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paper text:

1 Australian Journal of Basic and Applied Sciences, 9(23) July 2015, Pages: 729-737 ISSN:1991-8178 Australian Journal of Basic and Applied Sciences Journal home page: www.ajbasweb.com Integrating the Mediation and

2 Moderation Variables to Explain the Effect of Ownership Structure on Firm Value in Indonesian Stock Exchange 1Sri Handayani, 2Sutrisno, 2Aulia Fuad Rahman, 2Imam Subekti

1Ph.D Accounting Program, Brawijaya University and Diponegoro University, Malang-Indonesia, 65144
 2Economics and Business Faculty, Brawijaya University, Malang-Indonesia, 65144
 ARTICLE INFO
 ABSTRACT Article history: Previous studies about the effect of ownership structure on firm value based on Agency Received 1 June 2015 Theory framework show inconsistent result. Agency Theory perspective ignores both Received in revised form 17 June situational and conditional factors surrounding firm's operations and effecting on firm 2015 performance (Aguilera & Jackson, 2003). Eisenhardt (1989) recommends to develop a Accepted 25 July 2015 Agency theory by adding other theories that intersect in the assumptions and spectrum. Available online 15 October 2015 In responding to this suggestion, this study was carried out to investigate the mediation- moderation model of the relationship among dividend, free cash flow, ownership Keywords: structure and firm value. This relationship was developed

16based on the framework of Entrenchment Effect, Free Cash Flow, Agency Theory that

was integrated with the framework of Contingency Theory. Ultimate Shareholder's Domination Samples are 346 firms-years of listed firms in Indonesia Stock Exchange 2008-2012 to Power, Dividend, Type II Agency exclude State Ownership Enterprise/SOE. Purposive sampling method with judgment Conflict sampling is used. Hypothesis testing is done with path analysis. Research results show that the interaction between ultimate shareholder's domination power and free cash flow affect indirectly firm value through dividend. ©

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2Integrating the Mediation and Moderation Variables to Explain the Effect of Ownership Structure on Firm Value in Indonesian Stock Exchange.

1Aust. J. Basic & Appl. Sci., 9(23): 729-737, 2015 INTRODUCTION

Stock ownership structure is an important factor to determine the firms value (Demsetz and Lehn, 1985). Stock ownership structure reflects the agency conflict (Achmad, Rusmin, Neilson, & Tower, 2009). Most of firms listed on Indonesia Stock Exchange

18have a pyramidal ownership structure (Claessens, Djankov, and Lang, 2000; Claessens and Fan, 2002; LaPorta, Lopez-de-Silanes, & Shleifer, 1999).

Pyramidal ownership structure will create a concentrated ownership structure of single shareholder. These conditions will create a potential

5conflict between the ultimate shareholders with minority shareholders or agency conflict

type II (Villalonga & Amit, 2006) as well as legal protection for weak minority shareholders (LaPorta,

27Lopez-de- Silanes, Shleifer, and Vishny, 2000). Agency theory– entrenchment hypothesis states that

firms with more concentrated ownership structure have a tendency to have lower firm value (Demsetz, 1983; Shleifer and Vishny, 1997; Stulz, 1988). Concentrated ownership structure will lead to dispersion between control rights and cash flow rights owned by ultimate shareholder. If the

28control right is greater than the cash flow right, shareholders will have

the domination power. Greater dispersion between control rights and cash flow rights means greater dominance of rights. Ultimate shareholder's domination power gives ultimate shareholder to determine the firm's policy. It provides incentives to the ultimate shareholder to act which has entrenchment effect. There is a tendency of the higher such as increasing tendency to decrease firm value. Research of Thomsen (2006), Ahmad et al. (2009), Barry-Ariffin, Nor, and McGowan (2010), Barry-Ariffin (2010) and Bae, Baek, Kang, and Liu (2012) supports the entrenchment hypothesis. Adversely, agency theory-monitoring hypothesis states that higher ownership concentration will improve oversight quality to managerial opportunistic behavior so

that ownership concentration will improve firm performance (Shleifer and Vishny, 1986). Some results of empirical studies support this hypothesis (Claessens et al., 2000; Andrew, 2008). Shleifer and Vishny (1997) provide evidence on monitoring and entrenchment hypothesis that effect of control right of ultimate shareholder's domination power ownership has non linear relationship with Corresponding Author: Sri Handayani,

26JI Prof. Soedharto, SH, Tembalang, Semarang, Jawa Tengah, 50275, Indonesia.

Phone. (024)76486843; E-mail: handayanifeundip@yahoo.com firm value with an inverted U shape. On other hand,

19Demsetz and Lehn (1985); Demsetz and Villalonga (2001) show no relationship between the ownership concentration on firm' s value. Empirical studies

2the effect of ownership structure on firm' s value that developed in

Agency Theory framework gives inconsistent results. Aguilera, Filatotchev, Gospel, and Jackson (2008) state that agency theory is a closed system because agency theory perspective ignores situational and conditional factors which also affect on firm performance (Aguilera & Jackson, 2003). This weakness is considered will affect on accuracy of agency theory

2to explain the effect of ownership structure on firms value in

different institutional contexts (Aguilera et al., 2008; Aguilera & Jackson, 2003). Eisenhardt (1989) recommends to develop an Agency theory by adding other theories that intersect with the assumptions and spectrum. It is intended to increase the complexity and improve the statistical explanation power of Agency Theory. Pizzo (2013) recommends to consider contingency variables are supposed to affect on firm value to bridge inconsistencies results of previous empirical research. In responding to this suggestion,

23this study objectives investigate the effect of ownership structure on firm's

value within framework of Agency Theory and is integrated with variables in Contingency Theory perspective. Moderation and mediation model is developed to broaden and to strengthen the spectrum of agency theory

2to explain the effect of ownership structure on firm' s value.

Dividend becomes a mediation variable to reduce the negative effects of ownership structure on firm's value. Meanwhile, free cash flow as a contingency variable is moderator variable to strengthen the mediation effect of dividends on relationship between ownership structure and firms value. Literature Study And Development Hypothesis: Agency Theory- Entrenchment Hypothesis: Framework of agency theory- entrenchment hypothesis states that concentrated ownership structure tends to create imbalance between the amount of control rights and cash flow right owned by ultimate shareholder. Ultimate shareholders will have

15control right greater than cash flow

rights

15(Claessens et al., 2000). Obtaining greater control rights from cash flow rights

provide ultimate shareholder's domination power. Greater

11difference between control right and right cash flow creates greater the power of ultimate shareholder'

s domination power, so that greater incentive for ultimate shareholders to take the policies and actions to affect of entrenchment. Therefore, pyramidal ownership structure shows that greater the ultimate shareholder's domination power create a tendency to lower the firm's value (Demsetz, 1983; Shleifer and

Vishny, 1989; Stulz, 1988). Much of empirical research support the agency theory-entrenchment hypothesis as Thomsen (2006); Ahmad

7et al. (2009); Bany-Arifin et al. (2010); Bany-Arifin (2010) and Bae et al.

(2012). From the description can be formulated hypothesis below: H1a: Ultimate shareholder's domination power negatively affect on firm value. Agency Theory-

4Free Cash Flow Hypothesis: Agency Theory-Free Cash Flow Hypothesis states that in case of agency

conflict, distribution of dividends to shareholders will serve as a substitution of corporate governance mechanisms (Jensen, 1986). Dividends as a substitute of corporate governance mechanisms will reduce agency costs through a reduction of resources that are in control of a potential agent to entrench agent. Distribution of cash dividends will align the interests of shareholders with right to control the interests of minority shareholders to affect on entrenchment that is expected to increase firm's value (Baker, Farrelly, and Edelman, 1985; Brickley, 1982; Harry DeAngelo and DeAngelo, 2006; Harry DeAngelo, DeAngelo, and Skinner, 2000; Gordon, 1959; Higgins, 1972; Murekefu & Ouma, 2013; Rozeff, 1982). Dividend payments become part of an effort to make optimum supervision to reduce the agency cost through the reduction of resources under the control agent (Easterbrook, 1984; Farinha, 2003; Iturriaga & Crisostomo 2010; Rozeff, 1982) such as cash distribution to the shareholder in the form of dividend. Dividend intervention on the effect of agency conflict to firm value will lead the effort to create better firm value. Therefore, higher ultimate shareholder's domination power; dividend payout to shareholders is expected to increase firm value. The hypothesis of this study is below: H1b: Dividend mediates the effect of ultimate shareholder's domination power to firm value. Integrating variables in Framework of Contingencies and Agency Theories: Eisenhardt (1989) recommends to develop a Agency theory by adding other theories that intersect with assumptions and spectrum. It is intended to broaden the spectrum, enriching, increase the complexity and the statistical power explanation of Agency Theory. Eisenhardt (1988) conducted an analysis of election between salary compensation and performance-based compensation. To select the best one from of both, Eisenhardt (1988) uses the variables in perspective of Agency Theory and Institutional Theory. Aguilera and Jackson (2003) also use the Agency Theory and Institutional theory. The variables within framework of Agency and Institutional theories are analyzed to explain factors affecting the diversity

8of corporate governance applied in each country. Aguilera et al. (2008) conducted an

analysis

8the effectiveness of corporate governance and its implications for firm policy

based on Agency theory and Contingency Theory. The factors are

12used to explain effect of contingencies corporate governance practices on firm performance,

which based on Agency Theory. Aguilera and Jackson (2010) use the perspective of economics and management, culture and sociology, law and politics to explain differences and similarities of corporate governance practices in several countries. In perspective of economics and management of United States, Britain, Germany, China and France, variables in framework of Agency Theory are used to analyze and explain variations in corporate governance practices among firms. This research expands the Agency Theory. Explanation the mediation effect of dividends on relationship between ultimate shareholder's domination power and firm value as variables within framework of Agency Theory are integrated with free cash flow as a variables within Contingency Theory framework. Firm with free cash flow greater has tendency to increase

5agency conflict between ultimate shareholders and minority shareholders. Dividends as a substitution of

12corporate governance mechanisms are expected to reduce the effects of conflict

on firm value (Jensen, 1986). Dividend payments as a substitute of corporate governance mechanisms will intervene ultimate shareholder's domination power on firm value by reducing free cash flow. Dividend payment is expected to reduce the entrenchment effects of moral hazard actions taken by ultimate

shareholders on firm value. Surplus resources will strengthen the mediation effect of dividends on firm value through ultimate shareholder's domination power ownership. In perspective of contingency theory, free cash flow as a proxy of complexity of organizational problems (Chae, Kim, & Lee, 2009) is an organizational situational factors which will affect on suitability of existing mechanisms in each organization and affect on performance. Free cash flow is expected to strengthen the mediation effect of dividend to relationship between ultimate shareholder's domination power on firm value. Free cash flow strengthen indirect effect of ultimate shareholder's domination power to firm value through dividend. Greater free cash flow can increase dividends ability to mediate the effect of ultimate shareholder's domination power on firm value. The hypothesis of this study is below: H1c: Dividend mediates the effect of the interaction ultimate shareholder's domination power and free cash flow on firm value. Research Methods: Population and Sample: This study population is data (firms-years) of firms listed in Indonesia Stock Exchange for 2008- 2012, except for States Ownership Enterprise/SOE. Sampel was selected using purposive sampling with judgment sampling. Samples are 346 firms- years. Samples selection criterions are summarized in Table 1. Table 1: Determination of Research Samples Criterion Year firms Total Population 1875 Having reporting date other than December 31 (5) The currency reporting is not in rupiah (164) Not in reporting format as defined in Standard reporting of Indonesia (5) Doing Corporation action (merger) (1) Having more than one controller shareholder or the share less than 20% (340) Illiquid shares (21) Negative Cash Flow (77) Uncompleted data (881) Data were processed before Outlier 381 Outliers (to meet the classical assumptions of normality and heterokedasticity (35) Total of analyzed data 346 Source: processed data Operational Definition and Variables Measurement: a. Dependent Variable: The dependent variable is firm value. Firm value is a going-concern firm value that reflects the expected investment in a sustainable future (Myers, 1977). Firm value shows the present firm value for shareholders.

9 Firm's value is measured by Tobin's Q.

b. Independent Variables: Ownership structure is proxied ultimate shareholder's domination power. Ultimate shareholder's domination power (DCFRCR) is defined as the ultimate shareholder's discretion to take the policies, strategies and actions having entrenchment effect. Ultimate shareholder's domination power ownership at end fiscal year end shows the dispersion between control right and

25 cash flow rights (Claessens, Djankov, Fan, and Lang, 2002; LaPorta

et al., 1999; Lemmon and Lins, 2003). A value of 1 means there is not dispersion

6 between control rights and cash flow rights

or no power domination owned by ultimate shareholder. A value closer to 0 indicates greater dispersion

6 of control rights and cash flow rights; it means greater ultimate shareholder'

s domination power ownership. Control right

6 is defined as the smallest value of stock

ownership by ultimate shareholder in ownership chain and greater than 20% (Bany-Arifin et al., 2010). Cash flow right shows the financial claims held by ultimate shareholders at end of i fiscal year that determined by ownership chain of ultimate shareholders. c. Mediator Variable: Dividend (DIVMV) is the mediator variable study. Dividends are defined as profit distribution to shareholders (Rozeff, 1982). Dividend is measured with a dividend yield (Barclay, Holderness, and Sheehan, 2009). d. Moderator Variable: Free cash flow

29 (FCF) is the moderator variable. Free cash flow is defined as excess of cash flows from

the cash requirements

14 needed to fund all projects with positive net present value, discounted at a rate of cost of capital

(Jensen, 1986). Free cash flow reflects firm's ability to fund all projects in future (Uyara & Tausikal, 2003). The measurement is cash balance after operating activities, investing activities and dividends firms at t end year book divided by fiscal at t end year. e. Control Variables: 1. Type of agency conflicts in relation managerial ownership (DMUO). It is measured by a dummy variable, 1 = type II agency conflict, if the manager-shareholder has family relationship with ultimate shareholder and otherwise is 0. 2. The

24 firm size (LnTA) is measured by Ln of total book value of assets 3. Audit quality is

proxied by public accounting firms affiliated with Big 4. Audit-quality (DUAD) measured by

22a dummy variable, 1 = if firms are audited by Big 4 affiliation and otherwise is

0. 4. Leverage (LEV) is measured by ratio of total debt firms i at t end year to total assets of firm i at end year t . 5. Managerial ownership (DMOWN) is expressed as a dummy variable, 1 means some shares are owned by manager and otherwise is 0 (Ahmed, 2009; Mahadwartha, 2002). 6. Expropriation of assets by ultimate shareholders. Expropriation of controller shareholder is defined as rights transfer of minority shareholders to ultimate shareholder (Cheng, 1958). Ultimate shareholder expropriation is proxied by tunneling and propping the assets. Tunneling (EKSTUN) is defined as resources transfer from firm to shareholders through transactions with ultimate parties (Johnson, LaPorta, Lopez-de-Silanes, & Shleifer, 2000). Tunneling is measured by ratio between the number of related party transaction in form of firm's assets outflow at

3 end of fiscal year t toward total book value of firm i assets at end of fiscal year t

(Cheung, Jing, Lu, Rau, and Stouraitis, 2009; Faccio, Lang, & Young, 2001; Jiang, Lee, & Yue, 2010; Johnson et al., 2000). Propping (EKSPROP) can be interpreted as negative tunnelling. Propping is defined as bail out by ultimate shareholders to firm (Friedman, Johnson, & Mitton, 2003). Propping is measured by ratio between the number of related party transaction in form of inflows of assets received by

3 firm i at end of fiscal year t toward total book value of assets of firm i at end of fiscal year t

(Bae, Cheon, & Kang,

202008; Cheung et al., 2009; Friedman et al., 2003; Peng, Wei, & Yang, 2011).

7. Managerial Expropriation (EKSMAN). Managerial expropriation is

13 defined as the acquisition of firm assets by managers to maximize the

interests (Cheng, 1958). Managerial expropriation is measured by ratio of compensation amount received by corporate managers

3 of firm i at end of fiscal year t to book value of total assets of firm i at end of fiscal year t

(Cronqvist, Heyman, Nilsson, Svaleryd, and Vlachos, 2009). Types and Data Collection Methods: Secondary data used is unstructured panel data. Data sources are firm's annual reports has been audited that obtained from www.idx.co.id. While, ultimate ownership information and other supporting data sources are obtained from the OSIRIS database and firm websites. Data Analysis Methods: Classical Assumption Test: Hypothesis test is done by structural equation modeling based path analysis. There are 6 structural equation as follows: $LnFV = \beta_0 - \beta_1 LnDCFRRCR - \beta_2 DMOWN - \beta_3 LnEKSTUN + \beta_4 LnEKSPROP - \beta_5 LnEKSMAN + \beta_6 DMUO + \beta_7 LnTA + \beta_8 DAUD + \beta_9 LnLEV + \epsilon it$ (1) $LnFV = \beta_0 - \beta_1 LnDCFRRCR - \beta_2 DMOWN - \beta_3 LnEKSTUN + \beta_4 LnEKSPROP - \beta_5 LnEKSMAN + \beta_6 DMUO + \beta_7 LnTA + \beta_8 DAUD + \beta_9 LnLEV + \beta_{10} LnDIVMV + \epsilon it$ (2) $DIVMV = \alpha_0 - \alpha_1 DCFRRCR - \alpha_2 DMOWN - \alpha_3 EKSTUN - \alpha_4 EKSPROP - \alpha_5 EKSMAN + \alpha_6 DMUO + \alpha_7 LnTA + \alpha_8 DAUD + \alpha_9 LEV + \epsilon it$ (3) $DIVMV = \alpha_0 - \alpha_1 DCFRRCR - \alpha_2 DMOWN - \alpha_3 EKSTUN - \alpha_4 EKSPROP - \alpha_5 EKSMAN + \alpha_6 DMUO + \alpha_7 LnTA + \alpha_8 DAUD + \alpha_9 LEV + \alpha_{10} FCF - \alpha_{11} DCFRRCR*FCF - \alpha_{12} DMOWN*FCF - \alpha_{13} EKSTUN*FCF - \alpha_{14} EKSPROP*FCF - \alpha_{15} EKSMAN*FCF + \epsilon it$ (4) $LnFV = \delta_0 - \delta_1 LnDCFRRCR - \delta_2 DMOWN - \delta_3 LnEKSTUN - \delta_4 LnEKSPROP - \delta_5 LnEKSMAN + \delta_6 DMUO + \delta_7 LnTA + \delta_8 DAUD + \delta_9 LnLEV + \delta_{10} FCF - \delta_{11} LnDCFRRCR*FCF - \delta_{12} DMOWN*FCF - \delta_{13} LnEKSTUN*FCF - \delta_{14} LnEKSPROP*FCF - \delta_{15} LnEKSMAN*FCF + \epsilon it$ (5) $LnFV = \delta_0 - \delta_1 LnDCFRRCR - \delta_2 DMOWN - \delta_3 LnEKSTUN - \delta_4 LnEKSPROP - \delta_5 LnEKSMAN + \delta_6 DMUO + \delta_7 LnTA + \delta_8 DAUD + \delta_9 LnLEV + \delta_{10} FCF - \delta_{11} LnDCFRRCR*FCF - \delta_{12} DMOWN*FCF - \delta_{13} LnEKSTUN*FCF - \delta_{14} LnEKSPROP*FCF - \delta_{15} LnEKSMAN*FCF + \epsilon it$ (6) Structural equation modeling must meet some basic assumptions to produce a best estimate (Best Linear Unbiased Estimator-BLUE). Classical assumption test results to regression equation are as follows: Table 2: Test Results One-Sample Kolmogorov-Smirnov Z Model Kolmogorov- Smirnov Z Asymp. Sig (2 tailed test) Normality Equation (1) 0.542 0.930 Normal Equation (2) 0.484 0.973 Normal Equation (3) 0.965 0.309 Normal Table 3: Multicollinearity Testing Results Regression Models Correlation Value (in absolute value) Tolerance Variance Factor (VIF) Inflation

Multicollinearity Equation (1) 0.036 – 0.683 0.465 – 0.823 1.216 – 2.150 No multicollinearity Equation (2) 0.028 – 0.683 0.465 – 0.851 1.175 – 2.152 No multicollinearity Equation (3) 0.031 – 0.683 0.465 – 0.823 1.216 – 2.150 No multicollinearity Table 4: Autocorrelation Testing R results Regression Models Z value (Run Test) Asymp Sig Autocorrelation Equation (1) -6.891 0.000 Yes Equation (2) -6.676 0.000 Yes Equation (3) -4.307 0.000 Yes Table 2, Table 3 and Table 4 show that regression equation (1), (2) and (3) have a normal distributed residuals, there is no heteroscedasticity, and multicollinearity. However, all three models have autocorrelation. Autocorrelation is nature of time series so the analysis is continued. RESULTS AND DISCUSSION Descriptive statistics: Descriptive statistics describe the minimum value, maximum value, average and standard deviation of variables. Table 5 and 6 summarize the statistical description of total sample 346 firms.

9 Table 5: Descriptive statistics of Variables Variables Minimum Maximum Average Deviation

Standard DCFRCR 0.2349 1 0,856 0,219 EKSTUN 0.0102 596,860 21,428 46,751 EKSPROP 0.0095 215,964 14,616 31,658 EKSMAN 0.0228 4,6374 0,6851 0,631 LEV 9.4303 93,9103 48,9103 23,038 TA (Rp million) 782,000.00 442,994,197.00 15,271,318.00 46,628,424.00 DIVMV 0.2583 72.5000 6.1890 9.349 FV 0.0336 14.8220 1.3799 2.129 FCF 0.0004 0.7329 0.1789 0.141 Source: Data Processed DCFRCR: ultimate shareholder's domination power ownership; EKSTUN: tunneling; EKSPROP: propping, EKSMAN: managerial expropriation; LnTA: natural log total assets; LEV: leverage; DIVMV: dividend yield; FV: firm value; FCF: Free Cash Flow Table 6: Descriptive statistics of dummy variables Variables Frequency Percent Modus 0 1 0 1 DMOWN 164 182 47.4 52.6 1 DMUO 233 113 67.3 32.7 0 DAUD 144 202 41.6 58.4 1 Source: Processed data Table 7: Regression Analysis Result

17 Equation (1') Equation (2') Equation (3') Equation (4') Equation (5') Equation (6') Independent Variables

FVLn FVLn DIVLn DIVLn FVLn FVLn Constant -2.559 (-1.973)* -2.394 (-1.873)* 0.914 (0.691) 0.353 (0.268) -3.112 (-2.439)* -3.036 (-2.436)* DCFRCRLn 0,292 (1.754)* 0.229 (1.390)** 0.348 (2.049)* 0.887 (3.094)* -0.102 (-0.366) -0.292 (-1.059) DMOWN -0.4 (-2.652)* -0.363 (-2.439)* 0.205 (1.330)** 0.239 (1.120) -0.644 (-3.106)* -0.593 (-2.921)* EKSTUNLn -0.039 (-1,380)** -0.032 (-1.138) 0.040 (1.398)** 0.124 (2.863)* -0.021 (-0.493) 0.006 (0.141) EKSPROPLn 0.066 (2.265)* 0.075 (2.621)* 0.053 (1.779)* 0.116 (2.644)* -0.018 (-0.417) 0.007 (0.170) EKSMANLn 0.210 (3.110)* 0.269 (3.921)* -0.324 (-4.710)* -0.234 (-2.301)* 0.268 (2.717)* 0.318 (3.276)* DMUO 0.456 (2.799)* 0.438 (2.711)* -0.116 (-0.694) -0.152 (-0.912) 0.556 (3.427)* 0.523 (3.298)* LnTA 0.222 (4.667)* 0.217 (4.629)* -0.028 (-0.584) -0.043 (-0.887) 0.214 (4.603)* 0.205 (4.506)* DAUD 0.227 (1.718)* 0.263 (2.017)* 0.2 (1.485)** 0.203 (1.481)** 0.167 (1.254) 0.21 (1.614)** LevLn -1.090 (-10.089)* -1.042 (-9.721)* 0.263 (2.387)* 0.382 (3.349)* -0.930 (-8.395)* -0.848 (-7.708)* DIVMVLn -0.180 (-3.426)* -0.215 (-4.110)* FCF 2.963 (4.118)* 0.860 (1.231) 1.495 (2.138)* DCFRCRLn*FCF 2.902 (2.315)* 2.291 (1.914)* 1.669 (1.539)** DMOWN*FCF -0.321 (-0.402) 1.192 (1.539)** 1.123 (1.484)** EKSTUNLn*FCF -0.369 (-1.993)* -0.016 (-0.087) -0.095 (-0.537) EKSPROPLn*FCF -0.462 (-2.138)* 0.490 (2.333)* 0.390 (1.891)* EKSMANLn*FCF Adjusted R2 -0.478 (-1.054) -0.413 (-0.939) -0.311 (-0.722) 0.328 0.349 0.126 0.170 0.374 0.403 F value 19.708* 19.478* 6.539* 5.700* 14.758* 15.558* Description *

7 Significant at 5% level; ** Significant at 10% level; FVLn: Ln of

firm value; DCFRCRLn: Ln of ultimate shareholder's domination power ownership; DMOWN: managerial ownership dummy variables; EKSTUNLn: Ln of Takeover (tunneling); EKSPROPLn: Ln of propping, EKSMANLn: LNL managerial expropriation; DMUO: dummy variables for type of agency conflicts in associated with managerial ownership; LnTA: natural log firms scale; DAVID: dummy variable of audit quality; LevLn: Ln of leverage; DIVMVLn: Ln of dividend yield; FCF: free cash flow; DCFRCRLn*FCF: interaction of DCFRCRLn and FCF; DMOWN*FCF: interaction of DMOWN and FCF; EKSTUNLn*FCF: interaction of EKSTUNLn and FCF; EKSPROPLn*FCF: interaction of EKSPROPLn and FCF; and EKSMANLn*FCF: interaction of EKSMANLn and FCF Goodness of Fit Model Test: Determination coefficient (R2): Table 7, Table 8 and regression equation (1') to (6') have adjusted R2 values are 0.126 to 0.403. Hair, Black, Babin and Anderson (2010) suggest that for number of independent variables at a significance level (α) acceptance of hypothesis 0.05, adjusted R2value in this study considered shows

13 that independent variables have a pretty good ability to explain variation of dependent

variable. Anova: Table 7 and Table 8. explains ANOVA test results of each regression model. The value of F statistic of regression equation (1') to (7') have are 5.7 to 19.708, significant at a probability value $\alpha = 0.05$; it means that at least there is one independent variable affects on dependent variable. Hypothesis Testing: Hypothesis 1a states that " Ultimate shareholder's domination power negatively affect on firm value". Research result show the magnitude of regression coefficients for DCFRCRLn variable in regression equation (1'), β_1 , 0.292 and t value is 1,754 t value. Statistical tests mean that hypothesis 1a is accepted at 0.05 significance level. This results support the agency theory- entrenchment hypothesis which states that for pyramidal ownership structure, greater dispersion

10 **of control rights** above **cash flow rights by ultimate shareholders**

will increase dominance power of ultimate shareholders to take action which have the entrenchment effect, which will makes firms value tend to decrease (Claessens et al., 2000). Pyramidal ownership structures would make ultimate

10 **shareholders have** greater **control right than cash flow rights. The**

greater control right than cash flow rights allows ultimate shareholders to get domination power to firm's assets. Ultimate shareholder's domination power provides an incentive for the ultimate shareholders to act which has entrenchment effect and maximize their utility. The greater ultimate shareholder's domination power, there is a tendency that firm value will be lower.

21 **This finding is consistent with results of** Thomsena **et al.** (2006), Ahmad **et al.**

(2009), and Barry-Ariffin et al. (2010), (Barry-Ariffin 2010), Bae et al. (2012). Hypothesis 1b stated that "Dividend mediates the effect of ultimate shareholder's domination power to firm value". Comparing the DCFRCLn coefficients in regression equation (1') and (2') (see Table 7), it was concluded that dividend (DIVMVLn) serves as a partial mediation variables. The indirect effect magnitude of ultimate shareholder's domination power ownership on firm value through dividends as a mediation variable is equal to -0.06264 (0348×-0.18) and total effect of 0.22936 ($0292 + (-0.06264)$) (see Table 7 and Table 8). The results could support the Agency Theory-

4 **Free Cash Flow Hypothesis).** Theory **Agency- Free Cash Flow Hypothesis** that **in case of agency**

conflict, dividend distribution has a function as a substitution of good corporate governance mechanism (GCG) (Jensen, 1986). As substitution of good corporate governance mechanisms, dividend will reduce agency costs that arise as a result of agency conflicts that occur from desire of ultimate shareholders to keep control to firm's resource. Higher ultimate shareholder's domination power, dividend distribution will reduce the ability of ultimate shareholders to take action having entrenchment effect. Firms who pay dividend will have greater firm value. Hypothesis 1c states "Dividend mediates the effect of interaction between ultimate shareholder's domination power and free cash flow on firm's value". Decision to accept hypothesis 1c is based on significant effect of ultimate shareholder's domination power ownership and free cash flow (DCFRCLn*FCF) to firm value (FVLn) in equation (6'); as well as the significant effect of interaction between ultimate shareholder's domination power ownership and free cash flow (DCFRCLn*FCF) on firm value (FVLn); and significant effect of dividends (DIVMVLn) to firm value (FVLn) in equation (7'). Regression analysis of equation (6') (see Table 7) shows the regression coefficients for DCFRCLn*FCF for 2291 with t value of 1,913 is significant at $\alpha = 0.05$ level. Interaction of ultimate shareholder's domination power ownership and free cash flow (DCFRCLn*FCF) directly affect on firm value (FVLn) at 0.05 significance level. Regression analysis of regression equation (7') (see Table 7) shows that dividend has function as full mediator. Mediation effect of dividend for effect of interaction between ultimate shareholder's domination power ownership and free cash flow (DCFRCLn*FCF) on firm value (FVLn) is -0.62393 (2902×-0.215) (see Table 7 and Table 8). Total effect is 1.66707 ($2291 + (-0.62393)$). It can be concluded that the interaction between ultimate shareholder's domination power and free cash flow affect indirectly firm value through dividend. This results show that free cash flow strengthen indirect effect of ultimate shareholder's domination power ownership on firm value through dividend. It means dividends have function as a substitute of good corporate governance (GCG) mechanism in agency conflict on of

16 **free cash flow.** Greater **free cash flow** will increase desire **of**

ultimate shareholders to retain free cash flow and use it to maximize the utility. On condition of ultimate shareholders have greater control to free cash flow, dividend distribution can align the interests of ultimate shareholder who have domination power and minority shareholder (Easterbrook, 1984; Rozeff, 1982) so that there is a tendency of the higher firm value. On condition firm has free cash flow, dividend distribution will be able to control the actions of ultimate shareholders to avoid policy that could lead to

5 **conflict between the** ultimate **shareholders and minority shareholders,** including **the**

actions to invest excess cash on non- value added projects (Jensen, 1986). Conclusions, Limitations And Suggestions: The firm value is likely to decrease if the ultimate shareholder's domination power is likely higher. Pyramidal ownership structure tends to increase dispersion

11 **between control right** than **cash flow right.** Greater dispersion of **control**

rights over cash flows right gives greater possibility for ultimate shareholders to adopt policies and measures with entrenchment effect. Dividends as substitution of good corporate governance mechanisms will reduce the entrenchment effect from the action taken by ultimate shareholder, in order to the firm value tend higher. Likewise, in condition of greater free cash flow, firm value would be higher if firm distributes dividends to shareholders. Distribution of dividends will reduce the incentives of ultimate shareholder to invest the free cash flow on the non-value added projects. Future studies may use the other of corporate governance mechanism as a mediator variable to replace the dividend. Furthermore, to enhance the explanatory power of free cash flow as moderating variables, it needs to control the sample by splitting the sample based on profitability, investment opportunity set (Chen and Chuang, 2009; Dittmar, Mahrt-Smith, & Servaes, 2003) and firm's life cycle (Harry DeAngelo, DeAngelo, and Stulz, 2006).

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