

Analysis of Financial Distress of Companies Heading Towards Bankruptcy Viewed from the Aspect of Institutional Ownership and Audit Committees

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ARTICLE INFO

Keywords: Financial Distress,
Institutional Ownership,
Audit Committees,
Companies Bankruptcy

Received : 10 January

Revised : 15 February

Accepted: 30 March

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ABSTRACT

This research aims to analyze the direct influence of institutional ownership and audit committees on the financial distress of companies facing bankruptcy. The research approach is quantitative with causal methods. The research objects were 251 companies that had liquidity difficulties and had the potential to go bankrupt in the 2020-2025 period on the Indonesian Stock Exchange. Data analysis was conducted using EViews version 10 to perform path analysis with the t-test. The research results show (1) institutional ownership does not have a significant influence on financial distress; (2) the audit committee has a significant effect on financial distress. Companies are advised to strengthen internal governance mechanisms, especially the audit committee function

INTRODUCTION

In 2025, the global economic situation is expected to still face major challenges. According to IMF projections, global economic growth will reach 3.2% in 2025. Initially, the IMF predicted a figure of 3.3% for global economic growth in 2025. However, this prediction was cut to 3.2% due to warnings of increasing risks of war and trade protectionism (Saptati, 2024). The turbulent situation of war and geopolitical tensions was also clearly felt by the Indonesian financial market. In June 2025, the JCI opened down significantly after the US attacked Iran, where on June 2, the JCI value was still 7.065 and decreased significantly to 6.968 on June 19, 2025. The IDX confirmed that the spike in world oil prices and the weakening of the rupiah were the main effects of the escalation of the war, which caused pressure on issuers in the industrial, transportation, and energy sectors (CNBC Indonesia, 2025). This can be seen in Figure 1 below:



Figure 1. Composite Stock Price Index Movement Graph (Indonesian Stock Exchange, 2025)

Based on the Allianz Trade report (2024), the number of global bankruptcies in 2023 will increase by 7% and is expected to experience a further acceleration of 9% in 2024 before finally stabilizing. This situation has pushed many companies into a vulnerable position, especially those with weak capital structures and less than optimal risk management. Issuers experiencing suspension on the Indonesian Stock Exchange (BEI) are public companies whose securities have been temporarily suspended by IDX for various reasons. Problems that arise include financial problems (bankruptcy, unreasonable financial statement opinions), violations of reporting obligations, market activities that are not reasonable, and are not in accordance with the status or Special Notation features of the Indonesian Stock Exchange.

Companies with special notation (codes B/D/E/ED) on the IDX are issuers that receive warning signs because they experience certain conditions that have the potential to disrupt business continuity, such as negative equity, failure to pay obligations, disclaimer audit opinions, or being involved in serious legal problems. The IDX's granting of this notation status aims to provide transparency

to investors so that they know the risks inherent in the company. The existence of a special notation is an early warning signal that the company is facing significant financial pressure. In this context, companies with special notations are relevant objects to study in research on financial distress, because the conditions underlying the notation are real manifestations of financial difficulties, both in the aspects of liquidity, solvency, and profitability.

The relationship between special notation and financial distress can be explained through financial and accounting theory, which places financial distress as a stage towards bankruptcy. According to Platt & Platt (2002), financial distress occurs when a company is unable to fulfill its financial obligations on an ongoing basis, resulting in operational difficulties and declining financial performance. This is in line with the characteristics of companies with special notations, which generally record losses for years, have negative cash flows, or are even unable to comply with capital market regulations regarding financial reporting. This condition shows that the special notation is not just an administrative label, but reflects serious financial symptoms that indicate financial distress in the early to medium stages.

The effectiveness of the audit committee is highly dependent on governance practices that uphold transparency, independence, and accountability. An audit committee that functions well in the areas of board governance and internal auditing is proven to increase the reliability of financial reports and prevent financial irregularities that can worsen the company's financial condition. In the context of financial distress, this monitoring mechanism plays an important role in ensuring that financial resources are used efficiently and that liquidity risks or losses can be identified early before they develop into a crisis.

Manzaneque et al (2016) stated that Good Corporate Governance (GCG) practices through institutional ownership play an important role in influencing the possibility of financial distress. Institutional ownership by banks, pension funds, and insurance companies can serve as a powerful oversight mechanism for management because they have the resources and expertise to assess a company's financial risks. Agency theory explains that when institutional ownership increases, potential conflicts of interest between managers and shareholders can be reduced. This is caused by institutional investors who tend to focus on the long-term performance and financial stability of the company.

Institutional ownership functions as an external monitoring mechanism that strengthens managerial discipline. Based on the monitoring hypothesis and stewardship theory, institutional investors have the resources, expertise, and long-term orientation that enable them to carry out effective supervision of the company's strategic decisions. As the proportion of institutional ownership increases, the pressure on management to manage the company efficiently and avoid taking excessive risks also increases. This results in the risk of financial distress being minimized and financial performance and company value increasing. The synergy between the audit committee and institutional ownership forms a comprehensive governance system where internal and

external supervision work together to maintain financial stability and sustainable company performance.

GCG used in this research includes institutional ownership and the audit committee. These two proxies were chosen because they were considered capable of representing an effective internal monitoring mechanism in encouraging company performance, especially in companies facing indications of bankruptcy. This monitoring mechanism is in line with agency theory, which states that institutional ownership is able to reduce conflicts of interest between management and capital owners, so that companies can focus more on efforts to increase company value and financial performance (Jensen, M.C., and Meckling, 1976). Based on all these explanations, this research focuses on the direct influence of institutional ownership and audit committees on financial distress in companies that are almost bankrupt.

LITERATURE REVIEW

1. Institutional Ownership

Institutional ownership is ownership of company shares by institutions such as banks, insurance companies, pension funds, and other financial institutions. Institutional investors act as an effective monitoring mechanism because they have a big interest in maintaining company value. High institutional ownership is generally associated with tighter supervision, so that it can suppress management from opportunistic behavior (Indrayono, 2021). Institutional ownership is ownership of company shares by financial institutions such as banks, insurance companies, mutual funds, and pension funds. High institutional ownership can reduce agency conflicts and increase company value through tight supervision (E. F Brigham & Houston, 2019). Institutional ownership refers to ownership of shares by financial institutions or large organizations that have a significant interest in management oversight. From a managerial accounting perspective, these institutions often act as parties that pressure management to be more transparent, accountable, and oriented towards increasing long-term company value (Collier, 2015). Institutional ownership is share ownership by institutions such as pension funds, insurance companies, mutual funds, or investment banks.

Van Horne emphasized that high institutional ownership can be a positive signal for retail investors, because it indicates tight supervision of management (Van Horne & Wachowicz, 2002). Institutional ownership is the proportion of company shares owned by institutions such as banks, pension funds, insurance companies, or mutual funds. Institutional shareholders usually have a large influence in corporate governance because their significant ownership allows for close supervision of management so as to reduce agency conflicts (Gitman, L. J., & Zutter, 2012). Institutional ownership refers to company shares owned by financial institutions such as banks, pension funds, insurance companies, or investment managers. Institutional investors have significant influence on management because large ownership allows more effective oversight of company policies. This can reduce agency conflicts between management and shareholders (Knight & Bertoneche, 2000).

Institutional ownership is ownership of shares in a company owned by large financial institutions such as pension funds, insurance companies, banks, mutual funds, and hedge funds (Dasgupta et al., 2021). Recent research shows that the influence of institutional ownership is highly dependent on investor characteristics, for example, the differences between active and passive institutions, domestic and foreign, and long-term or short-term orientation (Liu et al., 2022). Institutional ownership is often associated with a company's financial performance. Research finds that long-term institutional investors are able to increase company profitability through active monitoring and strategic policy interventions (Kim & Kim, 2017). Short-term investors who are oriented towards quick profits sometimes pressure management to prioritize short-term profits, which can reduce investment in research, development, and innovation. Other research confirms that concentrated institutional ownership can actually increase the cost of capital and reduce innovation due to conflicts of interest (Xie & Xie, 2024).

Institutional ownership is the proportion of company shares owned by institutional investors who act as a corporate governance mechanism through monitoring management activities (Sulimany, 2024). Institutional ownership is defined as the proportion of company shares owned by institutional investors, such as banks, insurance companies, investment companies, and pension funds, which are part of the company's ownership structure (Alkurdi et al., 2021).

Based on theory and expert opinion, institutional ownership can be synthesized as one of the important mechanisms in Good Corporate Governance (GCG), which acts as a tool for external monitoring of company management. Based on agency theory, institutional ownership is believed to be able to suppress the opportunistic behavior of managers and reduce conflicts of interest between management (agent) and shareholders (principal). Institutional investors such as pension funds, banks, insurance companies, and mutual funds have large analytical capabilities, resources, and economic interests, so they tend to be more active in monitoring company policies. The high proportion of institutional ownership is a signal of stronger pressure and control on management to act efficiently and transparently.

2. Audit Committee

The audit committee is part of corporate governance, which functions to support the board of commissioners in overseeing financial reports, the internal control system, and the company's compliance with regulations. The existence of an independent and competent audit committee increases the transparency and accountability of the company, thus reducing the possibility of manipulation of financial reports or fraud (E. F. Brigham & Houston, 2019). The audit committee is one of the corporate governance tools that plays an important role in increasing the transparency and accountability of financial reports. The main function of the audit committee is to assist the board of commissioners or directors in ensuring that financial reports have been prepared according to standards, as well as supervising the internal control system. Thus, the existence of an audit committee strengthens shareholder trust in management performance (Collier, 2015).

The audit committee is supported by several theories that explain its role in corporate governance. Some of the major relevant theories include agency theory, trust theory, and signaling theory. The role of the audit committee that will be clarified is the theory of trust. The audit committee, in the context of this theory, plays a role in supporting and strengthening good management performance, as well as ensuring that the information presented is accurate and transparent. Trust Theory (Stewardship Theory) is a theory that describes situations where managers act as "stewards" or good administrators, who are motivated to achieve organizational goals, not just personal goals. This theory is in contrast to Agency Theory, which assumes that managers always act based on personal interests.

Based on theory and expert opinion, the audit committee was synthesized as a committee formed by and responsible to the Board of Commissioners, whose task is to assist the Board of Commissioners in carrying out supervisory duties and functions, especially those related to financial reports, internal control systems, and compliance with regulations. Its functions include: 1) Supervision of financial reports; 2) Supervision of the Internal Control System; 3) Internal and External Audit Supervision; 4) Compliance with regulations; 5) Quality of financial reports; 6) Risk management; 7) Independence of the Audit Committee.

3. Financial Distress

Financial distress is a condition in which a company faces serious financial difficulties, characterized by decreased profits, negative cash flow, and an increased possibility of default. This situation can lead to bankruptcy if not handled immediately. Financial distress also increases the cost of capital, worsens the company's reputation, and affects investor confidence. Therefore, good risk management is needed to minimize the possibility of financial distress (Brigham & Houston, 2019). Companies experiencing distress usually have high levels of leverage, negative cash flow, and low profitability. According to Manzanque et al. (2016), financial distress is a serious and continuous decline in a company's financial performance, which does not always end in formal bankruptcy, but reflects the company's inability to maintain the continuity of its business (going concern). (Salloum et al., 2014) explain that financial distress is a condition of a company's financial problems, which is reflected in a decrease in profitability and financial performance.

Based on the theory above, researchers synthesize that financial distress is a condition of financial difficulty experienced by a company, where the company experiences a significant decline in financial performance and has the potential to lead to bankruptcy. This condition is characterized by the company's inability to fulfill its financial obligations, both short and long-term. Causes of financial distress: 1) Business planning. 2) Cash flow problems. 3) Capital structure; 4) Operational losses. 5) External factors. Based on all these explanations, the following hypotheses can be formulated in this research:

H₁: Is there a negative and significant influence of institutional ownership on the financial distress of almost bankrupt companies

H₂: Is there a negative and significant influence of the audit committee on the financial distress of almost bankrupt companies

METHODOLOGY

The research uses a quantitative approach with causal methods to determine the influence of institutional ownership and audit committees on financial distress. Measurements of institutional ownership, audit committee, and financial distress can be seen in Table 1 below:

Table 1. Measurement of research variables

Variable	Indicator	Measurement
Institutional Ownership	<ul style="list-style-type: none"> • Number of institutional shares • Total shares outstanding 	$KI = \frac{\text{Total Institutional Shares}}{\text{Total Shares Outstanding}}$
Audit Committee	Number of audit committees	$KA = \sum \text{Member of the Audit Committee}$
Financial Distress	Model Altman Z-Score	$Z = 1.2 \times X1 + 1.4 \times X2 + 3.3 \times X3 + 0.6 \times X4 + 0.99 \times X5$

The sample selection criteria for this research involved 251 companies that had indications of liquidity difficulties and the potential for bankruptcy in the 2020–2025 period based on special issuers published by the IDX. The period within the last 6 years was chosen because the current pattern/state of financial distress is different compared to the period before the last 6 years, and research with the latest range can capture changes in distress characteristics that are relevant to current market and industry conditions. Data analysis used EViews (Econometric Views) version 10 software to calculate path analysis with the t-test.

RESEARCH RESULTS

The t-test is used to determine the effect of each independent variable on the dependent variable. Decisions are determined based on probability values. If the probability < 0.05 , then the independent variable has a partially significant effect. If the probability is > 0.05 , then the independent variable is not partially significant. Complete results of the t-test can be seen in Table 2 below:

Table 2. t-test results

Relationship	Coefficient	Prob	t-statistik	Conclusion
Institutional Ownership → Financial Distress	0.033487	0.9442	0.070170	H1 Rejected
Audit Committee → Financial Distress	1.551887	0.0007	3.486368	H2 Accepted

Based on the t-test results in Table 2, the institutional ownership variable on financial distress has a probability value. $0.9442 > 0.05$ with a t-statistic value of $0.070170 < 1.645$ and a coefficient value of 0.033487 . Thus, hypothesis 1 (H1) is rejected. It can be concluded that institutional ownership does not affect financial distress in companies that fall under the criteria for Special Notation Issuers with the notation B/D/E/ED, which publish their financial reports on the Indonesia Stock Exchange (BEI) during the 2020-2025 second quarter period.

The results of testing hypothesis 2 (H2) are based on the t-test results in Table 2. The audit committee variable on financial distress has a probability value of $0.0007 < 0.05$ with a t-statistic value of $3.486368 < 1.645$ and a coefficient value of 1.551887 , which means H2 is accepted. It can be concluded that the audit committee has an influence on financial distress in companies that fall under the criteria for Special Notation Issuers with the notation B/D/E/ED, which publish their financial reports on the Indonesia Stock Exchange (BEI) during the 2020-2025 second quarter period.

DISCUSSION

1. The Influence of Institutional Ownership on Financial Distress (H1).

The results of testing the first hypothesis show that institutional ownership does not affect financial distress in companies that fall under the criteria for Special Notation Issuers with the notation B/D/E/ED, which publish their financial reports on the IDX during the 2020-2025 second quarter period. This finding can be explained by the results of descriptive statistics, which show that the average institutional ownership is only 0.546096 or 54.61% . Although nominally this figure shows that more than half of the company's shares are owned by institutional investors, this proportion does not yet reflect strong dominance in the ownership structure. Institutional ownership at this level is not effective enough to carry out management monitoring and control functions optimally, especially in companies that are under operational and financial pressure. In the case of Special Notation Issuers, control of strategic decision-making tends to remain with management, while institutional investors are

passive or short-term oriented, so they are not actively involved in efforts to prevent financial distress.

These findings strengthen the view that company sustainability is not only determined by ownership structure, but is also influenced by other factors such as the quality of employee performance, the effectiveness of financial management, efficient use of resources, and the dynamics of industrial conditions. This is in line with research (Munawar et al., 2018), (Feanie & Dillak, 2021), and (Juhaeriah et al., 2021), which found that institutional ownership does not have a significant influence on financial distress. They emphasized that the presence of institutional investors is not always able to improve management's monitoring function, especially when the company's strategy faces more complex operational and financial risks.

Apart from that, the findings of this research are in line with the results of research (Cinantya & Merkusiwati, 2015), which states that institutional ownership also does not affect financial distress. Overall, the results of this study confirm that the level of institutional ownership in Special Notation Issuers cannot be used as a main indicator in predicting the risk of financial distress. Therefore, companies need to prioritize strengthening governance, improving the quality of management, and implementing more comprehensive risk management to minimize the potential for financial difficulties.

2. The Influence of the Audit Committee on Financial Distress (H2)

The results of testing the second hypothesis show that the audit committee has a positive effect on financial distress in companies that fall under the criteria for Special Notation Issuers with the notation B/D/E/ED, which publish their financial reports on the IDX during the 2020–2025 second quarter period. This means that the better the audit committee, the healthier the company, and the lower the occurrence of financial distress.

These findings indicate that the more effective the audit committee's role is in carrying out its supervisory function, the lower the level of financial difficulties experienced by the company. Theoretically, these results are in line with agency theory, which emphasizes the importance of monitoring mechanisms to reduce conflicts of interest and information asymmetry between management and shareholders. An active and independent audit committee is able to improve the quality of financial reporting, strengthen the internal control system, and detect potential financial risks early before they develop into more serious financial distress conditions.

The results of descriptive statistics show that the average audit committee score for most of the sample companies has met the minimum requirements for the number of audit committee members according to OJK regulations. Thus, the results of this research confirm that the audit committee plays a role as a strategic governance mechanism in suppressing potential financial difficulties, especially in companies with special notations that have a high level of financial vulnerability. This finding also strengthens previous literature, which states that the effectiveness of internal supervision through the audit committee is able to

increase financial stability and prevent companies from entering a deeper stage of financial distress.

The audit committee's role is to assist the board of commissioners in carrying out its supervisory responsibilities for adequate and effective risk management, financial reporting, control, and good governance. Financial Services Authority Regulation no. 55/POJK.04/2015 concerning the Establishment and Guidelines for the Implementation of Audit Committee Work regulates the duties and responsibilities of the audit committee. These arrangements include reviewing financial-related information published by the company for public or official use, including financial reports, projections, and other related reports, assessing complaints regarding the company's accounting and financial reporting processes, and assessing and providing recommendations to the board of commissioners regarding handling potential conflicts of interest.

Financial distress can arise due to influences from within the company and from outside the company. Internal company factors include: cash flow difficulties, large amounts of debt, and losses from company's operating activities over several years. The external factors can be in the form of an increase in loan interest rates, which causes the interest burden borne by the company to increase. Apart from that, there is also an increase in labor costs, which results in the large production costs of a company causing the increase in labor costs to also increase (Adnyana & Firdaus, 2020).

Previous researchers found that the audit committee had a significant effect on financial distress. An effective audit committee is able to reduce the risk of financial difficulties by improving the quality of supervision of financial reports and strengthening the internal control system (Sadaaa et al., 2023). Good Corporate Governance practices through the role of the audit committee have a negative effect on the possibility of financial distress, because the audit committee functions as an early warning system mechanism in detecting potential financial risks and managerial errors (Suluo et al., 2025). These results strengthen the view that the audit committee plays an important role in maintaining the company's financial stability and preventing worsening financial conditions.

CONCLUSIONS AND RECOMMENDATIONS

Institutional ownership does not affect financial distress in companies that fall under the criteria for Special Notation Issuers with the notation B/D/E/ED, which publish their financial reports on the Indonesia Stock Exchange (BEI) during the 2020-2025 second quarter period. The results of this study do not support the findings of Gerged et al (2023) and Md-Rus et al (2013), which stated that institutional ownership has a negative and significant effect on financial distress. This difference in results shows that in Special Notation Issuer companies (B/D/E/ED), the role of institutional investors as a monitoring mechanism has not been effective in reducing the level of company financial difficulties.

The audit committee has an influence on financial distress in companies that fall under the criteria for Special Notation Issuers with the notation B/D/E/ED,

which publish their financial reports on the Indonesia Stock Exchange (BEI) during the 2020–2025 second quarter period. This finding supports research by Altass (2024), which found that the characteristics and expertise of the audit committee significantly reduce the risk of financial distress. These results indicate that although the audit committee is theoretically and empirically recognized as having an influence on financial distress, its effectiveness is largely determined by its independence, competence, and intensity of supervision.

Companies are advised to strengthen internal governance mechanisms, especially the audit committee function. This strengthening can be done by increasing the competency of audit committee members, increasing independence, meeting frequency, and providing full access to internal audit information and financial reports so that the supervisory function can run more optimally.

ADVANCED RESEARCH

Future researchers are advised to add independent variables and moderating variables to make the research model more comprehensive. Considering institutional ownership does not show a significant influence in this study. Future research can expand the research object to companies in other sectors to see whether the pattern of relationships between variables is consistent across various industries. Research on the manufacturing, financial services, mining, or transportation sectors may show different results, considering that the risk characteristics and financial structure of each sector are not the same as those of Special Notation Issuers.

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