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The Role of Good Corporate Governance Banking Sector in Supporting Risk Management Principles as the Implementation of Prudential

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Abstract

Implementation of good corporate governance in the banking industry should always be based on five basic principles. First, transparency, namely openness in expressing material information and relevant as well as transparency in the decision making process. Second, accountability, the clarity of the functions and the implementation of the accountability organ bank that effective management. Third, accountability that the suitability of the bank management with the legislation in force and the principles of management of healthy banks. Fourth, independence that bank management in a professional manner with no influence / pressure from any party. Fifth, fairness, namely justice and equality in meeting stakeholder rights arising under the agreement and the legislation in force. In order to establish the five basic principles mentioned above, the bank shall be guided by the various regulations and minimum requirements and guidelines related to the implementation of good corporate governance).

Key Words: *Good corporate governance, risk management, precautionary principle*

Introduction

Banking industry very rapidly generally accompanied with the increasing complexity of business activities of the bank, resulting in increased risk exposure of banks. Good corporate governance in the banking industry is becoming more important for today and the days to come, given the risks and challenges faced by the banking industry will increase.

In order to improve the performance of the bank, protect the interests of stakeholders and improve compliance with laws and regulations as well as the code of conduct which applies in general to the banking industry, banks are required to conduct its operations based on the principles of good corporate governance.

Implementation of good corporate governance in the banking industry should always be based on five basic principles. First, transparency, namely openness in expressing material and relevant information and transparency in the decision making process. Second, accountability, the clarity of the functions and the implementation of the accountability organ bank that effective management. Third, responsibility, that bank management conformity with the legislation in force and the principles of sound bank management. Fourth, independency, is the professional management of the bank without the influence / pressure from any party. Fifth, fairness. Fairness and equity in meeting stakeholder rights arising under the agreement and the legislation in force. In order to establish the five basic principles mentioned above, the bank shall be guided by the various regulations and minimum requirements and guidelines related to the implementation of good corporate governance.

In efforts to repair and improve the quality of implementation of good corporate governance, banks are required to periodically perform a self-assessment of the adequacy of implementation of good corporate governance and prepare reports its implementation, so that if there are deficiencies, it can be done immediately corrective action necessary.

The need to apply the principles of good corporate governance also felt very strong in the banking industry. External and internal situation of increasingly complex banking. Risk increasingly diverse banking activities. These circumstances increase the need for good corporate governance practices are healthy in banking. The application of the principles of good corporate governance in addition to enhancing the competitiveness of the bank itself, as well as to better provide protection to the public. Implementation of good corporate governance becomes a necessity in view of the banking sector to manage public funds (customers).

Several regulations have been issued relating to the application of the principles of good corporate governance, among others, Central Bank of Indonesia Regulation No. 2/27 / PBI / 2000 dated December 15, 2000 concerning Commercial Bank, which in it set the criteria that must be met candidates for the Board and the Commissioner of Commercial Bank, as well as transaction limits permitted or prohibited by the board of the bank.

The main purpose of this rule is as a manifestation of corporate governance by eliminating the possibility of the bank's operations irregularities committed by directors and / or directors, or shareholders. The regulation has a strong correction, given the organ company that gets most attention for improved and enhanced performance is the Board of Directors and Commissioners. Moreover, in reality, the role of directors and commissioners are prone to be misused in the absence of checks and balances between all organs of the company.

Strengthening the Board of Directors and Commissioners is also supported by Central Bank of Indonesia Regulation No. 5/25 / PBI / 2003 on fit and proper test, in which candidates for directors and commissioners bank must meet certain competency to take charge of the bank. The existence of detailed requirements for candidates for directors and commissioners can make the election of an independent bank management and have the ability in the field. Thus, this rule may prevent the abuse of authority shareholders (majority) to appoint directors and commissioners are not independent.

In addition to regulating the directors and commissioners, this rule also regulates the competencies that must be met by the controlling shareholder. Not everyone can become the controlling shareholder. Under these regulations, only those who have the integrity and financial viability that can become the controlling shareholder. This regulation is intended to encourage the creation of a sound banking system, through the application of the principles of good corporate governance in the banking industry. To realize the implementation of the principles of good corporate governance, the banking industry needs to be managed and owned by the parties always have the competence and integrity as well as meet other requirements in accordance with the legislation in force.

Other regulations were issued related to the increasing need of good corporate governance is a Central Bank of Indonesia Regulation No. 5/8 / PBI / 2003 concerning Application of Risk Management for Commercial Banks, which is further followed by publication SE No. 5/21 / DPNP dated September 29, 2003. The regulation requires banks to establish authority and responsibility are clearly on each hierarchy associated with the implementation of risk management. Similarly arranged therein regarding the powers and responsibilities of directors and commissioners to be done related to the implementation of the risk management.

Application of risk management is expected to increase shareholder value, as well as provide an overview to the bank manager about a possible bank losses in the future, improve the methods and systematic decision-making process based on availability of information, are used as the basis for a more accurate measurement of the performance of the bank.

In addition, risk management can be used to assess the risk inherent in instruments or banking operations are relatively complex and creating a solid risk management infrastructure in order to improve the competitiveness of the bank. Thus, the application of risk management is closely related to the principle of accountability and responsibility. The application of risk management will also encourage better compliance with the principles of good corporate governance in a bank, especially in order to improve the performance and competitiveness of the bank itself.

According to the general description of Central Bank of Indonesia Regulation No. 5/8 / PBI / 2003 concerning Application of Risk Management for Commercial Bank stated that the principles of risk management will be adopted and applied in the Indonesian banking directed in line with the recommendations issued by the Bank for International Settlements through the Basle Committee on Banking Supervision. These principles is basically a standard for the banking sector to be able to operate more careful in the scope of development of business activities and banking operations were very fast today.

Application of risk management can vary from one bank to another bank in accordance with the objectives, business policy, size and complexity of operations and the ability of the Bank in terms of finance, support infrastructure and human resources. Central Bank of Indonesia sets this provision as a minimum standard that must be met by the Indonesian banking in implementing risk management.

Article 2 of Central Bank of Indonesia Regulation No. 5/8 / PBI / 2003 concerning Application of Risk Management for Commercial Bank determines that the bank is obliged to apply effective risk management and the application of at least include:

1. The active supervision of the Board of Commissioners and Board of Directors;
2. The adequacy of policies, procedures and limits;

3. The adequacy of the process of identification, measurement, monitoring and control of risk and risk management information system; and
4. Thorough internal control system.

Furthermore, based on the explanation of Article 8 of Central Bank of Indonesia Regulation No. 5/8 / PBI / 2003 concerning Application of Risk Management for Commercial Bank stated that the determination of risk management policies, among others by means of a strategy which ensures that:

1. The Bank retained risk exposures in accordance with the bank's internal policies and procedures and regulations and other applicable provisions;
2. The Bank is managed by human resources who have the knowledge, experience and expertise in risk management, according to the complexity of banking business.

Determination of risk management strategies also consider the financial condition of the bank, the bank organization and the risks that arise as a result of changes in external factors and internal factors.

Based on the above, the proposed formulation of the problem as follows:

1. What is the role of good corporate governance in the banking sector to support risk management as the implementation of the precautionary principle?
2. The constraints are faced by banks in implementing good corporate governance as an effort to support risk management in the implementation of the precautionary principle?
3. Efforts law whether that should be taken by the bank in overcoming the obstacles that occur in the application of good corporate governance as an effort to support risk management in the implementation of the precautionary principle?

Based on what has been presented on the background of the research above, it is the goal of this research is:

1. To identify and assess the role of good corporate governance in the banking sector to support risk management as the implementation of the precautionary principle
2. To identify and assess constraints faced by banks in implementing good corporate governance as an effort to support risk management in the implementation of the precautionary principle
3. To identify and assess the legal measures that should be taken by the bank in overcoming the obstacles that occur in the application of good corporate governance as an effort to support risk management in the implementation of the precautionary principle

Research Methods

The study, to be carried on a normative legal research, ie research that promotes library research to obtain secondary data as main data. The data in this library research is secondary data which is legal materials consisting of:

a. Primary law materials, namely legal binding material consisting of:
   1) Act of 1945
   2) Code Civil (Civil Code)
   3) Act No. 10 of 1998 concerning Amendment to Law Number 7 of 1992 concerning Banking
   4) Act No. 3 of 2004 on the Amendment of Act No. 23 of 1999 concerning Bank Indonesia
   5) Bank Indonesia Regulation No. 5/8 / PBI / 2003 dated May 19, 2003 concerning Application of Risk Management for Commercial Banks
   6) Bank Indonesia Regulation No. 8/4 / PBI / 2006 dated January 30, 2006 on the Implementation of Good Corporate Governance for Banks
   7) Bank Indonesia Regulation No. 8/14 / PBI / 2006 dated October 5, 2006 on the Amendment of Bank Indonesia Regulation Number 8/4 / PBI / 2006 on the Implementation of Good Corporate Governance for Banks
   8) other legislation related to this research.

b) Secondary law materials, ie materials that provide legal guidance and explanation of the primary legal materials, which consist of literature books, papers, articles, research, and other scientific papers related to the study.

c) Tertiary Laws materials, ie materials that provide legal guidance and explanation of the primary legal materials and secondary legal materials consisting of:
   1) General Indonesian Dictionary
   2) Law Dictionary
   3) Dictionary English - Indonesia
   4) Encyclopedia

The data have been collected both from the research literature and field research qualitatively analyzed with descriptive methods.

1. Descriptive; the method of analysis by describing the real situation on the ground.
2. Qualitative, the method of data analysis by classifying and selecting the data obtained from the study according to the quality and truth, then connected with the theories of the study of literature in order to obtain answers to problems in this study. In the analysis of this data is used inductive way of thinking, that concludes the study of things that are special to then conclude a general nature

Results and Discussion

1. **Role of Good Corporate Governance (GCG) Banking Sector to Support Implementation of Risk Management As Precautionary Principle**

The risk-based banking supervision has become the new silver bullet for the regulatory role as a shield and rules agreed on between the banks themselves. However, it will lose tuahnya moment when the bank and the business itself does not take strategy to apply corporate governance in their respective operations.

This is where the answer to the question why the supervisory review should be applied by the bank's management in a whole series of risk management process. As well as to answer how the distribution of responsibility is applied and implemented in banking management and the business world. That answer also the question of why should be required for disclosure or disclosure and public statements by the management or related to the implementation of risk management in banking.

Such is certainly the need for supervisory review applied to the management of the bank. It was not merely an effort to ensure that the bank always meet the minimum requirements of capital. The review also needs to encourage banks to develop and use the best management techniques in controlling the risks it faces.

However, it is also important to realize that the application of supervisory review still does not guarantee the certainty of the formation of a reliable management. Directors and senior ranks of the bank's management is responsible for ensuring maintenance of sufficient capital to support the bank's operations in accordance risks associated behind it.

Quality of internal capital assessment process which the bank is a central aspect of the assessment supervisory authorities. Any deficiencies that occur over bank capital which can be determined through calculation of the target capital ratio, should be the primary focus for the bank's risk management. From the results of its monitoring, supervisors can ask the bank's shareholders to add fresh capital. Beyond that there are available alternatives to address the problem of the capital deficiencies. One is through efforts to improve asset quality or banks trying to avoid risks that can suppress the amount of the nominal capital of the bank.

In September 1997 the Basel Committee has published a publication that contains "25 core principles for effective banking supervision" which covers seven areas, namely: institutional aspects, licensing, provision of prudence, methods of surveillance, information, issues of authority and the supervision of cross-country or limit (cross border). In the meantime, the Second Pillar of Basel Accord has also identified four main principles in the supervisory review. The fourth main principles include:

a. Bank must have and develop their own process of doing an assessment on its capital adequacy as a whole. For the bank at any time shall identify the risk profile at hand. Banks are also obliged to be ready to run a strategy that fits in maintaining the level of capital adequacy.
b. The supervisor must review and evaluate internal capital assessments and strategy of the bank. Similarly, the supervisor should also assess the bank's ability to monitor and ensure compliance with all regulations regarding regulatory capital ratios. To that end, the supervisor if necessary can take action that is deemed suitable if the results of the review process is unsatisfactory.

c. The supervisor should encourage banks to support its operations with a capital on top of the minimum regulatory capital ratios. Similarly, the supervisor may have the authority to require the bank retains the amount of capital above the minimum requirement.
d. Supervisors should intervene required at the first opportunity to prevent it from sliding down the amount of capital banks that are under the minimum requirement. These interventions need to be done as soon as possible. Because if not done the right remedial action bank capital becomes difficult to be maintained and repaired.

Disclosure is necessary for people to digest properly all the information required in assessing the performance of a company's business done, including banks. Disclosure has become one of the important aspects to be considered by potential investors because it can contain a picture of the state of the bank's current and projected performance in the future.

Generally all the companies belonging to the private or public companies are required to periodically publish financial statements that include the income statement, balance sheet and tax accounts. Capital market institutions that perform listing on enterprises or public banks are very concerned with what is required by the shareholders. It needs generally include a very detailed picture of financial information on a company or a bank.

As is the stakeholders are include shareholders, employees, customers and society in general. Aspects of the disclosure as promulgated under Basel II only covers a part of the disclosure as required to be fulfilled by a bank. And the requirement itself is part of the legal and regulatory obligations.

"Corporate governance" of a bank is a set of relationships between the board of commisioners, board of executive directors, stakeholders, and shareholders of the bank. The structure of corporate governance in banks has a wide range of variation depending on local custom where the bank is domiciled, restrictions on legal aspects and the historical record of each bank itself.

It must be noted that no single corporate governance structure was acceptable as an ideal structure. Nevertheless, an important related issue is whether corporate governance in which there are aspects of the checks and balances or not. That aspect which should be covered in the application of corporate governance in a company or a bank.

Is a very important thing for a bank to have a set of policies that contains strategic objectives and corporate ethos clear. Equally important also when the bank can disseminate and communicate these policies at all levels of the bank's management.

A set of values (values) of companies that have agreed reasonably likely to be implemented at all levels of the bank's management, including the board of directors. Values are defined for instance is a value that encourages openness and timely submission of the report openly to the problems that developed in the management of a bank, or a determination that forbid acts of corruption or bribery practice, both of which occurred in the internal and external environment of the bank.

Directors must be able to ensure that systems and procedures stipulated in the monitoring and reporting has been running on the right track and fulfill the requirements according to which this policy. In order for monitoring and supervision of bank operations really effective, the board needs to establish lines of authority and a clear responsibility in the management of the bank.

Nevertheless, it must be noted that the board of directors or management board that setaraflah that ultimately assume responsibility regarding the health of the management and performance of the bank. As a complement can be formed several committees that provide input and views on specific issues for the board of directors. This can be either an audit committee, risk management, and renumeration.

The senior managers need to have a comprehensive oversight function. All decisions relating to issues of strategic importance, should be done by more than one manager. The internal and external auditors in fact played a key role in enforcing implementation of corporate governance framework. In that regard, the directors should be placed as an element of management to provide input and views are critical to the interests of the directors themselves.

Therefore, the inputs delivered by the auditors must be used by directors to check the correctness of the information submitted by the senior manager. It is important also when the board of directors to develop and establish a compensation policy that reflects the culture of the work, objectives, strategies and surveillance systems applicable in the bank. The formation of a sound corporate governance (sound) can be driven through the application of transparency to the honesty of the prime

2. **Obstacles Faced by Bank BPD DIY Province in Implementing Good Corporate Governance (GCG) as an Effort to Support the Implementation of Risk Management In the Precautionary Principle**

Monetary crisis of 1997 has yielded lessons for Indonesian banks. Since then it has produced significant changes. Bank Indonesia has been consolidated. Although the number of remaining half but with better capital structure, compared with the picture before the crisis. Productive asset quality has also been much nicer. This is due to the transfer of non-performing loans into IBRA (Indonesian Bank Restructuring Agency), following the onset of the crisis. Although of 131 commercial banks rated by Infobank at the end of June 2006, a state of the end of 2005, there were only 90 banks are "relatively safe". That is CAR (Capital Adequacy Ratio) it has been above 12%, and NPL (Non Performing Loan) it had been under 5%. The monetary crisis that has functioned as natural selection, too, has changed the structure of ownership and management structure of banking in Indonesia. The intervention of the private owners of the private banking management policy has also been considerably reduced. Also with an increasing share of foreign ownership, intervention similar to large banks or banks Semi SOEs has decreased. The picture can be considered as the foundation is solid enough for the application of corporate governance in the Indonesian banking.

Bank Indonesia has received wisdom that great anyway. Act No. 23 of 1999 has set its sole purpose is to maintain stability in the rupiah. The central bank has also been declared free of any influence in achieving that goal. Includes free from the influence and interference of government. Law No. 24 of 1999 dated May 17, 1999 on foreign exchange flows and the exchange rate system has also strengthened the groundwork central bank. With this legislation, Bank Indonesia has gained a foothold clear in the conduct of monetary policy.

The issue of exit policy for the banking system has also been resolved with the formation of LPS (Deposit Insurance Corporation). There are no more shackles of hostages in the form of a blanket guarantee program guarentee as occurred following the outbreak of the financial crisis in 1997.

With the progress that can be understood when the central bank to be more aggressive with the idea of launching the Indonesian Banking Architecture (API). On behalf of the idea of the API is then urged the central bank's merger efforts between banks with assets of small and medium. Along with the steps the central bank has also set a "single presense policy" and encourage an increase in the nominal capital of these banks. Step forward have triggered numerous ideas to restructure the entire financial system through the establishment of "Financial Services Authority". The institute is planned to be effectively established since 2010. As well as the task of supervision of the banking system will be switched from the central bank's Financial Services Authority. This meant that Bank Indonesia will be more focused on their core task execution.

Thus armed with the progress that the central bank has launched at least two major policy. Both policies are as follows:

a. Application of the method of calculating the level of health of commercial banks

Its bases are fixed in the form of an assessment of the CAMEL as previously applicable. However, for the calculation of the amount of capital banks are now have been based on the risk-based capital by the amount of the minimum CAR of 8%. Here has been applied to the calculation of CAR and include elements of market and operational risk in addition to credit risk.

b. Application of risk management for banks in accordance with the risk management regulation

The consequences of the application of risk management, bank regulation is required to control the risks inherent in doing business behind. Under the supervision of Bank Indonesia, each bank must implement integrated management rumor. For it is necessary to build risk management structure. Bank should also establish management structures and systems of control are effective in controlling those risks. The necessary steps to include: (a) identification of the risks; (b) measuring the effect caused by these risks; (c) implementation of effective monitoring; and (d) the implementation of appropriate control systems, efficient and effective.

Most of these types of risks facing the banking Indonesia has been specified by Centra Bank of Indonesia. These risks include: credit, market, interest rate, foreign exchange rate, liquidity, operational, legal, reputation and compliance.

Furthermore, in carrying out the risk control, need organizational management that support them. The division of tasks and responsibilities of the triad (directors, commissioners and the management). Needs to be an assessment of the risk appetite and risk profile. Also limits setting in risk control. Here the necessary formulation of risk management policies and procedures for the determination of risk limits. Similarly, the internal control system in which the role of the auditor occupies a central position as well.

Within the organizational structure of risk management, need to be formed at least risk management committee and risk managemet units. Similarly, as part of the application coroprate healthy governance disclosure and transparency need to be developed through a reporting system that is complete, accurate and up to date.

However, apart from some measures that need to ponder the presence of obstacles to the implementation of risk management in general. Barriers were particularly regarding:

a. Risk quantification as a major challenge; and

b. To "stalking" is needed for the risk models.

Have ready the banking and business world in Indonesia to overcome the second obstacle. Especially in conditions where statistical mindedness yet menjsadi awareness evenly both in banking and in business here. While transparency, disclosure and good corporate governance is still not evenly applied.

3. Efforts Taken by Law Must Overcome Obstacles In The Bank Happens In Implementation of Good Corporate Governance (GCG) as an Effort to Support the Implementation of Risk Management In the Precautionary Principle

The need to apply the principles of GCG also felt very strong in the banking industry. External and internal situation of increasingly complex banking. Risk increasingly diverse banking activities. The circumstances increase the need for good corporate governance practices are healthy in banking. The application of the principles of good corporate governance in addition to enhancing the competitiveness of the bank itself, as well as to better provide protection to the public. GCG implementation becomes a necessity in view of the banking sector to manage public funds (customers).

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Strengthening boards of directors and commissioners is also supported by Central Bank of Indonesia Regulation No. 5/25 / PBI / 2003 on Fit and Proper Test, in which candidates for directors and commissioners bank must meet certain competency to take charge of the bank. The more detail requirements for prospective directors and commissioners can make the election of an independent bank management and have the ability in the field. Thus, this rule may prevent the abuse of authority shareholders (majority) to appoint directors and commissioners are not independent.

In addition to regulating the directors and commissioners, this rule also regulates the competencies that must be met by the controlling shareholder. Not everyone can become the controlling shareholder. Under these regulations, only those who have the integrity and financial viability that can become the controlling shareholder. This regulation is intended to encourage the creation of a sound banking system, through the application of the principles of good corporate governance in the banking industry. To realize the implementation of the principles of good corporate governance, the banking industry needs to be managed and owned by the parties always have the competence and integrity as well as meet other requirements accordance with the legislation in force.

Other regulations were issued related to the need for increased corporate governance are Central Bank of Indonesia Regulation No. 5/8 / PBI / 2003 concerning Application of Risk Management for Commercial Banks, which is further followed by publication SE No. 5/21 / DPNP dated September 29, 2003. The regulation requires banks to establish authority and responsibility are clearly on each hierarchy associated with the application of risk management. Similarly arranged therein regarding the powers and responsibilities of directors and commissioners to be done related to the implementation of the risk management.

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In addition, risk management can be used to assess the risk inherent in instruments or banking operations are relatively complex as well as creating a solid risk management infrastructure in order to improve the competitiveness of the bank. Thus, the application of risk management is closely related to the principle of accountability and responsibility. The application of risk management will also encourage better compliance with the principles of good corporate governance in a bank, especially in order to improve the performance and competitiveness of the bank itself.

Conclusion

1. Principles of Good Corporate Governance (GCG) banking sector in the form of fairness, transparency, accountability and responsibility has a strategic role in supporting the implementation of the principles of risk management as prudence which must be implemented by the bank, since the implementation of risk management required for applications of the principles of accountability, responsibility, fairness and openness
2. There are some constraints faced by the Bank in implementing good corporate governance as an effort to support risk management in the implementation of the precautionary principle obtained from the GCG Self Assessment conducted by the Bank as follows:
   a. Commissioner has not established committees as desired in GCG. Because the Central Bank of Indonesia Regulation still gives leeway for banks to establish a remuneration committee and nomination no later than the end of June 2008.
   b. Supervisory Board still can not reveal about the remuneration and other facilities received as GCG provisions have not been fully implemented. Because of the remuneration and nomination committee has not been formed that has not obtained the results of the analysis / recommendations regarding the nomination committee and the remuneration policy to the General Meeting of Shareholders. In addition, the remuneration has not been published because the obligation preparation of the new GCG applied for the position in December 2007 report.
   c. Board of Directors meeting has not been fully documented. Because there has been no order that details the working mechanism and the mechanism of Directors meeting.
   d. The Board of Directors did not use a bank for personal interests but no indication of directors co-profitable foundation. Because there has been no order that details the working mechanism and the mechanism of Directors meeting.
   e. Bank has not formed an audit committee, risk monitoring committee and the remuneration and nomination committee, which refers to the provisions of GCG. Because the Central Bank of Indonesia Regulation still gives leeway for banks to establish a remuneration committee and nomination no later than the end of June 2008.
   f. The internal audit function does not include an assessment of the implementation of risk management. Due to limited human resources, Internal Control Unit to focus more on operational activities.
   g. Information systems related to risk management has not been implemented optimally and policies still need to be refined. The parameters used to measure the risk control / risk is inherently not perfect.
3. Efforts should be made by the bank in overcoming the obstacles that occur in the setting of good corporate governance as an effort to support risk management in the implementation of the precautionary principle are: to establish appropriate committees ideal GCG principles, the audit function Internal need to be implemented optimally and includes an assessment of the implementation of risk management, and the Bank should implement an optimal risk management and information systems related to risk management should also be applied optimally

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