

# The effect of foreign institutional ownership, foreign directors and foreign commissioners on profitability

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## ABSTRACT

In 2018, the banking world became a hot topic of conversation because several foreign companies announced their plans to own shares in local banks in Indonesia. Merger between local banks and foreign banks will allow foreign workers to work in Indonesia. This study aims to examine whether foreign institutional ownership, foreign directors and foreign commissioners have an effect on profitability. The sample used in this research is banking companies listed on the Indonesia Stock Exchange in 2014-2018. The research method used is multiple regression analysis. The results of this study indicate that foreign institutional ownership has an effect on profitability. Acquisitions by foreign parties are considered to be able to improve the performance of local banks. Foreign-owned banks are associated with increased profits. Meanwhile, both foreign directors and foreign commissioners have no effect on profitability. The low number of foreign directors and commissioners makes their performance unnoticeable.

## ABSTRAK

Pada 2018 dunia perbankan menjadi perbincangan hangat karena sejumlah perusahaan asing mengumumkan rencananya untuk memiliki saham di bank lokal di Indonesia. Merger antara bank lokal dan bank asing akan memungkinkan pekerja asing bekerja di Indonesia. Penelitian ini bertujuan untuk menguji apakah kepemilikan institusi asing, direksi asing dan komisaris asing berpengaruh terhadap profitabilitas. Sampel yang digunakan dalam penelitian ini adalah perusahaan perbankan yang terdaftar di Bursa Efek Indonesia tahun 2014-2018. Metode penelitian yang digunakan adalah analisis regresi berganda. Hasil penelitian ini menunjukkan bahwa kepemilikan institusional asing berpengaruh terhadap profitabilitas. Akuisisi oleh pihak asing dinilai dapat meningkatkan kinerja bank lokal. Bank milik asing terkait dengan peningkatan profitabilitas. Namun, direksi asing dan komisaris asing tidak berpengaruh terhadap profitabilitas. Rendahnya jumlah direktur dan komisaris asing membuat kinerja mereka tidak terlihat.

## 1. INTRODUCTION

In 2018, the banking sector was considered a hot topic because several foreign companies announced their plans to own shares in local banks in Indonesia. Bank Indonesia Regulation No. 14/8/PBI/2012 of 2012 concerning foreign ownership in banking (BI, 2012) states that share ownership of commercial banks which still open the door to foreign ownership is more than 40%, but with a certain condition. This means that foreign parties still have the opportunity to acquire up to 99% of

the national banking shares. This is also in accordance with the statement of the Financial Services Authority (OJK) which gives permits to investors as long as they meet requirements, contributing to the Indonesian economy, and they do not violate the existing regulations.

Foreign ownership is expected to provide more objective supervision of company performance in order to reduce agency problems. The manager, as an agent, will not prioritize personal interests but the interests of the owner. The results of research conducted

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by Fang *et al.* (2019) showed that foreign ownership can improve market discipline and supervisory efficiency. Acquisition by foreign parties is considered to be able to improve the performance of local banks (republika.co.id, 2019). Banks owned by foreign parties are associated with increasing profits (Nereida & Ken, 2015). One of the local banks that are considered to have experienced positive changes after the acquisition by foreign parties is Bank CIMB Niaga. Initially, the name was Bank Niaga and changed to Bank CIMB Niaga in 2008 after being acquired by the CIMB Group. Currently, the fundamental performance of BNGA's shares continues to increase after the acquisition.

In 2019, several banks merged with other banks. PT Bank Danamon Tbk merged with PT Bank Nusantara Parahyangan Tbk and KCBA Bank Tokyo Mitsubishi UFJ. PT Bank Dinar Indonesia Tbk merged with PT Bank Oke Indonesia. PT Bank Agris Tbk merged with PT Bank Mitraniaga Tbk, whose shares are owned by the Industrial Bank of Korea. The merger between PT Bank Tabungan Pensiunan Nasional Tbk and PT Bank Sumitomo Mitsui Indonesia was effective as of February 1, 2019 (kontan.co.id, 2019).

The existence of foreign ownership will allow the presence of foreign directors, foreign commissioners, and other foreign experts. Improved corporate governance can minimize conflicts of interest between managers, agents, principals, and shareholders. Foreign commissioners can also play a role in monitoring because of the asymmetry of information which can lead to managers' opportunistic behavior toward asymmetry (Suhardjanto *et al.*, 2017). The results of research conducted by Sunday & Godwin (2017) showed that foreign board members have a significant positive effect on the financial performance of a bank. This means that the presence of foreign board members can improve the bank's financial performance.

Foreign ownership has a positive effect on the bank's financial performance, especially in terms of profitability (Houda *et al.*, 2014; Moez *et al.*, 2015). An increase in foreign ownership will increase the company's profitability. However, this influence will decrease as the number of domestic shareholders in the bank increases. Cooperation with foreign companies will also provide greater exposure in the world of practice and access to training, technology and human capital for domestic

banks. This can make the bank have a higher efficiency. The possibility of conducting earnings management will also be lower when there is foreign institutional ownership in the company (Lel, 2019). However, the results of research conducted by Peck-Ling *et al.* (2016) show that foreign ownership has no effect on profitability.

Foreign directors can function to improve corporate governance. According to Bremholm & Svensson (2015), the diversity of nationalities in the board of directors gives a signal that the company is ready for a stricter corporate governance system. If corporate governance is carried out more strictly, it will be possible to increase corporate value. Executives from foreign countries are considered to have better performance than executives from the respective countries (Sanda *et al.*, 2008). In addition, foreign directors also influence corporate social responsibility (Kang *et al.*, 2019). The results of research conducted by Pradono & Widowati (2016) also show that foreign directors are able to increase intellectual capital.

The ability of foreign directors to improve corporate governance, corporate social responsibility and intellectual capital has proven that having foreign directors will make the company better. Foreign directors have supervisory and advisory functions for the company (Liuhto, 2017). Foreign directors are also able to increase the company's profitability (Moez *et al.*, 2015; Peck-Ling *et al.*, 2016; Gambo *et al.*, 2019). However, the results of the research conducted by Cao *et al.* (2019) show that the presence of foreign directors has a negative effect on decision making because of cultural differences, especially in terms of transactions with a high level of uncertainty. Meanwhile, the results of research conducted by Darmadi (2011) show that diversity in citizenship has no effect on financial performance.

Apart from foreign directors, foreign commissioners also play an important role in corporate governance in terms of supervision. The presence of foreign commissioners also has several advantages, such as bringing international experience and enhancing external business, social and political relations (Masulis *et al.*, 2012). However, the results of research conducted by Suhardjanto *et al.* (2017) show that the characteristics of the board of commissioners, one of which is the nationality of the board of commissioners, has no effect on financial performance.

Based on the background described above, it can be concluded that foreign ownership, foreign directors and foreign commissioners can affect the company's profitability. However, there are several studies that show the opposite result. The difference in the results of previous research and the existence of several merger transactions between local banks and foreign banks are the reasons for conducting this research. This study aims to determine the effect of foreign institutional ownership, foreign directors and foreign commissioners on company profitability.

## 2. THEORITICAL FRAMEWORK AND HYPOTHESIS

### Agency Theory

Agency theory studies the design of contracts to motivate agents to act in the interests of the principal when the interests of the agents differ from those of the principal. Agency theory involves two types of contracts: contracts regarding employment and contracts regarding debt. The employment contract has a relationship with both the company and the manager. Contracts regarding debt have a relationship with company managers and lenders. In terms of employment contracts, the owner of the company is called the principal, while the manager who is hired to run the company for the benefit of the owner is called the agent (Scott, 2015: 358).

Managers, as agents, are expected to work in the interests of shareholders, as principals. Unfortunately, the agent's interest is different from the principal's interest. This is what causes a conflict of interest between the manager and the owner. This conflict of interest can increase especially when the principal is unable to monitor the day-to-day activities of management to ensure that management works in accordance with the wishes of the shareholders (owners).

### Foreign Institutional Ownership

Ownership structure is an important instrument in corporate governance to resolve conflicts of interest between shareholders and company management. Policy makers, researchers and companies think about how ownership structure can affect company performance (Herawanto *et al.*, 2017).

Ownership structure can be differentiated based on ownership concentration and ownership identity. Ownership concentration provides information about the rights of

shareholders, whereas ownership identity provides qualitative information about the character of shareholders. This study aims to determine the effect of foreign ownership so that this study will look at ownership from the point of view of ownership identity.

Institutional ownership structure shows share ownership by an institution. Based on the percentage, institutional share ownership is usually higher than individual or non-institutional share ownership. With a high percentage of share ownership, institutions can participate in the operational management of the company. This study uses foreign institutional ownership to see whether foreign institutions can also influence companies. According to Moez *et al.* (2015), foreign ownership provides greater exposure in the world of practice as well as providing access to training, technology and human capital for domestic banks, thus leading to an increase in efficiency.

Foreign investment can be profitable for the banking system. Research conducted by Dinger (2009) shows that private banks that are open as multinational companies will act as a counterweight to the banking system, especially in developing countries. This role can be performed through access to various international sources of liquidity.

### Foreign Directors

The board of directors is one of the mechanisms of corporate governance. Choosing the right composition of the board of directors is closely related to the opportunistic behavior of managers (Hooghiemstra *et al.*, 2015). Managers can behave opportunistically by prioritizing their own personal interests rather than the interests of shareholders. The board of directors takes part in determining important corporate decisions and strategies such as selling assets, investing or acquisitions and making deals with other companies. Due to the important role of the board of directors in the company's operations, the company is expected to be able to elect a board of directors who have good competence and performance. This will ensure that the interests of the company can be properly achieved. If the interests of the company can be achieved properly, the company's performance, as measured by profitability, is also expected to increase.

Currently, everyone can work in various countries in the world, including Indonesia.

This has also been regulated in Bank Indonesia regulation no 9/8 / PBI / 2007 concerning the use of foreign workers and a knowledge transfer program in the banking sector (BI, 2007). Positions that can be held by foreign workers are commissioners and directors, executive officers, and experts / consultants.

Research conducted by Choi *et al.* (2012) explains that the presence of foreign directors provides a signal that the company is willing to break free from managerial ties with the majority shareholder. In addition, the independence and expertise of the board can increase which is expected to be directly proportional to the value of the company.

### **Foreign Commissioner**

Apart from foreign directors, foreign commissioners also play an important role in resolving conflicts between shareholders and managers. Conflicts between shareholders and managers occur because of differences in interests and imbalance of information.

Information imbalance occurs because managers, as agents, have more information about the company than shareholders, as the principal. In addition, the difference in interests between managers and shareholders will make managers more concerned with their personal interests than the interests of the company. This shows that information imbalance plus differences in interests will make managers behave opportunistically. Therefore, a good monitoring mechanism is needed to ensure that conflicts due to imbalance of information and differences in interests can be minimized.

This supervisory role can be performed by the board of commissioners. The board of directors has a more role as a policy maker, while the board of commissioners has a more role as a supervisor. The board of commissioners has the task of supervising and managing management (Zulfikar *et al.*, 2017).

Foreign commissioner is a board of commissioners from outside the country concerned. In Indonesia, a foreign commissioner is a member of the board of commissioners who has a nationality other than Indonesia. Foreign commissioners have several advantages, such as bringing international experience, adding to external business, social and political relations (Masulis *et al.*, 2012).

### **Foreign Institutional Ownership and Profitability**

Agency theory explains the existence of a conflict of interest between shareholders and management. This conflict can be resolved by using the ownership structure which is an important instrument for corporate governance. According to Fang *et al.* (2019), that the existence of foreign ownership can improve corporate governance in banking companies. The price of shares in foreign-owned banks is also considered to reflect future earnings information compared to local banks.

The existence of foreign institutional ownership is expected to provide added value to the company so that it can improve company performance through profitability. An increase in company performance can improve the welfare of shareholders and this is in accordance with the wishes of shareholders. According to Moez *et al.* (2015), foreign ownership provides greater exposure in the world of practice as well as providing access to training, technology and human capital for domestic banks, thus leading to an increase in efficiency. Research conducted by Lel (2019) shows that the presence of foreign institutional investors as part of shareholders will reduce the likelihood of companies implementing earnings management.

Foreign investment can be profitable for the banking system. Research conducted by Dinger (2009) shows that private banks that are open as multinational companies will act as a counterweight to the banking system, especially in developing countries. This role can be performed through access to various international sources of liquidity.

The results of research conducted by Houda *et al.* (2014) show that foreign ownership affects the performance of banking companies. According to Moez *et al.* (2015), foreign ownership can increase the company's profitability as shown in return on assets (ROA) and return on equity (ROE).

Based on the explanation above, the first hypothesis can be formulated as follows:

**H<sub>1</sub>:** *Foreign ownership has an effect on profitability*

### Foreign Directors and Profitability

Agency conflicts arise because of differences in interests between owners and managers. Choosing the right composition of the board of directors is closely related to the opportunistic behavior of managers (Hooghiemstra *et al.*, 2015). In this condition, the manager tries to maximize his welfare and ignores the interests of the owner. This results in a decrease in company performance. Therefore, supervision is needed to monitor the manager-owner relationship so that conflicts do not occur. Thus, company performance will increase when there is a good relationship between manager and owner.

Supervision can be carried out by foreign directors because they are considered to represent and protect shareholders from inefficient decision making. The results of research conducted by Choi *et al.* (2012) showed that the presence of foreign directors can increase firm value. The results of research conducted by Moez *et al.* (2015) show that foreign directors can increase the value of ROA. In addition, the results of research conducted by Sunday & Godwin (2017) shows that foreign members of the board of directors have a significant positive effect on banking financial performance.

Based on the explanation above, the second hypothesis can be formulated as follows:

**H<sub>2</sub>:** *Foreign directors have an effect on profitability*

### Foreign Commissioner and Profitability

Similar to foreign directors, foreign commissioners also play a role in agency problems that occur between shareholders and managers. The existence of information asymmetry between shareholders and managers will increase the likelihood of opportunistic behavior by managers. To avoid these problems, companies need better supervision.

According to Suhardjanto *et al.* (2017), foreign commissioners can also play a role in monitoring. This monitoring will be useful to reduce the occurrence of information asymmetry which in turn can lead to opportunistic behavior.

Research conducted by Sunday & Godwin (2017) showed that banks that have foreign members of the board of commissioners tend to have better performance. The board of commissioners can act as a supervisor to ensure that managers work for the benefit of the company and not for their own personal interests. The presence of foreign

commissioners is also expected to provide more objective supervision and provide several other benefits such as bringing international experience and adding to external business, social and political relations (Masulis *et al.*, 2012). The benefits obtained by the presence of foreign commissioners can increase the company's profitability.

Based on the explanation above, the third hypothesis can be formulated as follows:

**H<sub>3</sub>:** *Foreign commissioners have an effect on profitability*

## 3. RESEARCH METHOD

### Population and Sample Research

The population consists of banking companies listed on the IDX (Indonesia Stock Exchange) from 2014 to 2018, while the sample was taken using a purposive sampling method. According to Sugiyono (2010), purposive sampling is a technique for determining research samples with certain considerations in order that the data obtained can be more representative. The criteria for determining the sample in this study were banking companies listed on the Indonesia Stock Exchange that issued financial reports for 2014 - 2018. The total sample used was 186 banking data.

### Operational Definition and Measurement of the Variables

This study uses profitability as the dependent variable. One of the profitability ratios used to measure the company's ability to generate profits is return on assets (ROA). ROA can be calculated as follows:  $ROA = (\text{net income} : \text{total assets}) \times 100\%$ . This proxy refers to research conducted by Suhardjanto *et al.* (2017).

This study uses foreign institutional ownership as the first independent variable. Institutional ownership structure shows share ownership by an institution. Foreign institutional ownership is ownership of shares by institutions from abroad. Foreign institutional ownership can be calculated as follows:  $\text{Foreign Institutional ownership} = (\text{total share ownership by foreign institution} : \text{number of shares outstanding}) \times 100\%$ . This proxy refers to the research conducted by Herawanto *et al.* (2017).

The second independent variable in this study is foreign directors. Within the company, the board of directors also has an important role in running the company. Foreign directors can be calculated as follows:  $\text{Foreign directors} = (\text{number of foreign directors} : \text{total directors})$

x 100%. This proxy refers to research conducted by Suhardjanto *et al.* (2017).

The third independent variable in this study is foreign commissioners. The board of commissioners has the task of supervising and managing management (Zulfikar *et al.*, 2017). They are members of the board of commissioners who come from abroad. Foreign commissioners can be calculated as follows: Foreign commissioners = (number of foreign commissioners: total commissioners) x 100%. This proxy refers to research conducted by Suhardjanto *et al.* (2017).

### Research Model

This study uses multiple linear regression analysis. The research model used is:

$$ROA = a_0 + a_1 FOWN + a_2 FD + a_3 FC + e$$

Note:

ROA = Profitability

FOWN = Foreign Institutional Ownership

FD = Foreign Directors

FC = Foreign Commissioners

### DATA ANALYSIS

The study used multiple linear regression models for analyzing the data. Multiple linear regression analysis is considered a good model if it meets the classical statistical assumptions such as normality, multicollinearity, heteroscedasticity, and autocorrelation. The researchers tested the hypotheses partially or t-test. The t-test aims to determine the influence of each independent variable partially on the dependent variable. The hypothesis is accepted if the  $\rho$ -value (in the Sig. Column) is <0.05 (Ghozali, 2016: 97).

## 4. DATA ANALYSIS AND DISCUSSION

### Descriptive statistics

Descriptive statistics provide a description of the variable data used. Data descriptions

include minimum, maximum, mean and standard deviation values. Descriptive statistics of profitability, foreign institutional ownership, foreign directors, and foreign commissioners can be seen in Table 1.

The sample consists of 186 banking companies for 5 years (2014-2018). Profitability has a minimum value of -0.01056 and a maximum value of 0.03049. This means that the lowest value of profitability is 1.06% of total assets and the highest value is 3.05% of total assets. The average value of profitability is 0.92% with a standard deviation of 0.76%. Foreign institutional ownership has a minimum value of 0 and a maximum value of 0.98990. It means that the lowest value of foreign institutional ownership is 0% of the number of shares outstanding and the highest value is 98.99% of the total number of shares outstanding. The average value of foreign institutional ownership is 34.08% with a standard deviation of 34.22%.

The variable of foreign directors has a minimum value of 0 and a maximum value of 0.5. This means that the lowest value of foreign directors is 0% of the total number of directors and the highest value is 50% of the total directors. The average value of foreign directors is 7.31% with a standard deviation of 13.03%.

The variable of foreign commissioners has a minimum value of 0 and a maximum value of 0.5. This means that the lowest value of foreign commissioners is 0% of the total number of commissioners and the highest value is 50% of the total commissioners. The average value of foreign commissioners was 9.95% with a standard deviation of 18.25%.

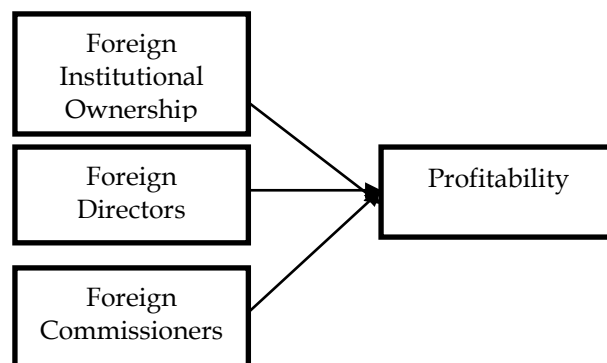


Figure 1  
Research Model

**Table 1**  
**Descriptive Statistics**

Variable	N	Min	Max	Mean	Standar deviasi
PrProfitability	186	-0.01056	0.03049	0.0092	0.0076
KeForeign Institutional ownership	186	0	0.98990	0.3408	0.3422
Foreign Directors	186	0	0.50000	0.0731	0.1303
Foreign Commissioners	186	0	0.50000	0.0995	0.1825

Source: Processed Data, 2020

**Table 2**  
**Normality Test Results**

Unstandardized Residual	
N	186
Significance	0.098

Source: Processed Data, 2020

**Table 3**  
**Multicollinearity Test Results**

	Tolerance	VIF
Foreign Institutional Ownership	0.550	1.819
Foreign Directors	0.399	2.504
Foreign Commissioners	0.438	2.285

Source: Processed Data, 2020

**Table 4**  
**Heteroscedasticity Test Results**

	Significance
Foreign Institutional Ownership	0.144
Foreign Directors	0.515
Foreign Commissioners	0.165

Source: Processed Data, 2020

### Normality Test Results

The normality test is used to see whether the residual data is normally distributed or not. A regression is said to be good if the residual data is normally distributed (Ghozali, 2016:156). The normality test in this study is carried out using the Kolmogorov-Smirnov. If the significance value is  $> 0.05$ , the data residual is said to be normally distributed.

Based on Table 2, the significance value of the normality test is  $0.098 > 0.05$ , so it can be said that the residual data is normally distributed.

### Multicollinearity Test Results

Multicollinearity test is used to see if there is a correlation between the independent variables. A regression is said to be free from multicollinearity problems if the VIF value is not more than 10 and the tolerance value is not less than 0.1 (Ghozali, 2016:103).

Based on Table 3, the tolerance value for all independent variables is higher than 0.1 and the VIF value is less than 10. It shows that this regression is free from multicollinearity problems.

### Heteroscedasticity Test Results

The heteroscedasticity test is used to determine whether there are deviations in the classical assumptions by looking at the variance inequality of the residuals in the regression model. Heteroscedasticity test was carried out using the Glejser test. A regression is said to be free from heteroscedasticity problems if the significance value is  $> 5\%$  (Ghozali, 2016:137).

Based on Table 4, the significance value for all independent variables is higher than 5%. It shows that this regression is free from heteroscedasticity problems.

**Table 5**  
**Autocorrelation Test Results**

DU	DW	4-DU
1.78178	2.108	2.21822

Source: Processed Data, 2020

**Table 6**  
**Hypothesis Test Results**

	T value	Significance
Foreign institutional ownership	2.962	0.003*
Foreign directors	-1.648	0.101
Foreign commissioners	-0.935	0.351
Signifikansi uji F	0.021*	
R <sup>2</sup>	0.036	

\*at the significance level of 5%

Source: Processed Data, 2020

### Autocorrelation Test Results

The autocorrelation test is used to see if there is a correlation between confounding errors in this period and before. The autocorrelation test was performed using the Durbin-Watson test. A regression is said to be free from autocorrelation problems if the durbin-watson value is between du and 4-du (Ghozali, 2016:108). The results of the autocorrelation test can be seen in Table 5.

Based on Table 5, the durbin-watson value is 2.108. The value of du is 1.78178, while the value of 4-du of 2.21822. This shows that the durbin-watson value is between the du and 4-du values. This means that this regression is free from autocorrelation problems.

### Hypothesis Test Results

This study has 3 hypotheses which are tested using multiple linear regression. The results of hypothesis testing are presented in table 6.

Based on Table 6, the F-count significance value is 0.021 < 0.05, thus, it can be concluded that the regression model is fit. The value of R<sup>2</sup> shows the extent to which the independent variable can influence the dependent variable. This shows that the independent variable in this study can affect the dependent variable by 3.6%.

### Foreign Institutional Ownership and Profitability

Based on Table 6, the significance value of the variable of foreign institutional ownership is 0.003, or less than 5%, which indicates that H1 is accepted.

Ownership structure is an important instrument for corporate governance to resolve

conflicts of interest between shareholders and company management. Policy makers, researchers and companies think about how ownership structure can affect company performance (Herawanto *et al.*, 2017).

Foreign institutional ownership has an effect on the company's profitability. The higher the level of foreign institutional ownership, the higher the profitability value is. On the contrary, the lower the level of foreign institutional ownership, the lower the value of profitability is.

Conflicts of interest between shareholders and management can occur because managers work for their own interests and do not pay attention to the interests of shareholders. It is expected that foreign institutional ownership can provide added value to the company so that they can improve company performance. Company performance can be seen through the company's profitability. If profitability is high, the company's performance is high too. The increase in performance which is shown by the increase in profitability shows that the shareholders' welfare has also increased. The shareholders receive a share of the profits. If the profit increases, the share of the profit for the shareholders also increases. This is in accordance with the shareholders' expectation.

According to Moez *et al.* (2015), foreign ownership can provide greater exposure in the world of practice and provide access to training, technology and human capital for domestic banks. The results of research conducted by Dinger (2009) showed that foreign investment can be beneficial for the banking system. A private bank that is open as a multinational



company will act as a counterweight to the banking system, especially in developing countries.

The result of this study is in line with that of research conducted by Houda *et al.* (2014) that foreign ownership affects the performance of banking companies. So do the research conducted by Moez *et al.* (2015). They found that foreign ownership can increase company profitability, which is shown in the form of return on assets (ROA) and return on equity (ROE). However, the results of this study are not in line with the results of research conducted by Peck-Ling *et al.* (2016) that foreign institutional ownership has no effect on profitability.

#### **Foreign Directors and Profitability**

Diversity of nationalities in the foreign directors induces both readiness for a good corporate government and increases profitability. It is argued that diversity of nationalities of board members indicates that the company is ready for a good corporate governance system (Bremholm & Svensson, 2015). The increase in corporate governance indicates that conflicts of interest between managers, as agents, and principals, as shareholders, can be minimized. In addition, executives from foreign countries are considered to have better performance than executives from within the country concerned (Sanda *et al.*, 2008). The results of research conducted by Moez *et al.*, (2015) and Peck-Ling *et al.* (2016) show that foreign directors can increase the company's profitability.

Based on Table 6, the significance value of the variable of foreign directors is 0.101, or greater than 5%, which indicates that  $H_2$  is rejected. Therefore, the variable of foreign directors has no effect on the company's profitability. The nationality of the directors has no effect on the company's performance. This can be due to the small number of foreigners in the board of directors of the company. Of the 186 research data, only 54 data have members of the board of directors who come from outside Indonesia. This means that 71% of banking companies do not have foreign directors or only 29% of banking companies have foreign directors. Yet, this small number of foreigners in the board of directors cannot affect the company's performance.

The Board of Directors works to carry out the company's operations. In Indonesian banking companies, there are more local directors than foreign directors. It may cause

the performance of foreign directors cannot be seen clearly because more local directors work in the company.

The result of this study is in line with that of research conducted by Darmadi (2011), nationality diversity has no effect on financial performance. However, this study is not in line with the results of research conducted by Moez *et al.* (2015), a study by Peck-Ling *et al.* (2016) and Gambo *et al.* (2019).

#### **Foreign Commissioner and Profitability**

The board of commissioners has a duty to ensure that managers work for the company's benefit. The existence of supervision can minimize conflicts of interest between managers and shareholders so that agency problems can be reduced. In terms of supervision, foreign commissioners are expected to provide more objective supervision and several other benefits such as bringing international experience and adding to external business, social and political relations (Masulis *et al.*, 2012). Thus, the presence of foreign commissioners can increase supervision of managers because they can make managers work better and improve the company performance. In this case company performance can be measured through the company's profitability.

Based on the hypothesis test results in Table 6, the variable of foreign commissioners has a significance value of 0.351, or greater than 5%. This shows that  $H_3$  is rejected, which means that the variable of foreign commissioners has no effect on company's profitability. As the nationality of the commissioners has no effect on the profitability of the company can be due to the number of them. The number of banking companies that have foreign commissioners is 47 out of a total of 186 samples. This means that 75% of banking companies do not have foreign commissioners and the remaining 25% have foreign commissioners. The low number of foreigners who work as commissioners cannot affect company performance.

Commissioners help oversee the running of the company to ensure that the shareholders' welfare is fulfilled. Foreign commissioners are believed to provide more objective supervision than local commissioners. However, the small number of foreign commissioners compared to local commissioners makes the performance of foreign commissioners unnoticeable.

The result of this study is in line with that of the research conducted by Suhardjanto *et al.* (2017) that the characteristics of the board of

commissioners, one of which is the nationality of the board of commissioners, has no effect on financial performance. A person's nationality is not always a factor in measuring one's competence.

## 5. CONCLUSION, IMPLICATION, SUGGESTION AND LIMITATION

This study aims to determine whether foreign institutional ownership, foreign directors, and foreign commissioners have an effect on profitability. Foreign institutional ownership has an effect on profitability. The higher the foreign institutional ownership, the higher the company's profitability is. Foreign ownership provides greater exposure in the world of practice as well as providing access to training, technology, and human capital for domestic banks.

The existence of foreign directors has no effect on profitability. This may be due to the low number of foreign directors working in Indonesian banking companies. In addition, citizenship is not the only factor that can be used to measure a person's competence.

The existence of foreign commissioners has no effect on profitability. Similarly, the number of foreign commissioners in Indonesian banking companies is still low. The low number of foreign commissioners can cause foreign commissioners from to gain the company's profitability.

This study only uses a sample of banking companies, thus, the results cannot be generalized. As such, further research is suggested to use other sector of companies as research samples.

The effect of the independent variable on the dependent variable in this study is small, only 3.6%, therefore, there are still many other independent variables that probably affect profitability. For further study, the reseacrhes can use other independent variables such as firm size, labor productivity, and so on.

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