between companies during the research period. This condition needs to be considered in further analysis as it may affect the model estimation results.

In relation to Hypothesis 5, the directorship metric records an average of 0.0849 with a dispersion of 0.0419, spanning a minimum of 0 and a maximum of 0.3151, indicate that the level of share ownership by directors is relatively small but still varies between companies.

Pertaining to Hypothesis 6, remuneration displays a mean of 1.28E+11 and a markedly high standard deviation of 1.02E+12. The wide range of values, from 0 to 1.35E+13, indicates very significant differences in remuneration levels between companies, as well as the possibility of extreme values (outliers).

As a control variable, Board Size has an average value of 5 members with a standard deviation of 2.527 and a range of 1 to 13 members, indicating variation in board size between companies. Leverage has an average value of 0.822 with a standard deviation of 3.156 and a very wide range, from 0.0001 to 64.657, indicating extreme differences in capital structure among some companies. Finally, liquidity has an average value of 9.416 with a standard deviation of 27.058 and a range of values between 0 and 332.29, indicating a very high level of liquidity variation.

Overall, the descriptive statistics show that several variables, particularly remuneration, leverage, and liquidity, have a high level of data dispersion, while the internal control variable is constant. This condition needs to be considered in the regression analysis and hypothesis testing stages because it has the potential to affect the stability and interpretation of the estimation results.

### 4.1.2. Hypothesis Testing

Table 1 presents the results of multiple linear regression testing used to analyze the influence of several independent variables on firm performance proxied by Return on Equity (ROE). This regression model is constructed to examine the relationship between corporate governance variables and firm financial characteristics with respect to profitability levels. The data processing results are presented in the form of regression coefficients, t-statistic values, probabilities, and model fit measures.

**Table 2. Multiple Linear Regression Testing**

| Source | SS | df | MS | | | |
|---|---|---|---|---|---|---|
| Model | 0.746857943 | 8 | 0,093357243 | Number of obs | = | 500 |
| Residual | 13.7096095 | 491 | 0,027921812 | F(8. 491) | = | 3.34 |
| | | | | Prob > F | = | 0.001 |
| | | | | R-squared | = | 0.0517 |
| Total | 14.4564675 | 499 | 0,028970877 | Adj R-squared | = | 0.0362 |
| | | | | Root MSE | = | 0.1671 |

| ROE | Coefficient | Std. err. | t | P > ItI | [95% conf. | interval] |
|---|---|---|---|---|---|---|
| NonComplianceIndex | -0.00105 | 0.0030767 | -0.34 | 0.732 | -0.0070989 | 0.0049913 |
| DirectorShareOwnership | 0.6361551 | 0.1797504 | 3.54 | 0.000 | 0.2829803 | 0.9893299 |
| Remuneration | 7.48e-15 | 7.58e-15 | 0.99 | 0.324 | -7.40e-15 | 2.24e-14 |
| InternalControls | 0 | (omitted) | | | | |
| ExtraCommittes | -0.0004113 | 0.0029059 | -0.14 | 0.888 | -0.0061208 | 0.0052983 |
| BoardIndependence | -0.1419774 | 0.0583026 | -2.44 | 0.015 | -0.2565308 | -0.0274239 |
| Laverage | 0.0015033 | 0.9923773 | 0.63 | 0.527 | -0.0031676 | 0.0061742 |
| BoardSize | 0.0088222 | 0.0039096 | 2.26 | 0.024 | 0.0011405 | 0.0165039 |
| Liquidity | -.0000917 | 0.0002824 | -0.32 | 0.746 | -0.0006466 | 0.0004632 |
| _cons | 0.0746107 | 0.0531675 | 1.40 | 0.161 | -0.0298531 | 0.1790745 |

As shown in Table 2, the general form of a regression model can be expressed as follows (Equation 6):

$$ROE=\beta_0+\beta_1 NCI+\beta_2 DSO+\beta_3 REM+\beta_4 IC+\beta_5 EC+\beta_6 BI+\beta_7 LEV+\beta_8 BS+\beta_9 LIQ+\varepsilon \quad (6)$$

Description:
NCI = NonComplianceIndex
DSO = DirectorShareOwnership
REM = Remuneration
IC = InternalControls
EC = ExtraCommittees
BI = BoardIndependence
LEV = Leverage
BS = BoardSize
LIQ = Liquidity

Based on the coefficient values in the output, the regression equation is given in Equation (7):

$$ROE=0.0746-0.0011NCI+0.6362DSO+7.48E-15REM-0.0004EC \quad (7)$$

The explanation of each regression coefficient is as follows.

1. Constant ($\beta_0 = 0.0746$)

The constant term indicates that when all explanatory variables are set to zero, the predicted ROE equals 0.0746 (7.46%). This estimate captures the firm's underlying profitability level, independent of the governance mechanisms and financial attributes incorporated in the empirical specification.

2. Non-Compliance Index ($\beta_1 = -0.0011$)

The negative coefficient indicates that every one-unit increase in the level of non-compliance will decrease ROE by 0.0011 or 0.11%. However, based on the significance test results, this variable is not statistically significant, so empirically, the level of non-compliance cannot be proven to affect company profitability.

3. Board Independence ($\beta_5 = -0.1420$)

The negative coefficient indicates that a one-unit increase in the proportion of independent directors will decrease ROE by 0.1420. This can be interpreted as excessive supervision or reduced managerial flexibility suppressing profit performance. This variable is statistically significant, so its effect on ROE is proven to be real.

4. Extra Committees ($\beta_4 = -0.0004$)

The negative coefficient indicates that the addition of one extra committee has the potential to reduce ROE by 0.0004. This condition may reflect increased bureaucratic complexity and coordination costs within the company. However, because this variable is not statistically significant, its effect on ROE cannot be strongly concluded.

5. Internal Controls

The internal control variable cannot be estimated in the regression model because it has a constant value across all observations (omitted). The absence of variation means that this variable does not meet the requirements for analysing its effect on ROE.

6. Director Share Ownership ($\beta_2 = 0.6362$)

The relatively large positive coefficient indicates that a one-unit increase in directors' share ownership will increase ROE by 0.6362. This finding shows that the greater the directors' share ownership, the more aligned the interests of management are with those of shareholders, thereby encouraging improved company performance. This variable is statistically significant.

7. Remuneration ($\beta_3 = 7.48E^{-15}$)

The remuneration coefficient is very small and close to zero, indicating that changes in remuneration levels have almost no effect on ROE. In addition, statistical tests show that this variable is not significant, so the amount of management compensation has not been proven to affect company profitability.

8. Leverage ($\beta_6 = 0.0015$)

The estimated positive coefficient implies that a unit increase in leverage is associated with a 0.0015 rise in ROE. While theory posits that leverage may amplify equity returns, this relationship is not statistically significant, and thus cannot be empirically confirmed.

9. Board Size ($\beta_7 = 0.0088$)

A positive coefficient indicates that each additional board member will increase ROE by 0.0088 or 0.88%. This suggests that a larger board can provide more diverse expertise, experience, and oversight. This variable is statistically significant, thus having a real effect on company profitability.

10. Liquidity ($\beta_8 = -0.00009$)

A negative coefficient indicates that an increase in liquidity tends to decrease ROE, albeit by a very small amount. This condition may occur due to excess current assets that are not being used productively. However, this variable is not statistically significant.

11. Simultaneous Test (F Test)

The F-test produces a statistic of 3.34 (Prob > F = 0.0010), and since the p-value falls beneath the 0.05 significance criterion, the null hypothesis is rejected. This indicates that the full set of explanatory variables, Non-Compliance Index, director share ownership, remuneration, internal controls, auxiliary committees, board independence, leverage, board size, and liquidity, jointly exert a statistically significant influence on Return on Equity (ROE). The model is therefore regarded as statistically suitable for capturing the relationship between governance structures and firm profitability.

## 4.2. Discussion

### 4.2.1. NonComplianceIndex

The coefficient of the Non-Compliance Index ($\beta = -0.0011$) indicates a negative direction toward ROE, yet is not statistically significant. Empirically, this finding confirms that the level of non-compliance with governance principles within the research sample has no measurable influence on firm profitability. The negative direction of the coefficient remains consistent with the theoretical construction of corporate governance. Non-compliance with regulations and governance principles increases potential legal risk, amplifies agency costs, and weakens internal oversight mechanisms. This is consistent with the findings of García-Sánchez et al. (2020); Aluchna & Kuszewski, T. (2020); Tran et al. (2022); and Fariha et al. (2022) which associate such conditions with a decline in firm value and performance. Therefore, conceptually, the negative relationship between non-compliance and ROE has a strong theoretical basis.

The insignificance of the coefficient indicates that variations in the level of non-compliance within the research sample have not been internalized in the Return on Equity indicator. ROE, as a net income-based ratio, reflects the end result of a firm's operational processes and financing structure, and therefore does not directly capture the latent dimensions of governance risk. The consequences of non-compliance with governance principles more frequently manifest as increased risk perception, a decline in corporate reputational quality, and a rise in the cost of capital, the effects of which are not always simultaneously reflected in accounting profitability ratios.

Furthermore, the non-compliance characteristics measured in this study represent deviations from formal governance standards. Such deviations do not necessarily correlate with operational inefficiency or cost structure distortions. As long as the firm's core activities continue to operate efficiently, variations in administrative compliance aspects do not automatically reduce the rate of return on equity. Accordingly, the relationship between the Non-Compliance Index and ROE in this study is weak because the profitability indicator used does not directly represent the economic consequences of governance risk.

The findings of this study indicate that the level of governance compliance within the sample is relatively homogeneous, and therefore does not produce significant performance differences. In conditions where the majority of firms have already met minimum regulatory standards, small variations in non-compliance scores are not sufficiently strong to influence return on equity.

This finding is consistent with Ronoowah dan Seetanah (2024) who also found a negative relationship without statistical significance. This consistency suggests that the relationship between governance compliance and profitability is neither linear nor automatic. Formal compliance with governance principles does not directly produce an increase in earnings, and conversely, non-compliance at a certain level is not always followed by a decline in ROE. Thus, the findings of this study confirm that the Non-Compliance Index is not a direct determinant of profitability. Its impact on performance is more structural and long-term in nature, rather than an operational determinant that is immediately reflected in the return on equity ratio.

### 4.2.2. Board Independence

The coefficient of Board Independence ($\beta = -0.1420$) is negative and statistically significant. This result indicates that an increase in the proportion of independent commissioners correlates with a decline in Return on Equity (ROE). This finding challenges the prior empirical consensus associating board independence with enhanced oversight effectiveness and firm value creation (Alipour et al., 2019; Shaikh et al., 2024; Kafidipe et al., 2021; Khan et al., 2024; Huynh et al., 2023).

Within the agency theory framework, independent commissioners are positioned as a monitoring mechanism designed to limit opportunistic managerial behavior. Conceptually, strengthening the oversight function should reduce agency costs and improve efficiency, which should ultimately be reflected in increased profitability. However, the empirical results of this study reveal a significant negative correlation, indicating that increased monitoring intensity does not always align with improved return on equity.

This negative coefficient suggests that a higher proportion of independence is associated with a more conservative decision-making approach. A strong oversight orientation tends to emphasize risk control, compliance, and long-term stability. This approach may constrain the aggressiveness of expansion strategies or high-risk investments that could potentially yield higher returns. In this context, board independence functions primarily as a risk control instrument rather than as a catalyst for earnings growth.

This finding also indicates that the effectiveness of board independence is not solely determined by its structural presence, but by its substantive capacity to contribute strategically. Formal independence does not automatically produce performance improvements if the oversight function places greater emphasis on control than on value creation. Accordingly, this study's findings confirm that the relationship between board independence and profitability is complex and influenced by the firm's strategic orientation.

### 4.2.3. Extra Committees

The coefficient of Extra Committees ($\beta = -0.0004$) is negative and not significant with respect to Return on Equity (ROE). This result indicates that the existence of additional committees beyond the mandatory committee structure has no measurable influence on firm profitability within this research model. Conceptually, the formation of additional committees such as risk committees, sustainability committees, or governance committees is regarded as a means of strengthening the oversight structure. Empirical literature suggests that additional committees can improve monitoring quality, enhance transparency, and strengthen corporate accountability, ultimately producing a positive impact on firm value (Almulhim et al., 2024; Alodat et al., 2023; Bhat et al., 2024; Erin et al., 2020; Ofoeda et al., 2020).

However, the results of this study do not reveal a significant relationship between the number of additional committees and ROE. This finding confirms that the expansion of governance structure does not automatically yield improvements in financial performance. The existence of additional committees is a structural indicator, whereas ROE reflects the economic outcomes generated from strategic decisions and operational efficiency. If additional committees are more oriented toward compliance functions and risk mitigation, their contribution to short-term profitability becomes limited.

The negative coefficient that emerges also indicates that increased complexity in governance structure does not correlate with improved return on equity. An increasingly complex structure may raise coordination costs and lengthen decision-making processes. Under such conditions, the benefits of additional oversight are not directly converted into increases in net income.

Accordingly, this finding confirms that the effectiveness of additional committees is not determined by their quantity, but by the quality of their function, authority, and integration within the firm's strategic processes. In the context of this study, Extra Committees do not serve as a direct determinant of profitability.

### 4.2.4. Internal Controls

The Internal Controls variable could not be estimated in the regression model due to the absence of variation across observations. All firms in the sample exhibited identical values based on the indicator used, causing the variable to experience perfect collinearity with the constant and to be automatically excluded from the model. This condition is not merely a technical issue, but carries important analytical implications.

In corporate governance, internal controls are regarded as a primary foundation of the corporate accountability system. The effectiveness of internal controls correlates with the quality of financial reporting, a reduction in earnings manipulation practices, and an improvement in the credibility of financial information (Hamed, 2023; Liu et al., 2024; Mangasih et al., 2020; Said et al., 2020). Theoretically, therefore, internal controls have a structural relationship with firm performance.

However, in the context of this study, the absence of variation indicates that all firms have met relatively uniform minimum internal control standards. This situation suggests that internal controls have become institutionalized as a regulatory obligation rather than a strategic choice. When a governance mechanism has become a universal standard and no longer exhibits differentiation, its contribution to variation in performance across firms becomes statistically unidentifiable.

Furthermore, internal controls function as a risk prevention mechanism and a safeguard for operational stability. Their function is more protective than productive in nature. That is, internal controls are designed to prevent losses and irregularities, not to directly increase profitability. Consequently, their impact on ROE tends to be indirect and long-term. In a profitability-based model such as ROE, this protective effect is not always measurable as an increase in return on equity.

Accordingly, the elimination of the Internal Controls variable from the model cannot be interpreted as an absence of its substantive role in governance, but rather indicates that within this research sample the variable lacks the discriminative capacity to explain differences in profitability. Internal controls function as a structural prerequisite for corporate stability, not as a differential determinant of equity performance.

### 4.2.5. Director Share Ownership (DSO)

The coefficient of Director Share Ownership ($\beta = 0.6362$) is positive and statistically significant. This finding indicates that an increase in the proportion of share ownership by directors correlates directly with an increase in Return on Equity (ROE). Empirically, this variable is one of the strongest determinants in the model, both in terms of the direction of the relationship and its statistical significance.

From the perspective of agency theory, share ownership by management functions as an alignment mechanism between managers and shareholders. When directors hold residual ownership in the firm, they act not only as managers but also as parties who bear the financial consequences of the decisions they make. Such an incentive structure reduces the potential for agency conflict and encourages an orientation toward long-term value creation.

This finding is consistent with those of Kjærland et al. (2020); Rahman (2024); Vo (2025); and Al-Matari et al. (2022) which demonstrate that director ownership has a positive influence on firm value and performance. This consistency reinforces the argument that ownership-based incentive mechanisms are more effective than structural oversight mechanisms in influencing financial outcomes.

From an economic standpoint, share ownership by directors increases their personal risk exposure to fluctuations in earnings and firm value. Consequently, directors are motivated to improve operational efficiency, optimize financing structures, and avoid decisions that could harm shareholders. The relatively large coefficient also indicates that small changes in the proportion of ownership have tangible implications for the level of return on equity.

This finding confirms that incentive-based governance has a stronger impetus toward profitability than formal control-based governance. Accordingly, Director Share Ownership in this study functions as a substantive governance mechanism with a direct influence on firm financial performance.

### 4.2.6. Remuneration (REM)

The coefficient of Remuneration ($\beta = 7.48E^{-15}$) is not statistically significant with respect to Return on Equity (ROE). The extremely small coefficient value indicates that variations in remuneration have no explanatory power over changes in the level of return on equity within this research model.

Theoretically, managerial remuneration is an incentive instrument designed to align the interests of management and shareholders. Performance-based compensation schemes are assumed to motivate management to improve efficiency and profitability. A number of empirical studies have found that compensation linked to performance indicators contributes positively to firm value (Bezuidenhout et al., 2017; Hsieh et al., 2024; Marzuki & Shukri, 2019; Sang et al., 2024; Daruwala, 2023).

The absence of significance in this study indicates that the remuneration structure of the sample firms does not yet have a strong linkage to equity-based profitability indicators. If remuneration components are not fully performance-based or lack adequate sensitivity to changes in earnings, the mechanism does not generate sufficient economic impetus to influence ROE. Accordingly, in the empirical context of this study, remuneration does not function as an effective incentive mechanism for improving return on equity.

### 4.2.7. Synthesis of Hypothesis Testing Results

The hypothesis testing results indicate that corporate governance mechanisms have varying influences on profitability (ROE). Director Share Ownership is proven to improve firm performance through an interest alignment mechanism between management and shareholders. Share ownership by directors creates direct economic incentives that encourage profit-oriented and efficiency-focused decision-making, consistent with the findings of Anh (2024) and Farooq (2022). Board Size also demonstrates a contribution to firm performance. The diversity of expertise, experience, and perspectives within the board strengthens the quality of decision-making and the effectiveness of the oversight function, as stated by Arsh (2025). Adequate board composition provides greater strategic capacity in responding to the dynamics of the business environment.

Conversely, other variables such as Board Independence, Non-Compliance Index, Extra Committees, Remuneration, Leverage, and Liquidity do not demonstrate a consistent or significant relationship with ROE. This finding confirms that the effectiveness of governance mechanisms and financial characteristics is contextual rather than universal, consistent with the arguments put forward by Al-Qudah (2024) and Saha (2024). Overall, the findings of this study confirm that mechanisms based on economic incentive alignment, particularly managerial ownership and board composition structure, play a more dominant role in supporting financial performance than formal structural governance mechanisms. Other formal mechanisms function as supporting elements that reinforce stability and accountability, but do not directly determine the level of return on equity.

The findings of this study make a theoretical contribution to the corporate governance literature by confirming that not all governance mechanisms have a direct influence on firm profitability. Although agency theory traditionally predicts that board independence always

strengthens oversight and improves performance, the empirical findings show that Board Independence can reduce ROE in certain contexts, indicating that the effectiveness of governance mechanisms is highly dependent on the context of implementation and the firm's strategic orientation. This finding extends theoretical understanding of contextual and non-linear control mechanisms, which have rarely been empirically explained in prior research. Furthermore, the positive findings on Director Share Ownership and Board Size reinforce the foundation of agency theory by highlighting the role of economic incentives and the diversification of board expertise as primary factors driving profitability. The distinctiveness of this study lies in the simultaneous combination of formal governance measurement and financial characteristics, enabling the identification of differential impacts of each mechanism on ROE within a single integrated model. This provides more detailed empirical evidence regarding the hierarchy of governance mechanism effectiveness, spanning ownership-based incentives, the strategic capacity of the board, and formal mechanisms such as additional committees or remuneration, which has previously not been comprehensively revealed in the literature.

In practical terms, this study emphasizes the importance of governance design tailored to the characteristics of the firm and the industry context, rather than merely applying formal standards. The policy implications for management and shareholders are reflected in the formulation of optimal ownership structures and board compositions to improve financial performance, while simultaneously confirming that formal mechanisms such as internal controls or additional committees function more as supporting elements than as direct determinants of ROE. Accordingly, the novelty of this study lies in three primary aspects: a contextual approach to governance effectiveness, particularly board independence which can be counterproductive to profitability under certain conditions; the identification of differences in the strength of influence of governance mechanisms, demonstrating that ownership-based incentives are more effective than formal structures in driving ROE; and the simultaneous integration of governance and financial characteristics to assess the relative impact of each factor on profitability, thereby producing a more holistic empirical framework than prior studies.

## 5. CONCLUSION

The empirical results from the multiple linear regression analysis reveal that corporate governance mechanisms and financial characteristics exert a statistically significant joint influence on ROE. The F-test confirms that the model adequately explains the relationship between governance and profitability. This evidence underscores the interdependent role of governance configurations and firm-level financial conditions in determining corporate financial outcomes.

Partial estimation results reveal a positive and significant relationship between Director Share Ownership and ROE, consistent with the notion that managerial equity participation mitigates agency frictions and promotes superior performance outcomes. In parallel, Board Size is positively and significantly related to ROE, indicating that a more expansive board composition may facilitate greater diversity of competencies and more rigorous supervisory capacity in strategic decision-making.

Conversely, Board Independence shows a negative and significant effect on ROE. This finding indicates that an increase in the proportion of independent commissioners does not always have a positive impact on company profitability. In certain contexts, overly strict supervision or increasingly bureaucratic governance processes can reduce managerial flexibility, thereby impacting profit performance. Meanwhile, the variables of Non-Compliance Index, Remuneration, Extra Committees, Leverage, and Liquidity were not found to have a significant effect on ROE. This indicates that the influence of these variables on company profitability is likely to be indirect, long-term, or influenced by other contextual factors not covered in this research model. The Internal Controls variable could not be analysed further because it had a constant value across all observations, thus failing to meet the data variation requirements in regression.

The relatively low coefficient of determination ($R^2$) value indicates that the ability of independent variables to explain ROE variation is still limited. Thus, company profitability is influenced by various other factors beyond the corporate governance mechanisms and financial characteristics tested in this study.

Theoretically, this study contributes to the corporate governance literature by showing that not all governance mechanisms have a direct impact on company profitability. The findings regarding the positive influence of Director Share Ownership and Board Size reinforce agency theory, while the negative results on Board Independence show that the effectiveness of governance is highly dependent on context and implementation. In practical terms, the results of this study can be taken into consideration by management and shareholders in designing an optimal ownership structure and board composition to improve the company's financial performance.

This study has several limitations. First, the relatively low coefficient of determination indicates that there are many other factors that affect ROE but have not been included in the model. Second, the use of ROE as the sole proxy for financial performance does not fully reflect the comprehensive value of the company. Third, the existence of constant variables, such as Internal Controls, means that their influence cannot be empirically tested in the regression model.

Further research is recommended to add other variables that have the potential to affect company profitability, such as risk management quality, institutional ownership structure, or macroeconomic variables. In addition, the use of alternative performance proxies such as Tobin's Q or Return on Assets (ROA) can provide a more comprehensive picture of company performance and value. Subsequent research could also extend the observation period or use different methodological approaches, such as dynamic panel models, to obtain more robust and comprehensive results.

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