CURRENT ASSET TUNNELING THROUGH RELATED PARTY TRANSACTION: EMPIRICAL EVIDENCE IN INDONESIA

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Abstract

This study focuses on the expropriation of non-controlling shareholders through tunneling activity. Current study in tunneling still found obstacles in measurement because it is difficult to prove, although tunneling activity going on in business practices. The objective of this research is to test tunneling hypothesis and develop tunneling valuation model. This study defines tunneling as related party transactions that are used to tunnel out of public companies's resource for the benefit of the controlling shareholder. This study focuses on current asset tunneling. This study found that from the perspective of the being-tunneled companies, receivables to related parties negatively affect the company's profit margin. Company which announced related party transaction which indicated tunneling obtain negative abnormal return during the announcement of the related party transaction. Based on the assessment method of tunneling, Companies with concentrated ownership have a tendency to do tunneling transactions, compared to firms with dispersed ownership. Being-tunneled companies have lower performance than that are not.

Keywords: tunneling, current asset tunneling, related party transaction.

INTRODUCTION

This study focuses on the expropriation[1] of noncontrolling shareholders through tunneling activity. Johnson et al. (2000a) defines tunneling as a transfer of resources out of the company for the benefit of controlling shareholders.

Current study in tunneling finds obstacles in tunneling measurement because it is difficult to prove, although tunneling activity going on in business practices. Jian and Wong (2003), Cheung et al. (2009b) , Aharony et al. (2009) find that tunneling activity can be conducted through related party transactions[2]. Almost all public companies in Indonesia perform related party transactions (Ratna, 2013). Indonesia is a developing country with characteristics such as low level of investor protection, low level of law enforcement and group structure. these characteristics lead to related party transactions will benefit the group members and at the end will destroy value of the firm (Khanna and Palepu, 2000).

The following is an tunneling illustration that uses related party transactions that result in a decrease in the company's financial performance. Public companies in Indonesia, namely MI[3] indicated perform tunneling activity in the form of coal price manipulation by KC. KC using a special purpose company that is RL in Cayman Island to transfer profits. Here is the structure of corporate ownership:

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[1] Expropriation is the use of controls to maximize their own welfare than the distribution of wealth from another party (Claessens et al. 2000b)

[2] Related party transaction is a transfer of resources, services or obligations between the reporting entity with related parties, regardless of whether a price is charged (PSAK 7,2010).

[3] Code for ethical purpose
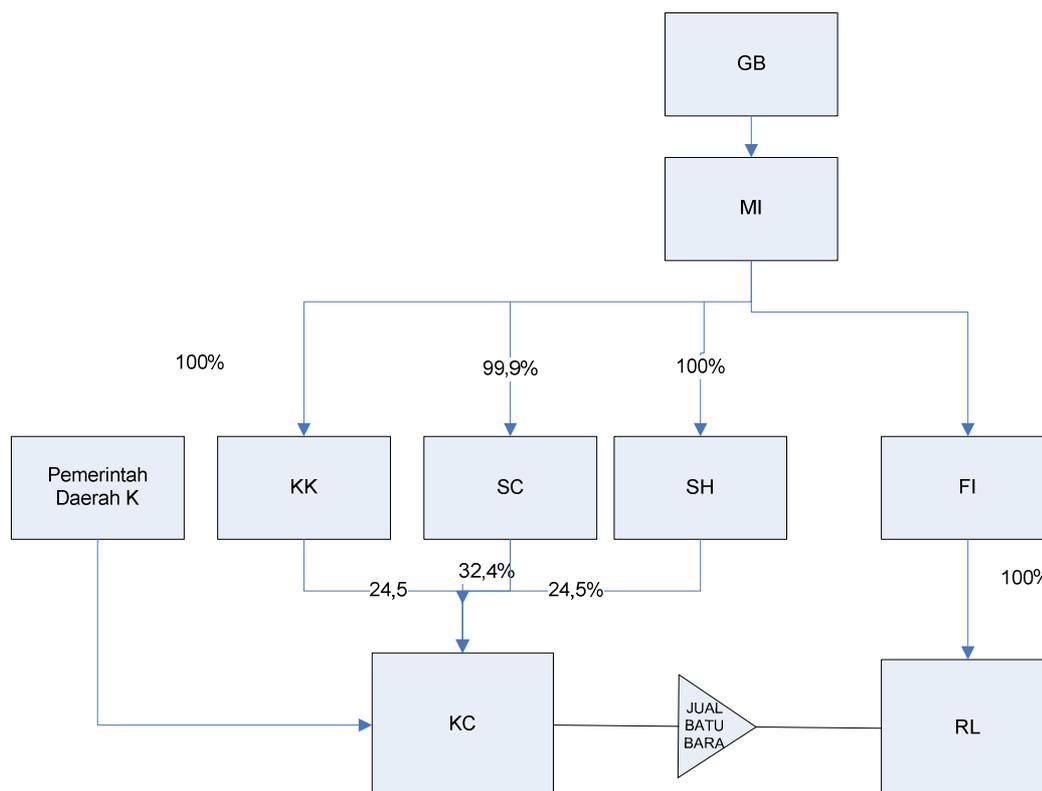
KC and the RL is a subsidiary of PT MI. GB is the ultimate owner of PT MI. KC

does not sell coal directly to potential buyers, but sell it through RL. Coal sold to RL under

reasonable prices, this led KC earnings decline. Then, RL coal reselling at market price,

thereby increasing profits RL. KC is being- tunneled company. Goverment-K, KC non-

controlling shareholder is harmed by the transaction, while the controlling shareholder

(GB) as a whole is benefited, the loss in KC can be covered by profits from RL. These

transactions are classified as cash flow tunneling because (1) the transaction lead a transfer

of resources out of firms in the form of liquid assets, (2) the transaction is beneficial

controlling shareholder at the expense of non-controlling shareholders. Cash flow

tunneling transaction is also as tax avoidance because it is a way to tunnel profits from

Indonesia to Cayman Island which is a tax heaven country. Motivation controlling

shareholders to transfer profits from KC to RL because of cash flow rights in RL is greater

than cash flow rights in KC.

Almost all public companies in Indonesia perform related party transactions (Ratna, 2013). Indonesia has low level of law enforcement and group structure, it will lead to related party transactions will benefit group members and at the end will destroy value of the firm (Khanna and Palepu, 2000). Poor law enforcement and the culture of corruption in Indonesia makes tunnelling cases are not touched by the law. If not prevented, tunnelling causes loss by reducing state tax revenues, causing the migration of resources from Indonesia to tax haven countries, lowering the investment climate, and reducing investor confidence.

To date, unfortunately, research on expropriation is mainly focused on tunneling activity in countries with high level of corporate governance and developed countries ((Bae et al., 2001; Facio and Stollin, 2006; Cheung et al., 2006; Cheung et al., 2009a). However, none of them has taken in developing countries into very close consideration. This research project is therefore dedicated to investigate the issue on tunneling activity in country with low level of corporate governance and emergent economy. Indonesia is a very interesting laboratory for this research, since the problems with governance, such as related part lending or crony capitalism. It is one of the institutional problems behind the 1997 Asian crisis.

The first issue in this study is related to the tunneling hypothesis and the implications for the company's financial performance. Accordingly, this study defines the tunneling hypothesis as related party transactions that are used to tunnel out of public companies's resource for the benefit of the controlling shareholder.

Related party transactions that are used for tunneling will cause the company's performance decline. Testing the influence of related party transactions on the company's

performance is expected to provide a direct measure of tunneling due to measure the company's actions/activities which led to the transfer of resources out of the company for the benefit of the controlling shareholder.

In this study, tunneling is divided based on resources being tunneled[4] into three categories: current asset tunneling, fixed asset tunneling and equity tunneling. Current asset tunneling is a transaction that transfers cash or current assets out of company to the related party. Fixed asset tunneling move the long-term assets (tangible/intangible) from (to) the company to (from) the related party. Equity tunneling is increased ownership of the controlling shareholder at the expense of noncontrolling sharehoder, but does not change the company's productive assets. Categorization is important because each category has a different effect on the company's financial ratios. This study focused on current asset tunneling.

The second research issues is to develop cash flow tunneling prediction model. Currently there is no model to predict which firms are likely to be the object of tunneling or not based on the characteristics of the company. The absence of predictive models resulting in high risks faced especially by non-controlling shareholders, because empirical evidence showed that being-tunneled company will be impaired.

Theoretical Framework and Hypothesis Development

Johnson et al. (2000a) define tunneling as transfer of assets and profits out of the company for the benefit of controlling shareholders. Johnson et al. (2000a) divide tunneling into two types:

1. Controlling shareholder can move resources from the company to its interests through self-dealing transaction, the transaction either illegal/fraud, sale of assets

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[4] Atasanov et al. (2008) divide tunneling into 3 chategories: cash flow , asset and equity tunneling.

through contracts such as transfer pricing that benefit the controlling shareholder, excessive executive compensation, loan guarantees, expropriation on the occasion of the company, etc..

2. Controlling shareholder can increase their ownership in the company without giving/transfer of assets through a dilutive share issues, minority freeze-outs, insider trading, creeping acquisitions and other transactions that harm noncontrolling shareholders.

Company conduct related party transactions for three motives: First, the transaction relates is used to minimize transaction costs (Cook, 1977 and Fisman and Khanna, 1998). The transaction is categorized as a related party transaction for economic goals. Second, related party transaction can be used to manipulate earnings (Jian and Wong, 2003; Aharony et al, 2009). Third, the related party transaction is used for the purpose of tunneling (Cheung et al., 2009a; Cheung et al., 2009b; Cheung et al., 2006). The second and third transactions are for opportunist goal.

As a developing country, Indonesia has characteristics such as low level of investor protection, low level of law enforcement and group structure. these characteristics lead to related party transactions will benefit the group members and at the end will destroy value of the firm (Khanna and Palepu, 2000). Lack of information and regulations regarding related party transactions cause difficulties for users of financial statements to assess whether the transactions relate done for economic or opportunistic purpose.

Some studies indicate that related party transaction is used to tunneling. Jian and Wong (2003) found that the company uses receivables to related party as a tunnel to transfer resources out of the company. Cheung et al. (2009b) find empirical evidence that the sale and purchase of assets to related party are used to perform tunneling. Asset tunneling through the sales of assets to related party at a lower price than the price at an

independent party transactions and the purchase of the assets from related party at higher prices compared with in independent transactions.

Companies that conduct related party transaction which indicated tunneling has values decreased at the announcement of the transaction (Cheung et al., 2006 and Cheung et al., 2009a). Related party transaction which indicated as current asset tunneling is receivables to related party (Cheung et al., 2006; Cheung et al., 2009a).

Jian and Wong (2003) states that there are two ways to do tunneling. First, the company provides a high accounts receivable or long credit periods to the related party when selling the product. Second, the company providing the loan to related party (in the financial statements included in other receivables post). Loans to controlling shareholders and affiliates is one way for controlling shareholders to transfer resources to their interests.

Jian and Wong (2003) find empirical evidence that when firms have high free cash flow, they will tunnel the excess of such resources for the benefit of controlling shareholders through the provision of credit. Aharony et al. (2009) provide empirical evidence on tunneling activities in China through a credit transaction to related party after the IPO. Receivables to related party can also be understood as a put option, related parties can exercise such option by not paying their loan in the bad state (Atanasov, 2008).

As a developing country, Indonesia has low level of investor protection. It will cause that related party transactions will benefit group members and at the end will destroy value of the firm (Khanna and Palepu, 2000). Jian and Wong (2003) and Aharony et al. (2009) find empirical evidence that companies that have excess resources will transfer resource for the benefit of controlling shareholders through related party receivables. Receivables to related party can also be understood as a put option, related parties can exercise such option by not paying their loan in the bad state (Atanasov, 2008). We predict that receivables to related party as a tunnel to transfer resource for the benefit controling

shareholders. If the credit to related party is used for tunneling, the company will provide a larger credit than received credit from the related parties. In addition, the company will provide credit terms to related party at lower interest rates than market rates. Provision of credit under the interest rate will decrease in net earnings.

H1a: From being-tunnelled company perspective, accounts receivable to related party negatively effect on the company's performance.

H1b: From being-tunneled company perspective, there are negative abnormal return during the announcement of the account receivables to related party transaction.

In concentrated ownership structure, the controlling shareholder can control the company's resources for personal gain at the expense of the interests of non-controlling shareholders. Shleifer and Vishny (1997) suggest that controlling shareholders are more interested in using its control to obtain private benefits. Controlling shareholders can implement policies that benefit them at the expense of minority shareholders (La Porta et al. 2000b). The controlling shareholder can effectively determine the manager's decision. Controlling shareholders can adopt policies that benefit themselves, including contractual policies to related party. For example, the entity selling the goods to subsidiaries at cost, may not be sold with such requirements to other parties, entities also can making loans without interest to the related party. So we hypothesized that being-tunneled firms have more concentrated ownership than firms that are not .The proposed hypothesis is:

Hypothesis 2a: there are differences in company's structure between the *being-tunneled* companies and that are not

Bertrand et al., (2002) found that being-tunneled companies experience decreased performance, while the tunneling company will increase performance. Jian and Wong (2003) states that when a company has excess financial resources, the controlling

shareholder will move resources or tunneling of resources to their interests rather than distribute dividends. Therefore, we predicts that being-tunneled firms has lower performance than firms that are not.

Hypothesis 2b: there are differences in company's performance between being-tunneled companies and that are not.

RESEARCH METHOD

The population in this study were all public companies listed on the Indonesia Stock Exchange except banking company. Observation period began in 2008 to 2010. Sample selection using purposive sampling method, the method of sample selection with some specific criteria. The criteria are intended is as follows:

1. Companies that do related party transaction because the transaction has a chance as a channel for tunneling.

2. Listed companies are active at the Indonesia Stock Exchange consistently from year 2008-2010.

3. The Company has a full financial report for the period of observation.

4. Companies with profits close to zero were excluded from the sample because the company can be used to related party transactions to manipulate earnings (increase profits). The focus of this study was related party transactions that are used to perform tunneling, so that companies with profits close to zero were excluded from the sample.

5. The Company is not engaged in the financial industry.

To test hypotesis 1b,2a and 2b, data obtained from the affiliate transaction and conflict of interest disclosure earned from BAPEPAM and LK. The report includes details on affiliate and conflicts of interest transactions such as objects of the transaction, the transaction value, transaction date, announcement date, a description of the relationship. While data

from the financial statements do not disclose about the announcement date of the transaction.

Measurement of Variables:

1.Measurement of account receivables to related party

Variabel account receivables to related party	Measurement
Account receivables/TA	$\dfrac{Account\ receivable\ to\ related\ party}{total\ asset}$
Net Account receivables/TA	$\dfrac{Account\ receivables - account\ payables\ on\ related\ party}{total\ asset}$
Change Account receivables/TA	$\dfrac{Account\ receivables(t) - Account receivables\ (t-1)on\ related\ party}{total\ asset}$
Account receivables/SA	$\dfrac{Account\ receivables\ to\ related\ party}{total\ sales}$
Net Account receivables/SA	$\dfrac{Account\ receivables - account\ payables\ on\ related\ party}{total\ sales}$
Change Account receivables/SA	$\dfrac{Account\ receivables(t) - Account receivables\ (t-1)on\ related\ party}{total\ asset}$

Variables net receivables are measured from the difference between accounts receivable with account payable. Cheung et al (2009) classifies accounts receivable to related party as tunneling while account payable on related party as propping. Net Receivables measure how likely companies do tunneling than propping. Net receivables positively show account receivables greater than account payable, so the company has a high propensity to tunneling than propping.

2. Measurement of ownership variables

Ownership of public companies can be classified into two general categories: dispersed ownership and concentrated ownership. Companies with dispersed ownership is a company that does not have a controlling shareholder. Companies with concentrated

ownership is a company that has a controlling shareholder on the boundary separating certain control rights.

3. Measurement of abnormal return

Abnormal return is the difference between actual returns and expected returns, the formula of abnormal returns following :

$$AbnReturn = R_{i,t} - E(R_{i,t})$$

Return expectations using the mean-adjusted model:

$$E(R_{i,t}) = \frac{\sum_{t1}^{t100} R_{ij}}{T}$$

Empirical Model

the following equations to test hypothesis 1:

MLB $= \alpha_{11} + \alpha_{12}$TPB $+ \alpha_{13}$ KI $+ \alpha_{14}$ JI $+ \varepsilon$ ……………(1)

GM: gross margin

RPT: receivables to related party

IP: industry performance

IT: industry type

To test Hypothesis 1b, we measure abnormal return arround announcement of related party transaction. Return expectations using the mean-adjusted model:

$$E(R_{i,t}) = \frac{\sum_{t1}^{t100} R_{ij}}{T}$$

To test Hypothesis 2a and 2b, we conduct two stages steps. The first stage, Valuation method for identification of related party transactions which tunneling and which are not. Related party transactions are categorized as tunneling if have the following characteristics:

1. Negative abnormal return during the announcement of the related party transaction.

2. Related party transaction are classified as tunneling category based on the classification of Cheung et al. (2006) and Cheung et al. (2009b).

3. There is overlapping the owner. Overlapping owner is similarities controlling owner between the company and related party. Goranova (2007) found that the overlapping owner will transfer resources from the company's low cash flow right into the company's high cash flow rights.

4. There are similarities the directors and commissioners between the company and the related party. The similarity of key management personnel provide the opportunity of using power to regulate the financial policies and operations, so as to obtain benefits from such activities.

5. There are family relationships that may affect or be affected. Company policy can be influenced by family.

6. These transactions are not considered by the Office of Appraisal Services.

The second step, the prediction model tunneling is using Multiple Discriminant Analysis (MDA) to predict group membership. The Purpose of the prediction model is to predicts correctly the company which conducting tunneling transaction and not by the independent variables. This analysis requires a comparison sample of the companies that do not conduct related party transaction which not indicated tunneling (non tunneling). Because the majority of companies in Indonesia do relate to the transaction, then the non-tunneling company must meet all the following conditions:

Table 1: Criteria of Comparison Sample (Non Tunneling)

No	Criteria of Comparison Sample (Non Tunneling)
1	Ratio of related party sales less than 0.00014. This value is below the average of all related party sales transactions in Indonesia by 0.1218
2	Ratio of the related party purchase is less than 0.000124. This value is below the average of all related party purchase in Indonesia 0.6790
3	The ratio of related party accounts receivable less than 0.000124. This value is below the average related party accounts receivable to all public companies in Indonesia 0.2475
4	Net Income positive. Tunneling aims to transfer resources, so companies with NI positf will have the opportunity to perform tunneling than companies with negative NI.

Analysis of MDA is used to predict the being-tunneled companies and not. The equation used is as follows

$D = \beta_1 KM + \beta_2 KID + \beta_3 KIA + \beta_4 KP + + \beta_5 KN + \beta_6 KK + \beta_7 ROA + \beta_8 PM + \beta_9 GM + \beta_{10} PER + \beta_{11} OPRM$ . .(2)

RESULT

Hypothesis 1a predicted that from the perspective of the being-tunneled companies, receivables from related parties negatively affect the performance of the company. This hypothesis is supported if the coefficient α12 estimation equation 1 negative and significant. The estimation results of equation1 for all measurement indicate that the negative and significant coefficient α32.

Table 2
Hypothesis Testing Results
$MLB = \alpha_{11} + \alpha_{12}TPB + \alpha_{13} KI + \alpha_{14} JI + \varepsilon$ ……………(1)

Independen Variable	Prediction	α_{32}	α_{33}	α_{34}	F	R^2	N	Hypothesis
Account receivables /TA	α_{12} negatif	-0.826***	33.484**	-4.368**	12.256***	4.6%	694	supported
Net Account receivables /TA	α_{12} negatif	-0.943***	33.493**	-4.377**	11.701***	4.4%	694	supported
Change Account receivables /TA	α_{12} negatif	-0.047*	32.787**	-4.442**	4.364***	1.4%	694	supported
Account receivables /SA	α_{12} negatif	-0.127***	33.376**	-4.640**	13.032***	5%	694	supported
Net Account receivables /SA	α_{12} negatif	-0.149***	33.643**	-4.624**	12.905***	4.9%	694	supported
Change Account	α_{12} negatif	-0.060***	34.065**	-4.405**	8.833***	3.3%	694	supported

| receivables |
| /SA |

In the first measurement that is related receivables/total assets, the coefficient α_{12} (-0826) was negative and significant at 1% alpha. In the second measurement that is net-receivables of related party transaction. Net-receivables is difference between receivables to related party and debt from related party of related debt. Receivables from related parties are indicated as tunneling while the debt from related party transaction are indicated propping (Cheung et al, 2009). Net receivables measures how likely the company doing tunneling than propping. Positive net receivables- demonstrate that companies have a higher tendency than do tunneling propping. The test results showed that the coefficient of the variable net receivable $\alpha 32$ negative and significant at 1% alpha.

In the third measurement that is changes receivables to related party, α_{12} negative and significant coefficient on alpha 1%. The test results show that firms in period t gives receivables greater than the previous period (t-1) will decrease the company's net profit margin.

Empirical evidence, as shown in Table 1, hypothesis 1a supported that from the perspective of the being-tunneled companies, receivables to related parties negatively affect the company's net profit margin.

Testing hypothesis 1b show that companies which announce receivables to related party obtain the abnormal return (AR) negative at the time of announcement of the transaction to the period of the window (-3, +3).

Tabel 3
Cumulative abnormal return at the time of announcement of receivables to related party
2009-2010

Transaction	Mean Adusted, (-3,+3)
CASH FLOW *TUNNELING* :	
1 Elimination of related party receivables	-0,00669
2 Account receivables to related party	-0,06755
3 Warranty account receivables	-0,01284

On average, during the window period (-3, +3), the company indicated that the transaction cash flow tunneling obtain mean adjusted return negative. Elimination of related party receivables obtain mean adjusted abnormal return of -0.66%, Account receivables to related party gain -6.7% and warranty account receivables from related party obtain -1.2%.

Based on the valuation of tunneling methods in this study, the following are examples of transactions are indicated as tunneling. In the case of tunneling, the researchers used the code for ethical reason. Although the valuation method was built based on theoretical studies and discussions with regulatory authorities and academicians, researchers do not make confirmation with the company. Therefore, the researchers used a code for ethical reasons. A public company in Indonesia, namely PT ED through PT DD conduct transactions with PT MM. Family GQ as controlling shareholder of PT ED and PT MM. Figure 2 show the nature of the related party transactions of PT ED / DD with PT MM.

KELUARGA GQ

100%   100%

EC   SC

60,6%   39,4%

MIN   COD   ST   ECE   PUBLIK

10%   90%   0,9   11,65%   36,76

50,7%

PT ED

MM   TRANSAKSI   DD

DTA   DTI
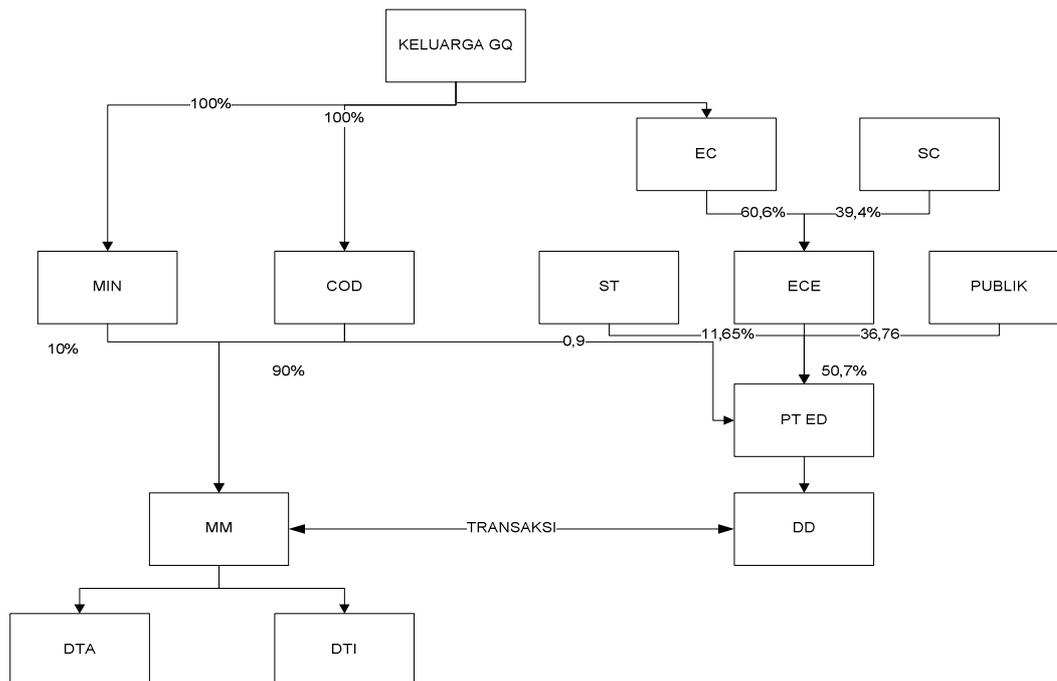
Figure 2. Ownership Structure PT ED

PT ED and PT MM and also have the same Commissioners and Directors. The commissioners and directors held by family members of the controlling shareholder.

On June 26, 2009, through its subsidiary PT ED, DD, has signed a purchase agreement with the MM to take over 99.9% of DTA and 99.9% of the DTI. PT ED also pay off the entire debt of DTA and the DTI to MM. Total transaction and subrogation agreed amount of U.S. $ 886,013. Amount of US $75,122 used to buy shares DTA and the DTI and US$ 810,891 used for debt repayment DTA and the DTI to MM.

GQ has a family of total cash flow rights in MM at 100% while the total cash flow rights in PT ED by 50.7%. Cash flow rights of controlling shareholders is greater in MM than in a public company (PT ED). The difference in cash flow rights is an incentive for companies to tunnel resources from the low company's cash flow right (PT ED tbk) to the high company's cash flow rights (MM). The tunneling are classified as cash flow tunneling. PT ED and MM/ DTI / DTA are related because both parties have jointly controlled entity and that share a common key management personnel. PT ED issue of

U.S. $ 810,891 cash for debt repayment DTA and the DTI. In addition, PT ED issue of US $75,122 cash to buy the DTI although the DTI enterprises that have a net loss (Rp5.257.128.705,) and the DTA, which had a net loss worth (Rp734.908.351).

Transaction of PT ED is indicated as tunneling. Indicators used are:

1. There is a negative abnormal return during the announcement of the transaction (-0.01079). This shows the company and minority shareholders suffered losses as a result of the transaction.

2. Included in the category of transaction tunneling under study Cheung et al. (2009a).

3. There are overlapping owner. The company and related party is owned by the same owner of the family of GQ.

4. There are common key management personnel.

Provision and elimination of accounts receivable also can be used for tunneling transaction. The following is an illustrative case indicated as cash flow tunneling. PT AI (Public company) give affiliate receivables to INC. INC is owned by PT AI by 50%. Financial statements INC are not consolidated on Financial Statement of PT AI. PT AI and the INC also have the same key management personnel. Chairman and president of the INC is a director at PT AI. President director of the INC was a director at PT AI. Commissioner of the INC is also a commissioner of PT AI.

PT AI provides interest-free receivables, unsecured and unspecified payment period. Receivables awarded since 2005. On 11 November 2010 the company announced the elimination of these receivables. At date of the announcement, the company experienced a negative CAR of -0. 06%. Based on the assessment method of tunneling, the transaction is indicated as tunneling by the indicator:

1. There is a negative abnormal return during the announcement of the transaction by -0.006689.

2. PT AI INC has the same commissioners and directors.

3. There are resources out from company. Cheung et al. (2006) classify the transaction of account receivable to related party as a tunneling transaction.

The next step is to create predictive models of companies that do tunneling and are not based on firm characteristics. MDA Analysis using equation 1 is used to predict being-tunneled company or not.

Table 4
MDA Analysis

$$D = \beta_1 KM + \beta_2 KID + \beta_3 KIA + \beta_4 KP + \beta_5 KK + \beta_6 KK + \beta_7 ROA + \beta_8 MLB + \beta_9 MLK + \beta_{10} PER + \beta_{11} MOPR \ ....(1)$$

Independent Variables	
Manajemen Ownership (KM)	1,146
Domestic Instututional Ownership (KID)	1,153
Foreign Institutional Domestic (KIA)	0,955
Public Ownership (KP)	0,000
Ownership Classification (KK)	12,011***
Return On Asset (ROA)	1,320
Net Profit Margin (MLB)	8,089**
Gross Margin (MLK)	20,0447***
Price Earnings Ratio	2,130
Operating Margin (MO)	5,482**
Wilks' Lambda	0,697*
Classification result	75,2%

***Nilai F signicant at alpha 1%
**Nilai F signicant at alpha 5%
*Nilai F signicant at alpha 10%

In general, ownership structure variables had no significant effect on the possibility of tunneling transactions by company. This is consistent with Cheung et al. (2009a) that the ownership structure variables can not explain the possibility of corporate conduct the value destroy related party transactions.

Ownership classification variables significant at alpha 1% that is able to distinguish being-tunneled companies and that are not. Companies with concentrated ownership have a tendency to make transactions tunneling, compared to firms with dispersed ownership. Profitability ratios that use the components of operating income (gross margin and operating margin) and net income (Profit margin and PER) have a significant effect. It means be able to distinguish between being-tunneled companies and that are not. This is consistent with research Bertrand et al. (2002) that the being-tunneled companies experiance decreasing profitability, while the tunneling company experience increasing profitability.

Conclusion, Implication and Limitation

Empirical findings of this study have important theory implications, accounting implication, policies implication, and practices implication. Implications of the theory deals with the expropriation phenomenon through contractual policy with other companies, whereas past research has focused on expropriation through operations policy. Expropriation can occur through the related party transactions. With significant control and influence that is owned, controlling shareholders have the power to set corporate policy to obtain benefits from the related party transaction. Controlling shareholder can influence the pricing policy, ammount and type of related party transactions. This study found empirical

evidence that related party transaction can be used as a tunnel to transfer resources out of the company to the controlling's interests at the expense of minority shareholders. Being-tunneled companies decreased the financial performance and market performance. These results are consistent with the phenomenon of expropriation of minority shareholders through contractual policies. Companies with concentrated ownership have a tendency to do tunneling transactions, compared to firms with dispersed ownership. Being-tunneled companies have lower performance than that are not.

Accounting implications related to the quality of disclosure of related party transaction. Disclosures of related party transactions set forth in PSAK No. 7 of 2010. The quality of disclosure is important as a basis for decision making by users of financial statements. However, based on the results of data analysis, the disclosure of related party transactions in the financial statements are very limited.

Practice implications related to the development of predictive models to predict companies which had a tendency to do tunneling and which are not. Model predictions are expected to assist investors in anticipation of the risk of tunneling that may occur through related party transaction.

Limitations and Suggestions

Formation model consists of two stages. The first phase of building the model and the second phase of model testing. This study is limited to building a predictive model of tunneling, testing the model predictions can not be done because the affiliate transaction data obtained from Bapepam-LK from 2009 to 2011. Data in 2009 and 2010 are used to build the model, the data used to test the model 2011. But at the time the study was made, in 2011 the company's financial statements have not been published, so that further research is expected to test the model that has been established in this study.

The research data was taken prior to the effective date of the application of PSAK 7 2010.

Further research can be done using the data of financial statements in 2011, to know the

differences to the quality of related party disclosure before and after implementation of

PSAK in 2010.

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