Corporate growth and CEO compensation: Case from Indonesia

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Abstract

This study aims to obtain empirical evidence about whether a corporate growth affects the amount of compensation received by CEOs in Indonesia. The contribution of this study is to provide empirical evidence about the existence of perceived of justice by the CEO in the term of compensation when they succeeded create the value of the firm. It is important to ensure the sustainability of performance, even encourage CEO loyalty to the firm. The samples used are as many as 395 firms-years with growth data used are from the firm's annual report, period 2005-2008. The growth of the corporate performance for three consecutive periods (2005/2006; 2006/2007, and 2007/2008), then compared it with the amount (growth) of compensation received by CEOs.

Test results showed that the growth of the corporate performance growth has a positive relationship to the amount of compensation received by the CEO in Indonesia. Two of three financial performance used in the model, the net income and total assets, are significantly linked to the amount of compensation received by CEOs. While stock price is not show a relationship with what the theory predicted. With these findings, the research hypothesis that says the growth of the company's performance was positively related to the amount of compensation received by the CEO, statistically supported.

Keywords: Corporate growth, Net Income, Share Prices, Total Assets, CEO compensation.

1. Background

This study aims to obtain an empirical evidence about whether the growth of the company performance effect on the amount of compensation received by CEOs in Indonesia. The researchers seemed to agree that the company's performance is an instrument that can be used to determine the compensation to be awarded to company executives (see Eriksson, 2005; Yu, 2009), although there are also some other researchers found only a small relationship between corporate performance and compensation (see Jensen and Murphy, 1990). The debate on the results of this research topic area more attractive and become motivated to do this study.

The ongoing debate on the issue of determining the amount of compensation received by the CEO to be the main motivation of this research is conducted. In Indonesia, as reported, there was a salary increase of 11% plus a bonus on the Board of Directors and director in the company, after serving two years of its new CEO, in one of the major companies listed on the Indonesia Stock Exchange. General Meeting of Shareholders (AGM) PT Bank Mandiri Tbk. approve the increase is due to be adjusted to the achievement of individual performance. A total of 61.63 million bonus given to all directors and commissioners, with the distribution of 22% to 78% for the commissioners and directors (VIVAnews.com, May 4, 2009). Additional salary increases and bonuses due to significantly improved performance directly felt by the banking company shortly after the change of leadership brings new strategy is a concern. This condition indicates that when the CEO can increase the growth of the company, the CEO's received compensation will increase.

The study's research questions about whether the growth in corporate performance associated with the amount of compensation received by CEO? Furthermore, the main contribution is a contribution to be practical, that the justice received by the CEO in the form of compensation when they succeeded in raising the value of the company. It is important to ensure the sustainability of good performance, even encourage loyalty to the company's CEO.

Test results showed that the growth of the company's performance has a positive relationship to the amount of compensation received by the CEO in Indonesia. Two of the three financial performance used in the model, the net profit and total assets, is significantly linked to the amount of compensation received by CEOs. While stock returns, did not show a corresponding relationship with what the theory predicted. With these findings, the research hypothesis that says the growth of the company's performance was positively related to the amount of compensation received by the CEO, supported by statistics.

Writing of this article will be organized as follows: background, as has been done before; the theoretical foundation, the literature review, and subsequently used for the development of hypotheses; method of research that would explain the data and sample

used in this study, the research models and statistical tools is used, as well as explanations of research variables. At the end there is a discussion of the results of hypothesis testing, and subsequently given a review of the conclusions, implications, and limitations and suggestions for further research.

2. Literature Review and Hypothesis Development

2.1 Theoretical Grounded

Issues which discuss about influence of the growth of the company's performance on the size of CEO compensation received, still have a great chance for research in Indonesia. Many theories can explain the interaction of both, and among these theories are described separately as below.

2.1.1 The theory of agency

Agency theory is the fundamental theory (grand theory) explaining the interaction (and often in the form of conflict) of the owner with the management. In the agency theory, known also by the theory of agency (Agency Theory) which was introduced by Jensen and Meckling (1976), stated that among the parties concerned, the owner and CEO, in a public company since the separation between the two, there is asymmetric information between both of them. This further encouraged the owners to form an agreement (contract) with the CEO as a tool to direct the CEO to conduct the action that leads to increase welfare of owners.

Using agency theory to explain that the owner requires the management company to increase their wealth, and as a consequence owners will give a bonus to the management on the performance. Through a bonus program, as described in the positive accounting theory, corporate owners try to minimize the moral hazard that may occur as a consequence of the bonus scheme.

2.1.2 The theory of contract

The second contract theory is a theory that can explain the relationship between company performance to compensation. Contract theory is a theory that explains how labor

and investors agree (dealt) on the production parameters, the number of risks and benefits of each party that will emerge in the future. Contract theory also studies how economic actors can establish the rules of the contract, generally when the economic agents in the presence of asymmetric information. Contract theory is also often applied in designing the optimal managerial compensation scheme.

Contract theory has been discussed in the 1960s in studies of economic studies in the area, as described in the study of Arrow (1963). Topics that study the subject of medical care industry explains some facts that may arise from the presence of informational inequality between doctor and patient. In this case, the patient requires the most out of the service provided by a doctor, and will only take advantage of the conditions that give "guarantee" to them for services. Guarantees referred to here is a form of appointment (contract) awarded by a doctor to the patient. In these conditions, trust preferred and doctors will ignore the maximization of their profits from their patient and then trying to give the best effort, since the concept of trust and delegation is applied. Motivational models built with this theory lies in finding ways to motivate the theoretical agent to take appropriate action, even under the insurance contract, if necessary.

Study of Arrow (1963) is a preliminary study that was monumental. He investigated the problems caused by the presence of asymmetric information in markets. In many transactions, one party (usually the seller) has more information on products sold from the other party. Asymmetric information creates and encourages for the next who have more information to deceive the party with less information. As a result, a number of market structures emerging, including in security and authentication which involves a third party (insurance), which allows the market with asymmetric information to function. In the relationship between company performances to compensation, the owners are realizing that they do not have much more information than the CEO, and then create a contract that can provide security for them. Contract is intended to direct the CEO to act that leads to the increasing wealth of the owner. However, long-term contracts between the company and the CEO can not be managed just like that. Agrawal and Nasser (2010) explains that there is

still debate about whether the CEO contract is a long-term effective bargain or control of power can be held by CEO.

2.1.3 Equity theory dan expectancy theory

Traditionally, payments motivation can be explained using two theories, equity theory and expectancy theory (Ellig, 2007). Equity theory predicts that individuals will improve performance if they believe the level of payment they receive is greater than the outcome, and conversely, the performance will decrease if they believe the level of payments lower than the performance they provide. Proportion of these three theories of justice (distributive justice, procedural justice and referent cognitions), distributive justice to be an assumption of the relationship between performance with compensation.

Distributive justice is a concept that underlies the theory of justice (Adams, 1963, 1965; Blau, 1964; and Homans, 1961 - in Lindquist, 1995). In the formulation of the theory of justice, Adams describes the comparison of reference that often occurs in each individual. However, he suggested that individuals will use themselves as a comparation to reference. Individuals feel the distribution of justice as the ratio of output to their input. Distribution of justice is created when there is a proper balance between the input and the output, or when the ratio is 1. Therefore, if executives feel confident that they receive compensation in accordance with the performance they have given, then the initial reaction was a desire to be loyal to the company.

Explanation of equity theory is supported by the expectancy theory, which explains that individuals will increase their output in the hope to receive increased payments. For the case of the executive, if the individual does not receive the consistent improvement of the performance improvements they provide, individually (using the equity theory) is likely to degrade their performance or find a new job. Ellig (2007) offers an illustration to explain the relationship between effort, performance, and payment.

2.1.4 The theory of the labor market for executives (Labor Market Theory for Executives)

This theory has very well explainanation on CEO compensation at the market who have been able to target CEO talent. CEO compensation may be viewed as a market response to

the specific expertise that is owned by the CEO. Labor market will be strongly influenced by economic conditions and the nature of a country relative to the supply and demand for the caliber CEOs. So if it is a relatively good performance (increased) from year to year, followed by high compensation, this may be an indication that the economic conditions of the labor market (the executive) has gone well. On the research held by Finkelstein and Hambrick (1988), managerial labor market is used as one of the variables that determine CEO compensation, when they doubt the existence of bias that occurs in the setting payments for the CEO.

2.2 Previous research addresses the issue of corporate growth and compensation

The terms of compensation, usually divided into two categories, intrinsic and extrinsic compensation [see Ellig (2007), and Porter and Lawler (1968)]. Intrinsic form of compensation is usually associated with autonomy and power which are obtained in the organization. Meanwhile, extrinsic compensation in areas where a person works can be seen from the type of work, the opportunity to grow, and more recognition of a person, other than payments received from the organization. In this study, the compensation in question is the extrinsic compensation. Compensation referred to in this study is the whole of financial reward or remuneration which are disclosed in the company's annual report.

Research by Jensen and Murphy (1990), became a widely used benchmark of economic research in the field of study compensation. A total of 350 companies they choose to be tested in a model of research, and found that the compensation is pretty close to the company's performance. If the findings of Jensen and Murphy models show close enough compensation to performance, the Myers and Majluf (1984 - in Haubrich and Popova 1998) which uses a model based on the model of investment, stating that the compensation is so strongly tied to company performance. Some previous research suggests that compensation is determined by the achievement of corporate performance. Haubrich and Popova (1998) is one of the researchers who made the paper Jensen and Murphy to be a reference. Haubrich and Popova study aims to develop a model framework that can be used in an optimal

compensation contract. They found a scheme which is able to explain about the linear compensation schemes assumed by Jensen and Murphy (1990) implicitly and even explicitly by other researchers did not show the optimal compensation of contracts.

Jensen and Murphy (1990) assessed the relationship between CEO pay to performance. On average, the welfare of CEO changes by $ 3.25 per shareholder wealth change of $ 1000. Authors show that managerial ownership declined since the 1930's and subsequently lead to decreased sensitivity of CEO compensation received. This condition may be consistent with the political. This paper is a classic work in archival research in the areas of CEO compensation, which is used a lot of next research. Study held by Jensen and Murphy (1990) tested the sensitivity of CEO compensation received shareholder return. In particular, Jensen and Murphy saw a change occurs in payments to the CEO of any change of U.S. $ 1000 value of property received by shareholders. This can be seen with the increased salary and bonus of U.S. $ 3.5 for the increase in shareholder wealth. In statistics, these findings are positive and significant. Although these findings suggest that this argument is consistent with the hypothesis, but Jensen and Murphy believe these results as the findings are not consistent with the theory because the relationship is found to be too small than expected to occur. They argue that the internal and external political pressures have resulted in compensation and performance relationship to have a decreased sensitivity.

Deckop studies (1988) which refers to the study of Lewellen and Huntsman (1970) about the factors that determine CEO compensation, is a preliminary study that discusses CEO compensation has been made before 1990. Deckop using three accounting variables are Sales (Sales), Profit (Profit) and Equity to be controlled by the type of industry. Deckop Studies (1988) that uses the 120 companies in the United States in the period 1977-1981, showed that sales and profits found to be significant as a determinant of compensation, in which profits are strongly linked to compensation, while equity related weaker against compensation. Deckop findings showing that a very powerful profit related to compensation consistent with Lewellen and Huntsman (1970). But Deckop findings which found that

income is the best predictor for compensation is not consistent with previous research that has been done by Roberts (1959), and McGuire, Chiu, and Elbing (1962) who found that the sales are used as a proxy for firm size is more strongly correlated with compensation compared to income. These results indicate that the CEO be given incentives to maximize firm size compared to profitability (profitability) of the company (in Deckop 1988).

Faulkender et al., (2010) emphasize the issue of compensation and corporate performance. They suggest reforms in the determination of compensation to the manager, when the high compensation given to the CEO is not accompanied by the creation of the performance of the company or property owner. On the other hand, Barros and Nunes (2007) explained that the compensation-performance contract which was originally intended to align the interests of the principal-agent, in the end it gives flexibility to the management to gain an advantage because of the measures provided in the accounting standards can be manipulated by management. They suggested that the board remain to supervise the executive.

Executive employment market will be very sensitive to the executives who have a special talent, so the size of compensation to individuals like this will be very important. Studies Faulkender et al. (2010) discusses each of the three aspects of the problem; the level of payments, payment structure and setting the payment process. In terms of compensation structure, of several executives who receive a salary in the form of stock or stock options, it has the undesirable effect when it actually encourages executives to be more willing to take additional risks. However, these changes are intended to improve the process on the target area, such as the mechanism of governance and transparency in the payment of compensation by using the payment through the bank.

Magnan and St. Onge (1997) conducted an investigation of how the relationship between bank performance and executive’s compensation influenced by the level of executive managerial discretion. Secreted managerial level is characterized by the presence of "range" of the policy options available to managerial, executive behavior that can be programmed, ambiguity between cause and effect in the company and the uncertainty of

outcomes. Because the points are ultimately complicate the discretion of the director (in the case of Canada) to measure the performance of the executive, the determination of executive compensation policies are also becoming more difficult.

The results Magnan and St-Onge found that executive compensation is more strongly linked to the performance of the company that managerial discretion is higher than the company's low managerial discretion. In his paper, Magnan and St-Onge explained that the pattern of managerial discretion is determined by many conditions, such as the strategic nature of the company who can be identified through service orientation (Clinch and Magliolo, 1993; Ely, 1991; Lambert and Larcker, 1987; Rajagopalan and Prescott, 1990; Sloan, 1993), the extent of diversification and complexity of corporate business, international or / and super-regional (Murthy and Salter, 1975, Napier and Smith, 1987; Lambert and Larcker, 1987), and the regulatory environment in which the company stands, such as whether the branch establishment permit easier or not (Hambrick and Finkelstein, 1987; Smith and Watts, 1992) - in Magnan and St-Onge (1997). The results of this study indicate that the higher managerial discretion the more to determine the amount of compensation to be received by the management because managers have the opportunity to explore the activities of the company to book the incoming cash flow. So for the same relative value of compensation in similar industries (in this sample is banking) is a company that has a high managerial discretion will further strengthen the relationship between the financial performance of the compensation received by executives.

Kaplan study (1998) is one of the many studies that have contributed in a practical issue of CEO compensation. Economic conditions in America which was quite alarming, when too many CEOs get paid a very special (high) but the payment failed to motivate the CEO to take the company to perform well, or at least the average of the industry, Kaplan has been a motivational research . The number of complaints about the bonus plan for executives of companies in the United States, because in fact no attempt has been made asymmetric to the executive to improve company performance.

Using a sad phenomenon in the American economy written in the book written by Crystal (1991), Kaplan developed two models of the dynamic between principals and agents that incorporate the efficiency wage (effeciancy-wage) and the link between pay and performance (the researchers used to write the pay- for-performance). The first model is a pay-for-performance, suggesting that the profit-maximizing firms in an environment (an environment that is meant here is an industrial environment) tend to have certain high-performance variation, which might be an option in the awarding of more compensation is also high, although perhaps the performance is bad. Kaplan offered the first model, is aimed at companies that have CEOs who are working hard in creating the company's performance. Consideration of the size of the company that offered in the study Frydman and Saks (2010) provide a solution to the problem efficiency wages are debated in the study of Kaplan (1998).

Research conducted Frydman and Saks (2010) stimulated by the increasing debate about executive payment at public companies, while previous studies increasingly show that the findings are not conclusive. They conducted an analysis of the relationship between compensation with the company's growth from the year 1936-2005. By using the sample design and a different methodology to assess the components of remuneration that are not available in its entirety, they are ultimately unable to provide a systematic explanation of the development of executive compensation over time. They present new evidence on the trend of long-term compensation through the collection of data manually (hand collecting) to the individual executive remuneration of the proxy statements and 10-K financial report. Relationship they found was flat between the two during the 1940s to 1970. But after the 1970s to 2005 (during the last three decades) the relationship of executive compensation with the company's growth is strong.

Frydman and Saks paper explains that the size of payments to executives parties related to the size of the company. Competition for corporate managers who have rare skills likely will result in the compensation given to executives getting bigger. This is consistent with the prediction that large companies, will offer higher payments to certain managers than

smaller companies (Kucas, 1978; Rosen, 1981; Tervio, 2008; Gabaix and Landier 2008 - in Frydman and Saks, 2010). Firm size is also a variable to be included in research models of Nicolitsas and Conyon (1998). They used a proxy firm size by total employment, total real assets and real sales, and found evidence that the payments to the CEO are made on small firms are more sensitive to sales growth.

In a previous study, we conducted an analysis of CEO compensation contracts are linked to organizational performance. Puffer and Weintrop (1991) explains that CEO compensation contracts are generally considered a bonus scheme that usually takes three forms: stock option plans that are based on future stock prices, the performance is based on the achievement of corporate earnings, and, on the lower level is targets of a particular accounting ratios set by the board of directors (within the United States).

Puffer and Weintrop (1991) states that CEO compensation contracts often include a bonus scheme based on more than one indicator of corporate performance. There are at least two reasons underlying this practice which is derived from agency theory scheme. The first, based on a theoretical model contracts which indicates that some increase in the performance criteria have been established, has the consequence of increasing the effectiveness assessment of the CEO which more optimal (Holmstrom, 1979). Because each of the criteria included in the compensation can measure the performance of the contract is different, combining several different performance measures can help to eliminate some of the disturbances (bias) that contained in each measure, thus providing a clearer assessment of the contribution of the CEO on organizational performance. The second reason is based on several performance indicators that are used for performance measurement, should be able to encourage the CEO to act in the interests of shareholders and to protect some interest of its own CEO (the compensation to be received). If not, the CEO will feel threatened or even feel exploited, so it probably will not act to give the best interests of the organization (Lambert and Larcker, 1987). As mentioned previously, Puffer and Weintrop (1991) offers three types of performance assessment that is used as the CEO bonus plan, the stock plans, target earnings, and accounting ratios. Stock planning often

appears as a boost for CEO compensation contracts in the form of stock options, stock appreciation rights, phantom stock, dividend units, and restricted stock (Larcker, 1983).

Another study also found that the compensation will be provided in accordance with the performance of the CEO is Frydman and Saks (2010). They describe the main hypothesis that is important today in explaining executive compensation, CEO payment is by using stock options associated with the growing and ever contract manager within the firm (Bebchuk and Fried, 2003; Bebchuk and Fried, 2004; Kuhnen and Zwiebel, 2007 - in Frydman and Saks, 2010). Garvey and Milbourn (2003) states that there is still controversy about the relationship between executive compensation with the company's stock market value. Evidence obtained from previous studies showed results that were not strong enough to conclude the performance of large-size market affects compensation. There is also ample evidence from previous studies that show the diversity of the payment package for the executive, as described in the Contract Theory. However, when value stocks are relatively stable, many companies are tying his managers with stock market performance.

Associated with the relationship between executive compensation with the company's stock market value, although some researchers had previously found a strong relationship between the two (Hall and Murphy 2003; Jensen, Murphy, and Wruck 2004; Gabaix and Landier 2008), Frydman and Saks (2010) found a weak association between executive compensation to the company's market value and stated that the relationship is not always strong in the last 25 years. Frydman and Saks using the aggregate size of the company that used in the study Gabix and Landier (2008).

Target earnings is a second method that can be used to evaluate the performance of the company by using the annual earnings targets. Although there are linkages between stock prices and earnings, we know that there is no evidence to suggest that stock prices are set of multiples of earnings. Additional information provided by earnings will assist users in distinguishing the impact of CEO actions and exogenous factors beyond the control of management. Target earnings also helped balance the impact of risks will be borne by the CEO if they are only compensated with stock (Lambert and Larcker, 1987).

Bonus program by using the annual earnings targets is an overview of the compensation plan in the United States. In 1980 the bonus plan based on earnings targets already in use by 90 per cent of the 1000 largest manufacturing companies in the U.S. (Healy, 1985). Bonus plan based on earnings is a substantial part of short-term executive compensation. For example, in 1978 the average ratio of accounting bonus of base salary for senior executives is 52 percent (Fox, 1980). Bonus plan based on earnings targets is also commonly used in Indonesia.

2.3 Hypotheses Development

Results of study that explain the link between company performance to compensation is not consistent. The study by Jensen and Murphy (1990), as also described in the study Takahashi (2006), found that of U.S. $ 1000 increase in the welfare of the company owner, was only U.S. $ 3.5 increase in payments to be received by the executive. In the study Haubrick and Popova (1998) using 350 sample companies selected through a previous survey conducted by Jensen and Murphy (1990), found that the results can be explained that the data they use is consistent with optimal incentives as the theory predicted. Haubrick and Popova (1988) argued that the compensation given to the CEO of his company is considering the performance of the firm (Myers and Majluf, 1984). However, Jensen (1989) argued that the actual political factors also play a role in influencing the company to use the company's performance in determining compensation.

Green and Heywood (2007) provide an explanation in terms of job satisfaction related to payments received by workers. His paper investigates the impact on several dimensions of job satisfaction if the payment is based on performance which has been achieved. Green and Heywood study findings show the result that there is strong support that the performance is used as the basis for setting payment will be given to employees, can increase employee intrinsic motivation. This condition occurs because of increasing job satisfaction, as predicted in theory of expectancy.

Several previous studies which suggest that the compensation is determined by the achievement of corporate performance is Jensen and Murphy (1990), Myers and Majluf (1984), Haubrich and Popova (1998), Deckop (1988), Lewellen and Huntsman (1970), and Frydman and Saks (2010). A study conducted by Jensen and Murphy (1990) showed that the compensation is quite close to the performance. This finding is consistent with Myers and Majluf research results (1984 - in Haubrich and Popova 1998), using a model based on the model of investment, stating that the compensation is so strongly tied to company performance.

Faulkender et al., (2010), and Barros and Nunes (2007) are two researchers who provide enlightenment as well as reinforce the issue of compensation and corporate performance. They suggest reforms in the determination of compensation to the manager, when the high compensation given to the CEO is not accompanied by the creation of the performance of the company or property owner, one of which is to continue to supervise the executive (in and Nunes Barros, 2007).

Using the results of research and review the appropriate assumptions with theoretical predictions described in the previous section, the hypothesis of this study are:

Ha: the growth of the company's performance has a positive impact to CEO compensation growth

There are three corporate performances will be tested in this study, namely net income (earnings), stock prices and company size (poxyfied with total assets).

(1) Hypothesis for the relationship of net income growth to CEO compensation growth

Healy (1985) research in the area had been preceded by a bonus scheme using ernings changes. Healy suggests that by using the bonus plan earnings management may encourage moral hazard, namely the selection of accounting procedures that can increase profits, which in turn affects the maximization of compensation they receive. Other studies that use earnings as variables related to the compensation is performed by Puffer and Weintrop (1991). They stated that one of the bonus scheme which is applicable to the

assessment of planning performance on the achievement of the target company's earnings. Research on other U.S. companies conducted by Deckop (1988) by using a sample of 120 companies, the period 1977-1981, showed that sales and profits as a significant determinant of compensation, which is found to be very powerful profit related to compensation, while equity related weaker against compensation. Deckop argued that research findings are consistent with Lewellen and Huntsman (1970).

This study tries to predict that the growth of the company's performance will affect the amount of compensation received by CEOs. Furthermore, a hypothesis which describes the relationship between changes in the compensation income is:

Ha1: net income growth is positively related to CEO compensation growth

(2) Hypothesis for the relationship of stock prices growth to CEO compensation growth

Previous studies use more stock options as a bonus scheme preparation (see Puffer and Weintrop, 1991; Balsam and Miharjo, 2007; and Frydman and Saks, 2010). However, because the data of stock options is not easy to obtain in Indonesia, this research will use the stock price as a proxy of the market performance of companies. Lambert and Larcker (1985) is a researcher who see the good and bad side, if the stock price is used as a determinant of compensation. On the one hand, ownership of company shares will be the impetus for the CEO to do projects that enhance the company's stock price. But on the other hand, if only by relying on the stock price as a consideration of the determination of compensation, it can overload the CEO with a big risk, because stock prices can not be controlled by management.

Lambert and Larcker argument (1985) is supported by Garvey and Milbourn (2003), who in an article stating that there is still controversy about the relationship between executive compensation with the company's stock market value. The inference that the market will affect the performance of large-small compensation not show strong enough results. Even Frydman and Saks (2010) found a weak association between executive

compensation to the company's market value and stated that the relationship is not always strong in the last 25 years. However, the study of Hall and Murphy (2003); Jensen, Murphy, and Wruck (2004); Gabaix and Landier (2008), found a strong relationship between stock prices and compensation.

Of debate and research on the theory by using the assumptions described in the previous section, the hypothesis related to the relationships built with the compensation stock price are:

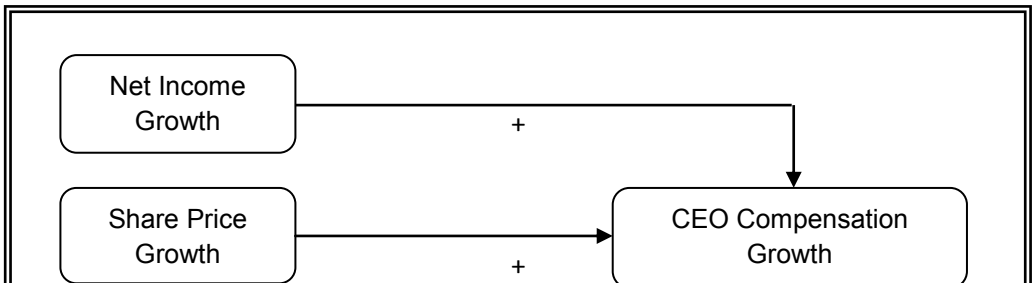
Ha2: stock prices growth are positively related to CEO compensation growth

(3) Hypothesis for the relationship of firm size growth to CEO compensation growth

Frydman and Saks using the aggregate size of the company that used in the study by Gabix and Landier (2008). The size of the company used in their research is selling. However, some researchers also use the asset as a variable representing the size of the companies in research of this field. Their study indicates that the CEO will be given incentives in order to motivate CEOs to maximize the size companies than to company's profitability. Asset valuation has been used Byström (2010) to conduct assessments on executive compensation. Asset is also an important variable that is used by Cooper, Gulen and Ray (2009). Asset variables taken into account in some of the variables they use. Meanwhile, Farrell and Winters (2001) also found a significant positive relationship between total assets and the payments to company executives.

From two sizes of companies that used in previous studies, this study will use total assets as a proxy for company size. On the above explanations, and theories that have been described previously, the hypothesis that describe the relationship between size growth of the company with compensation are:

Ha3: firm size (total assets) growth is positively related to CEO compensation growth



Picture 1 Research Model

3. The research method

3.1 The research sample

Sample of this study is as much as 395company-year, with growth data used are from the company's annual report data in 2005-2008. All companies listed on the Indonesia Stock Exchange has a chance as a sample of this study. Availability and completeness of the data into the final determinant of whether a particular company at a certain period can also be a sample of the study. The growth of the company's performance for three consecutive periods (2005/2006; 2006/2007, and 2007/2008) then compared to the (growing) amount of compensation received by CEOs in the same period.

3.2 Econometric Model

The hypothesis of this study which says that the growth of corporate performance is positively related to the amount of compensation will be tested using a model such as the following equation:

$$Comp_{it} = \alpha_0 + \alpha_1 NI_{it1-3} + \alpha_2 SP_{it1-3} + \alpha_3 Assets_{it1-3} + \alpha_4 MoB + \alpha_3 Age + \alpha_3 Industry + \varepsilon_{it} \quad \text{..... (1)}$$

Description: Comp = Compensation; NI = Net income: SP = Stock Price. Mob = number of the Board (of directors and commissioners), Age = age of firm (1 if the company's age <10 years; 2 if the company's age 10 to 20 years; 3 if the company's age> 20 years); Industry is the type of industry (1 = state owned enterprices and 0 = others).

3.3 Research Variables

3.3.1 Dependent variable

The dependent variable of this study is CEO compensation growth. Data obtained compensation from the company's annual report, as well as from the JSX/IDX Watch and Bisnis Indonesia.

3.3.2 Independend variable

The study used three independent variables which is a proxy measure of corporate performance growth: growth of net income, growth of stock returns, and the growth of total assets.

3.3.3 Control variable

To provide assurance that changes in compensation due to the growth of the company's performance, this study will include the control variables. The selected control variables are Age = age of firm (1 if the company's age <10 years; 2 if the company's age 10 to 20 years; 3 if the company's age> 20 years); Industry is the type of industry (1 = state-owned and 0 = Non- SOE), all three control variables that are commonly used in cross-sectional sample.

4. Testing Results and Discussion

Test results showed that the growth of the company's performance has a positive relationship to the amount of compensation received by the CEO. At least two of financial performance used in the model, i.e. profitability (Net Income) and assets, is significantly linked to the amount of compensation received by CEOs. While the share price, showed no relationship in accordance with what the theory predicted.

4.1 Descriptive Statistics

Descriptive statistics is a way to present information about the group or collection of data used in the testing of a study. This information is useful to know the data structure briefly. Each of the variables used to test the third hypothesis will be described separately, as below.

Changes in compensation. CEO compensation is the value of changes in the mean (average) of 0.32, median 0.135 and average (mean) is equal to 0.322. Furthermore, the maximum change in CEO compensation received amounted to 15.55 times that the PT

Squibb Indonesia Tbk, from 2006 to 2007. Compensation changes also are at the lowest point of 2005 to 2006 in PT Indo-Rama Synthetics Tbk, amounting to -0.902%. In the Indo-Rama period showed virtually no growth in a good performance. Assets grew only by 6.1%, -3.3% while corporate profits and stock prices fell as much as -108.8%.

Net Income growth. Growth in net income as a mirror the performance of the CEO is at the mean (average) of 0.43, median 0.102 and average (mean) is equal to 0.426. The maximum value is the net profit growth of 48.5 times that in PT Medco Energy Corporation Limited, from 2007 to 2008, while PT Multi Prima Sejahtera / Lippo Enterprises Inc. has the lowest point in the period 2006 to 2007 in the amount of -20.206.

Stock price growth. Growth stock prices reflect more confidence in the market to corporate management. In connection with the performance of the CEO, the stock price indicates how much more confidence that the CEO can perform the market provides a wealth of shareholders. Value of share price growth had a mean (median) of -1.8. This condition is due in 2007 and 2008 world crisis, and very influential in the market. In many of the news, explained that almost all of the stock price decline. The median stock price of -1.055, while the average (mean) of -1.795.

Total assets growth. Same thing with the growth of its net income, total asset growth can be a measure of CEO performance. Growth in total assets has a mean (average) of 0.29, median of 0.124 and the average (mean) of 0.288. Maximum value of total asset growth amounted to 20.9 times that in Ciptojaya Kontrindoreksa Tbk PT, from 2007 to 2008, while Dynaplast Tbk PT in the same period (period 2007-2008) had the lowest point that is equal to -0996.

Table 1 Description of statistics

Nama Variabel	Mean	Median	Average	Max	Min	StdDev
Compensation	0.32	0.14	0.32	15.55	-0.90	1.057
Net Income	0.43	0.10	0.43	48.48	-20.21	4.54

Assets	0.29	0.12	0.29	20.97	-0.99	1.51
Share Price	-1.8	-1.06	-1.79	29.23	-128.30	10.51
Member of Board (MoB)	0.01	0.00	0.01	1.25	-0.50	0.17
Age	1.81	2.00	1.81	3.00	1.00	1.81
Industry	19.67	22.00	19.67	34.00	1.00	10.28

Maximum value of share price growth amounted to 29.23 times that the PT BFI (Bunas Finance Indonesia) Limited, was in the period 2007 to 2008, while PT Bank Negara Indonesia Tbk is at its lowest share price growth in the period 2007 to 2008 in the amount of - 128.39. BNI shares fall in value in 2008 is the accumulated value of the shares continued to decline from the previous year. In 2008, BNI stock prices stay Rp600.

4.2 Hypothesis Testing

4.2.1 Testing of net income growth was positively related to CEO compensation growth

Financial performance as represented by the growth of corporate profits showed a significant relationship to the amount of compensation received by the CEO. T-value of 4.394 count proves that profit growth is in the region H0 rejection, or in other words that net income growth has a positive relationship in determining how much compensation will be given to the CEO. The strength of this relationship indicated by the R value of 21.6%, adjusted R-square of 10.5%, and with a significance of 0.000. These test results provide a strong reason for researchers to accept the research hypothesis that states net income growth is positively related to the CEO compensation growth.

The results of this study support previous research that found the significance of income as a determinant of compensation in the period 1977-1981 of 120 companies in the United States carried out by Deckop (1988). Deckop find very strong profit-related compensation, while equity-related weaker. Deckop also argued that research findings are consistent with Lewellen and Huntsman (1970). Support is also given on the research study conducted by Puffer and Weintrop (1991) who found the achievement of corporate earnings as one of the variables that determine a company bonus scheme. Conditions in Indonesia is also, in line

with the study of Healy (1985) who found a bonus plan based on earnings targets already in use by 90 per cent of the 1000 largest manufacturing companies in the U.S. in 1980.

4.2.2 Testing of stock prices growth was positively related to CEO compensation received

The second financial performance in the model is a growth company's stock price. As described in the previous section, the stock price is market performance can not be controlled by company management, including CEO. So that the test results on the growth of stock prices that do not show the significance of the magnitude of the compensation received by CEOs. Test results show that the value of t-count of 0.385 indicates that the total growth in stock prices are on the acceptance of H0. These results also indicate that the growth in stock prices have no connection with the compensation given to CEOs. The weak relationship is indicated also by the value of R of 1.9%, adjusted R-Square of -0.002, the significance of 0.70. Overall results of this test does not provide reason enough for researchers to receive the initial allegations of this study that the growth of the company's stock price is positively related to the amount of compensation received by the CEO. Important justification for why the stock price growth is not a determinant in awarding compensation, as explained in Garvey and Milbourn (2003), that in the market which already has achieved stability, it would be fair if the stock price is used as a measure of CEO performance, and subsequently became a reference in compensation.

The controversial findings on the relationship between stock prices by the amount of compensation has been described in the previous section. Lambert and Larcker (1985) is a researcher who has been explaining the good and bad, if the stock price is used as a determinant of compensation. Well, when the CEO owns a company that will be the impetus for the CEO to do projects that enhance the company's stock price. Bad, if only by relying on the stock price as a consideration of the determination of compensation, can overload the CEO with a big risk, because stock prices can not be controlled by management. Lambert and Larcker statement (1985) is supported by Garvey and Milbourn (2003), which states that the controversy about the relationship between executive compensation with the company's

stock market value is still there to this day. The inference that the market will affect the performance of large-small compensation does not show strong enough results.

Failure of this study are expected to accept the hypothesis of the relationship of growth stock prices is positively related to CEO compensationgrowth, other than in accordance with Lambert and Larcker argument (1985) and Garvey and Milbourn (2003), means also support previous studies which found a weak association between executive compensation to the market value of the company and stated that the relationship is not always strong in the last 25 years (Frydman and Saks, 2010). However, these studies failed to support the study by Hall and Murphy (2003); Jensen, Murphy, and Wruck (2004); Gabaix and Landier (2008), all of which found a strong relationship between stock prices to compensate.

4.2.3 Testing of total assets growth is positively related to CEO compensation growth

The third of financial performance which participated in this hypothesis was tested in the growth of total assets. Similar to the results of testing the growth of earnings, total assets also showed a significant relationship to the amount of compensation received by the CEO. *t-value* is calculated at 6.777 indicating that the growth in total assets is in the rejection of H0, or in other words that the growth in total assets has a positive relationship when determining how much compensation will be given to the CEO. The strength of this relationship is also indicated by the R value of 32.3% and adjusted R-square of 4.4%, while the significance for these both relationship is 0.000. The overall results of this test gives a strong reason for researchers to receive preconception of this research that corporate profit growth was positively related to the amount of compensation received by the CEO. This finding is in line with previous research that found that total assets is an important value to be taken into account when determining executive compensation (see Farell and Winters, 2001; Byström, 2010).

4.2.4 Testing of the control variables

To elucidate further the influence of other variables that might explain the amount of compensation received by the CEO, this study included three control variables, namely changes in the number of commissioners and board of directors, company age and type of industry. Changes in the number of board members who show a positive relationship indicates that when the larger members of the board, the greater the compensation received by CEOs. These findings are very logical and is consistent with reality.

Two other control variables, namely age and type of industrial companies, showed no relation to the value of compensation given to the company's CEO. This indicates that the relatively newly established company, can provide substantial compensation to the CEO. As well as any form of industry, whether the type of company owned by state or not, the amount of compensation received by the CEO does not depend on the type of industry.

Table 2 shows the statistical results of testing the relationship between corporate performance and the three control variables (member of board (MoB), Age, and Industry) in the amount of compensation received by CEOs. Furthermore, we will explain each part of hypothesis.

Table 2 Results of testing the hypothesis

Firm Performance	R	R Square	Adj. RSquare	T	Sign
Net Income	0.216	0.047	0.044	4.394	0.000
Share Price	0.019	0.000	-0.002	0.385	0.700
Total Assets	0.323	0.105	0.102	6.777	0.000
Control Variables:					
- Member of Board (MoB)	0.274	0.075	0.073	5.654	0.000
- Age	0.069	0.005	0.002	1.376	0.170
- Industry	0.029	0.001	-0.002	-0.581	0.562

Overall testing this hypothesis provides empirical evidence that the amount of compensation awarded to a company depends largely on how much the CEO can create the growth of the company's financial performance. How established is age of the company and any type of industrial enterprise, the compensation will have no effect on both grounds. So in this case, the accounting information provides an important role to define corporate

governance as a very important decision for the company's key personnel. These results also to provide empirical evidence of the usefulness of accounting information in corporate decision making.

5. Conclusion, Implications, Limitations and Suggestions

The amount of compensation given to the CEO of their company is in accordance with the performance of the CEO. When the CEO successfully brought the company to significant growth, the value of compensation received by the CEO will get better too, and vice versa. Profit and total assets becomes critical size, when the company determines how much compensation to be awarded to their top leadership.

Compensation received by CEOs at major companies in Indonesia in accordance with the performance they put on the company. Predictions of theories that have been raised earlier in this paper has been demonstrated empirically. Furthermore, it shows the usefulness of accounting information in the determination of the bonus program in Indonesia.

Another implication is that the labor market for executives in Indonesia has been on an established position. This is indicated by the compensation received by CEO is significantly influenced by their performance. These conditions may encourage the work ethic and positive dynamic among executives in particular, and labor in general. With the talent you have, the success of the company where the loyal brings to the position of a lot better growth, increased prosperity will provide the labor as well.

This study uses only three of the many measures of corporate performance. It will be possible for further research to use other performance measures, especially those that have been done in previous research in other countries. The new findings on this issue is still very much needed, because research in the area of CEO compensation has not been done in Indonesia.

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