Influence of Accounting Policies on Financial Distress: The Moderating Role of Corporate Governance

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ABSTRACT

This study investigates the impact of investment policy (IOS), funding policy (LEV), and operational policy (TATO) on financial distress, with good corporate governance (GCG) as a moderating variable. The research employs a quantitative approach, focusing on manufacturing firms listed on the Indonesia Stock Exchange (IDX) from 2018 to 2022. The sample includes 935 companies, with financial data represented by ratios such as CAPBVA, DAR, TATO, and GCG. Logistic regression analysis is used to evaluate the relationships. The findings reveal that both funding policy and operational policy significantly influence financial distress, whereas investment policy does not exhibit a significant effect. Furthermore, the study shows that GCG moderates the relationship between LEV and financial distress. However, GCG does not moderate the relationships between investment policy or operational policy and financial distress. These results underscore the nuanced role of corporate governance in mitigating financial distress, depending on the specific financial policies under consideration.

Keywords: Financial Distress; Investment Policy; Funding Policy; Operating Policy; Good Corporate Governance.

Good Corporate Governance Sebagai Pemoderasi Antara Kebijakan Akuntansi Terhadap Financial Distress

ABSTRAK

Riset ini mempunyai tujuan untuk menganalisa pengaruh kebijakan investasi (IOS), kebijakan pendanaan (LEV), dan kebijakan operasi (TATO) serta variabel moderasi GCG terhadap financial distress. Sampel penelitian berupa perusahaan bidang manufaktur yang terdaftar di Bursa Efek Indonesia (BEI) dari tahun 2018 – 2022 yang berjumlah 935 perusahaan yang diuji dengan metode kuantitatif. Data penelitian terdiri dari rasio keuangan pada laporan keuangan yaitu terdiri dari CAPBVA, DAR, TATO, dan GCG. Penelitian ini dianalisa dengan menggunakan teknis analisis regresi logistik. Hasil riset ini yaitu kebijakan pendanaan dan kebijakan operasi dapat mempengaruhi terjadinya financial distress, sedangkan kebijakan investasi mempengaruhi terjadinya financial distress. GCG sebagai pemoderasi hanya dapat memoderasi LEV dengan financial distress, sedangkan hubungan antara kebijakan investasi dan kebijakan operasi terhadap financial distress tidak dimoderasi oleh GCG

Kata Kunci: Financial Distress; Kebijakan Investasi; Kebijakan Pendanaan; Kebijakan Operasi; Good Corporate Governance.

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INTRODUCTION

In the business world, companies often encounter financial difficulties that can escalate to bankruptcy. Understanding the factors contributing to financial distress is crucial to mitigating such risks. One significant aspect influencing financial health is corporate governance, which can improve organizational structure and transparency. Poorly managed debt also exacerbates financial difficulties, as noted by Mariano et al., (2020). Developing countries in Asia face unique economic, regulatory, and market challenges, where economic uncertainty, market fluctuations, and weak regulatory oversight can amplify financial distress (Younas et al., 2021).

Manufacturing firms listed on the Indonesia Stock Exchange (IDX) frequently experience financial volatility, manifesting as challenges such as credit defaults, declining sales, bad debts, unpaid dividends, and other indicators of financial distress. These early warning signs, if not addressed, can lead to bankruptcy, resulting in losses for investors and creditors (Widhiastuti et al., 2018; F. Zhou et al., 2022). Economists describe financial distress as a condition that increases a firm's expenses and forces critical decisions affecting stakeholders, including creditors, suppliers, employees, and customers. Financial distress also weakens a firm's market position, making it vulnerable to competitors seizing its market share (Opler & Titman, 1994).

The fluctuating nature of economic conditions continuously affects firms' performance and operational stability. Intense competition further compounds costs, and firms unable to sustain themselves under such pressures face bankruptcy (Syuhada & Muda, 2020). Financial reports provide critical insights into a company's condition, enabling stakeholders to assess performance and make informed decisions. Converting financial data into actionable information is essential to minimize the risk of bankruptcy. Improvements in financial distress models can aid in identifying and addressing potential failures, thereby safeguarding companies against insolvency (Rissi & Herman, 2021).

Globally, bankruptcies in the manufacturing sector are prevalent. In Texas, for example, the first half of 2023 witnessed a sharp rise in bankruptcies across the retail, service, and manufacturing sectors, with manufacturing bankruptcies nearly doubling compared to 2022 and accounting for 33% of all cases during that period (Schwartz et al., 2023). Similarly, Indonesia has experienced significant layoffs in the manufacturing industry, particularly in the Textile and Textile Products (TPT) sub-sector, due to declining sales and factory closures. By August 2024, the Indonesian Manufacturing Purchasing Manager's Index (PMI) contracted to 48.9, indicating decreased output, new orders, and employment levels (Revo, 2024).

The financial reports of firms listed on the IDX are publicly accessible, enabling stakeholders to assess corporate performance. These reports are critical for determining whether a company is thriving or experiencing financial distress, providing transparency for external and internal assessments (Istiani et al., 2020). Financial distress arises from three primary factors: sustained losses, excessive debt burdens, and insufficient capital. Balancing these elements is crucial to prevent financial distress from escalating to bankruptcy. Companies must proactively analyze their financial conditions to maintain investor and creditor

confidence. When financial distress occurs, stakeholders such as creditors and investors may become hesitant to provide loans or capital, further jeopardizing the firm's stability (Saputri, 2023; Dirman & Utami, 2023).

A company acts as an agent entrusted by shareholders and bears full responsibility for its activities. When a company incurs losses that lead to financial distress, management is often perceived as ineffective in fulfilling its fiduciary duties. Governance issues, such as those observed during Indonesia's 1997 economic crisis, highlight the importance of robust corporate oversight. At that time, weak institutional supervision, substandard business practices, and poor funding and investment decisions reflected the absence of sound governance principles. These challenges emphasized the critical role of governance, particularly during periods of financial instability (Handriani et al., 2021).

Financial distress typically arises when a company's financial condition deteriorates consistently. This decline can result from inadequate financial planning, poor decision-making, and interrelated weaknesses within management. Poor managerial practices are among the most significant contributors to financial distress, as management decisions influence recovery efforts and affect the firm's market value relative to its industry peers. Effective corporate governance mechanisms are essential for improving financial performance, fostering recovery, and maintaining stakeholder trust (Annisa et al., 2022; Fakhar et al., 2021). A well-functioning governance system guides a company's policies, strategies, and operations, ultimately enhancing profitability and sustainability.

To mitigate financial distress, firms must adopt sound financial policies encompassing operational, funding, and investment strategies. These policies improve financial performance and reduce the likelihood of financial distress (Jariyah & Budiarti, 2019). In this study, investment, funding, and operating policies are represented by the investment opportunity set (IOS), leverage, and total asset turnover (TATO), respectively. Agency theory underpins the selection of these proxies, as financial distress often reflects agency problems. Increased agency conflicts reduce firm performance and heighten financial distress risk. However, aligning managerial incentives with organizational goals can mitigate these conflicts and enhance managerial performance (Ugur et al., 2022).

Leverage, as a financial proxy, plays a dual role in reducing agency conflict. It pressures management to optimize performance by meeting debt obligations and invites stricter oversight by creditors, thereby lowering bankruptcy risk. Similarly, total asset turnover reflects the efficiency of asset utilization. High TATO indicates effective resource management and serves as a tool to monitor and discipline managers, thereby reducing agency problems and financial distress risks (Sumani, 2020).

IOS, which represents the firm's investment opportunities, is another critical factor in agency theory. Firms with high IOS may incur elevated agency costs due to underinvestment or risk-shifting behaviors. Managers in such firms might prioritize risky projects over stable, profitable investments, increasing the potential for financial distress (Callen & Chy, 2024).

Prior research on financial distress has yielded mixed findings. For example, Prasetyo & Kristanti (2021) found that leverage does not significantly

affect financial distress, whereas Chrissentia & Syarief (2018) concluded that leverage positively influences financial distress. Similarly, Mahaningrum & Merkusiwati (2020) reported that TATO has no impact on financial distress, while Agustini & Wirawati (2019) identified a negative relationship between TATO and financial distress. These inconsistencies highlight the need for further investigation into the determinants of financial distress.

While leverage and TATO have been extensively studied, research on the influence of IOS on financial distress remains limited. Given the inconsistencies in existing findings, further exploration of these variables is crucial to enhance our understanding of financial distress and its underlying causes. This research aims to address these gaps by examining the nuanced roles of IOS, leverage, and TATO in financial distress, providing new insights into their interplay within the context of corporate governance.

Good Corporate Governance (GCG) serves as a moderating variable in this study, as it is a critical factor in preventing financial distress. Widyaningsih (2020) emphasizes that GCG enhances economic efficiency by fostering robust relationships among shareholders, stakeholders, the board of commissioners, and management. GCG, as a framework emerging from globalization, enables companies to strengthen their market positions and maintain competitive advantages. Effective governance practices can also reduce capital costs, improve firm performance, and mitigate the risk of financial distress.

Begum et al., (2023) underscore that optimal corporate governance minimizes the likelihood of financial distress, while weak governance heightens it. Key governance elements, including an effective board, high-quality audits, and active owner involvement, significantly enhance a company's financial health. Jurnali & Putri (2024) further highlight that GCG is instrumental in fostering corporate development, ensuring the sustainability of operations, and maintaining investor confidence. Conversely, mismanagement of financial and asset structures can exacerbate financial distress.

One of the core accounting principles, the going concern assumption, underscores the importance of a company's ability to sustain operations in the future. Analyzing financial distress and potential bankruptcy remains highly relevant for identifying strategies to ensure long-term viability, particularly during periods of unexpected economic difficulty.

Agency theory provides a useful lens for understanding conflicts between shareholders (principals) and managers (agents) when pursuing corporate strategies. High-profile corporate failures, such as Enron, demonstrate how poor governance and conflicts of interest can precipitate financial difficulties. Agency theory posits that governance weaknesses, including poorly structured boards and inadequate oversight, contribute to agency problems, such as financial fraud, tax evasion, and bribery (Mariano *et al*., 2020).

Defined as a contract between a firm's owners and managers, agency theory highlights the potential for conflict arising from the separation of ownership and control. Prasetyo & Kristanti (2021) note that this separation necessitates entrusting management to experienced professionals capable of maximizing profitability at efficient costs. Gerged et al., (2022) further explore how agency theory can inform strategies to optimize governance practices, reduce

conflicts of interest, and improve financial performance, thereby mitigating financial distress.

Financial distress encompasses various adverse conditions within a company, such as insolvency, default, or bankruptcy. Martini *et al.* (2023) describe insolvency as a liquidity crisis linked to poor financial performance, while default arises when a firm fails to meet creditor agreements, often resulting in legal proceedings. Persistent negative operating profits can signal a company's vulnerability to financial distress.

Nanda, *et al.* (2018) find a negative relationship between financial distress and investment opportunity set (IOS) in property and real estate sector companies. Financial distress diminishes IOS, thereby lowering firm value. Enhancing IOS and avoiding financial distress are crucial for sustaining firm value and long-term profitability.

H_1: Investment policy has a negative effect on financial distress.

Several studies indicate that leverage, as a funding policy, significantly influences financial distress. Excessive debt increases vulnerability, particularly when firms struggle to generate stable revenue to meet debt obligations. High leverage ratios relative to equity or assets expose firms to greater risks from economic fluctuations, potentially leading to repayment difficulties. Conversely, lower leverage ratios indicate financial stability, signaling a favorable investment environment for investors (Pane et al., 2023; Rissi & Herman, 2021; Mahaningrum & Merkusiwati, 2020; Maeyen, 2021).

H_2: Funding policy has a positive effect on financial distress.

Research by Anita Putri et al (2022) concludes that total asset turnover (TATO) significantly influences financial distress. Effective asset management enhances financial performance, enabling companies to use assets efficiently and avoid financial distress. Similarly, Oktariyani (2019) finds that TATO negatively affects financial distress in manufacturing firms, indicating that ineffective asset utilization can lead to corporate losses and financial instability. These findings underscore the importance of optimizing asset performance to mitigate the risk of financial distress.

Further research by Safa & Nuswandari (2022) also highlights a negative relationship between TATO and financial distress. A high TATO reflects efficient resource utilization and robust management practices. Companies with strong asset efficiency can generate sufficient profits, allowing them to meet financial obligations and avoid distress. This demonstrates how operational efficiency safeguards financial health.

H_3: Operational policy has a negative impact on financial distress.

The implementation of good corporate governance (GCG) provides a clearer picture of a firm's financial condition and enhances its attractiveness to investors, thereby reducing the likelihood of financial distress (Yuliani & Rahmatiasari, 2021). Al-Gamrh et al., (2020) found that firms with strong corporate governance are better positioned to mitigate the adverse effects of investment opportunities on performance. By optimizing governance practices, firms can reduce external risks and sustain performance, minimizing the risk of financial distress.

H_4: Good corporate governance strengthens the influence of investment policy on financial distress.

Sakinah (2018) shows that leverage, when moderated by GCG, has a significant positive effect on financial distress. While poor balance between obligations and income negatively affects firms, those with strong governance and robust income generation can improve their financial condition. Effective GCG fosters competent managerial decision-making, enabling firms to manage leverage more effectively.

Research by M. Zhou et al., (2021) demonstrates that high-quality corporate governance negatively impacts financial leverage. Firms that practice optimal governance tend to have lower leverage, reducing their vulnerability to financial distress. This finding highlights the critical role of GCG in minimizing financial risk associated with excessive leverage.

H_5: Good corporate governance weakens the influence of funding policies on financial distress.

Putri & Wulandari (2021) emphasize that GCG enhances company performance while fostering investor confidence, customer satisfaction, and a positive corporate image. Optimal governance promotes efficient asset utilization, boosting sales and reducing the risk of financial distress. This aligns with the notion that robust governance practices strengthen operational policies, improving financial stability.

H_6: Good corporate governance strengthens the influence of operational policies on financial distress.

RESEARCH METHODS

This study adopts a quantitative approach to examine the relationships between variables and the moderating role of good corporate governance (GCG). The quantitative method is employed to analyze the effects of investment policy (IOS), funding policy (leverage), and operating policy (TATO) on financial distress, with GCG moderating these relationships. The independent variables are examined for their influence on the dependent variable of financial distress, providing a comprehensive understanding of these interactions.

Financial distress refers to a company's financial condition during periods of economic difficulty. This study measures the dependent variable using a nominal scale, following the methodology of Syuhada & Muda, (2020). A dummy variable is applied, assigning a code of 1 if the company records negative profits for two consecutive years and 0 if otherwise during the observation period. This approach is grounded in empirical evidence, as studies by (Manurung & Munthe, 2019; Syuhada & Muda, 2020; Shen et al., 2020; F. Zhou et al., 2022) indicate that companies reporting consecutive years of negative profits are at a significantly higher risk of financial distress.

F. Zhou et al., (2022) highlight that many regulators and stock exchanges use consecutive negative profits as a criterion for identifying companies at risk of financial distress. This criterion is often the basis for imposing special status or treatment on affected firms. For instance, in certain jurisdictions, companies that incur losses for two consecutive years may be categorized under a "Special

Treatment" (ST) status, reflecting their precarious financial position and signaling the need for regulatory attention.

Investment Policy uses the Investment Opportunity Set (IOS) proxy measured through CAPBVA referring to research from Nanda *et al*. (2018) which is formulated as follows :

$$\frac{Book\ Value\ of\ Fixed\ Assets\ Year\ t - Book\ Value\ of\ Fixed\ Assets\ Year\ t-1}{Total\ Assets} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(1)$$

Funding Policy using leverage proxy calculated through Total Debt to Asset Ratio (DAR) value referring to research Syuhada & Muda (2020) which is formulated as follows :

$$\text{DAR} : \frac{\text{Total Liabilities}}{\text{Total Assets}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(2)$$

Operational Policy using the Total Asset Turn Over (TATO) proxy which refers to research Syuhada & Muda (2020) yang dirumuskan sebagai berikut:

$$\text{TATO} : \frac{\text{Sales}}{\text{Total Assets}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(3)$$

Good corporate governance calculated using the company's internal control mechanism referring to research Wahidahwati (2012) which includes 4 dimensions, namely Investor, Audit Committee, Management, and Board of Commissioners, producing a final GCG value with the following formula :

$$GCG = \frac{Total\ Score\ Obtained}{Total\ Score\ Expected}\ x\ 100\% \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(4)$$

The population of this study is secondary data from manufacturing companies listed on the IDX or Indonesian Stock Exchange (IDX) throughout the period 2018 - 2022. The data was obtained through www.idx.id as the official website of IDX or IDX. The purposive sampling method was used to determine the sample with the following criteria :

Table 1. Research Sampling Process

Description	Total Company
Companies listed on the IDX are engaged in the manufacturing sector 2018 – 2022	195
Delisted companies	(8)
Sample companies	187
Amount of research data (5 years of observation)	935

Source: Research Data, 2024

RESULTS AND DISCUSSION

The following is a descriptive statistical analysis presented in the table 2

Table 2. Descriptive Statistics Results

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
IOS	935	-5.4993	0.5933	0.0010	0.2011
LEV	935	0.0002	5.1677	0.5490	0.5278
TATO	935	0.0000	6.9494	0.9259	0.6991
GCG	935	0.2632	0.6211	0.3986	0.0620
Valid N (listwise)	935				

Source: Research Data, 2024

Table 2 presents descriptive statistics for the variables used in the study, providing insights into their distribution and variability. The average value of the investment policy (IOS), proxied by CAPBVA, is 0.0010. Among the observations,

478 data points (51.12%) reflect a positive fixed asset difference, indicating firms engaged in investment activities. In contrast, 457 data points (48.88%) show a negative fixed asset difference, suggesting firms not in an active investment condition. The standard deviation of IOS is 0.2011, which exceeds the mean, indicating significant variability in the data.

The funding policy, represented by LEV, has an average value of 0.5490. This suggests that most firms have a debt level smaller than their total assets. The standard deviation of LEV is 0.5278, which is lower than the mean, reflecting less variability in the dataset.

The operational policy, proxied by TATO, has an average value of 0.9259, indicating that the sales of most companies are relatively low compared to their asset base. The standard deviation of TATO is 0.6991, also lower than the mean, which implies limited variability in the data.

Good corporate governance (GCG), the moderating variable, has an average value of 0.3986. This indicates that, on average, firms do not achieve the maximum possible value across all components of GCG measurement. The standard deviation for GCG is 0.0620, lower than the mean, suggesting that the data is relatively homogeneous.

Table 3. Regression Model Feasibility Test Results

Step	Chi-square	df	Sig.
1	15.386	8	0.104

Source: Research Data, 2024

Table 3 presents the Sig value or probability of 0.104 which is greater when compared to the significance level of 0.05. This means that the regression model has met the model feasibility requirements.

Table 4. Overall Model Fit Results

Nilai -2log-likelihood Model 2			
Iteration History[a,b,c]			
Iteration		-2 Log likelihood	Coefficients Constant
Step 0	1	854.485	-1.325
	2	844.508	-1.573
	3	844.451	-1.594
	4	844.451	-1.594

Source: Research Data, 2024

Table 5 Menguji Model Fit 2

Iteration	-2 Log likelihood	Coefficients Constant	IOS	LEV	TATO	GCG	IOS_GCG	LEV_GCG	TATO_GCG
1	800.989	1.178	-0.016	-0.819	-1.167	-5.871	0.040	2.597	1.989
2	759.450	3.148	-0.031	-1.313	-2.955	-10.816	0.079	4.165	5.206
3	754.302	3.599	-0.065	-1.472	-3.593	-11.649	0.178	4.669	6.025
4	749.968	3.635	-0.462	-1.480	-3.726	-11.642	1.334	4.698	6.165
5	748.678	3.594	-0.645	-1.430	-3.720	-11.536	1.867	4.582	6.137
6	708.059	0.379	-0.733	2.971	-2.790	-4.143	2.122	-5.582	4.020
7	702.053	-0.764	-0.756	5.849	-3.438	-1.264	2.189	-12.728	5.521
8	701.765	-1.076	-0.748	6.650	-3.600	-0.476	2.166	-14.708	5.879
9	701.764	-1.093	-0.748	6.694	-3.609	-0.433	2.165	-14.817	5.898
10	701.764	-1.093	-0.748	6.694	-3.609	-0.433	2.165	-14.817	5.898

Source: Research Data, 2024

Table 4 shows the statistical value of -2log-likelihood in the fourth iteration is 844.451 while in Table 5 the statistical value of -2log-likelihood in the tenth iteration is 701.764. The statistical value of -2log-likelihood is the value for the logistic regression model involving independent variables. The statistical value of -2loglikelihood in the logistic regression model using independent variables is smaller than the model that does not involve independent variables, so the logistic regression model involving independent variables, namely IOS, LEV, TATO, and GCG is better in terms of matching the data.

Table 6. Results of Determination Coefficient Test (Uji Nagelkerke R-Square)

Model Summary			
Step	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	701.764[a]	0.257	0.362

Source: Research Data, 2024

Table 6 presents the statistical value of Nagelkerke R-Square which is 0.362. This value describes IOS, LEV, TATO, and GCG in influencing FD, which is 36.2% while the rest, which is 63.8%, is explained by other variables or factors that are not included in this study.

Table 7. Simultaneous Test Results (Omnibus Test of Model Coefficients)

		Chi-square	df	Sig.
Step 1	Step	142.687	7	.000
	Block	142.687	7	.000
	Model	142.687	7	.000

Source: Research Data, 2024

Table 7 presents data that the probability value is 0.000, smaller than the significance level of 0.05, meaning that it can be stated that IOS, LEV, TATO, and GCG together or simultaneously has an effect on financial distress significantly.

Table 8. Results of Multiple Linear Regression Analysis Moderation

		B	S.E.	Wald	df	Sig.	Exp(B)
Step 1[a]	IOS	-0.748	0.861	0.755	1	0.385	0.473
	LEV	6.694	1.722	15.120	1	0.000	807.621
	TATO	-3.609	1.236	8.521	1	0.004	0.027
	GCG	-0.433	3.624	0.014	1	0.905	0.648
	IOS_GCG	2.165	2.497	0.752	1	0.386	8.717
	LEV_GCG	-14.817	4.462	11.027	1	0.001	0.000
	TATO_GCG	5.898	3.274	3.246	1	0.072	364.451
	Constant	-1.093	1.354	0.651	1	0.420	0.335

a. Variable(s) entered on step 1: IOS, LEV, TATO, GCG, IOS_GCG, LEV_GCG, TATO_GCG.

Source: Research Data, 2024

Based on Table 8, the results of the multiple linear regression equation are as follows:

Y = –1,093 – 0,748 IOS + 6,694 LEV – 3,609 TATO – 0,433 GCG + 2,165 IOS*GCG –14,817 LEV * GCG + 5,898 TATO * GCG + e……(1)

The regression results for the moderating variable, good corporate governance (GCG), reveal a coefficient of -0.433. This indicates that as the GCG value increases, the financial distress value decreases, assuming other variables remain constant. The regression coefficient for the interaction term IOSGCG is 2.165, suggesting that a higher GCG value moderating IOS leads to an increase in

financial distress under similar assumptions. For the interaction term LEVGCG, the coefficient is -14.817, demonstrating that an increase in GCG moderating leverage reduces financial distress. Lastly, the TATO*GCG regression coefficient of 5.898 indicates that higher GCG moderating TATO increases financial distress, assuming other variables are constant.

The hypothesis test for the investment policy (H1) yields a regression coefficient (B) of -0.748 with a significance level of 0.385 (>0.05), indicating that H1 is not supported. This suggests that investment policy does not significantly affect financial distress. This finding contradicts agency theory, which posits that management optimizes firm value to align with shareholder interests. A notable observation is the prevalence of negative CAPBVA values in the sample, signifying a decline in firm assets. However, despite reduced asset values, firms can sustain operational activities through alternative funding sources, mitigating the likelihood of financial distress. This outcome diverges from previous studies, such as Nanda *et al*. (2018), which identified a negative relationship between investment opportunity sets and financial distress.

The investment policy in this study, proxied by CAPBVA, compares fixed asset growth to total assets. The findings suggest that fluctuations in asset values are not a significant determinant of financial distress. Even with declining asset values, companies appear to leverage alternative funding mechanisms to maintain operations, reducing their vulnerability to financial distress.

The second hypothesis (H2) tests the relationship between leverage and financial distress. The regression coefficient (B) is 6.694 with a significance level of 0.000 (<0.05), supporting H2. These results indicate that funding policy, represented by leverage, has a positive effect on financial distress. Agency theory highlights the complexity of managing funding policies due to differing interests among stakeholders, which can lead to agency conflicts and additional costs (Paryanti & Mahardhika, 2020). Higher debt ratios increase the likelihood of financial distress, as excessive reliance on debt to finance operations elevates financial risk. These findings align with prior research by Pane et al., (2023), Rissi & Herman (2021) and Mahaningrum & Merkusiwati (2020), which also observed a positive relationship between leverage and financial distress.

The third hypothesis (H3) examines the effect of operating policy on financial distress. The regression coefficient (B) is -3.609, with a significance level of 0.004 (<0.05), supporting H3. This suggests that operational policies, proxied by total asset turnover (TATO), negatively impact financial distress. According to agency theory, conflicts between principals and agents incentivize agents to optimize performance to align with principal expectations. Effective asset utilization reflects optimal performance, reducing the likelihood of financial distress. These findings are consistent with studies by Anita Putri et al., (2022), Oktariyani (2019) and Safa & Nuswandari (2022), which established a negative relationship between TATO and financial distress.

The fourth hypothesis (H4) explores whether GCG strengthens the influence of IOS on financial distress. The regression coefficient (B) for the interaction term IOS*GCG is 2.165, with a significance level of 0.386 (>0.05), leading to the rejection of H4. These results indicate that GCG does not effectively moderate the relationship between investment policy and financial distress. This

outcome diverges from agency theory, which suggests that effective corporate governance ensures management decisions prioritize stakeholder interests with integrity. The findings reveal that many manufacturing companies in the sample exhibit negative IOS values, reflecting a lack of active investment opportunities. Consequently, the role of GCG in mitigating financial distress through investment policy remains limited (Sopiani et al., 2020).

The less-than-optimal implementation of GCG contributes to inadequate financial oversight, particularly concerning investment policies. The absence of significant investment opportunities, as evidenced by negative IOS values, further diminishes the moderating role of GCG in this context. These results highlight the need for stronger governance mechanisms to enhance the supervision of corporate investments and minimize financial distress risks.

Management's inability to maximize the value of the firm's assets contributes to a low IOS value, indicating that the firm is underdeveloped and unable to instill investor confidence in its ability to enhance shareholder welfare. This deficiency increases the likelihood of financial distress. These findings diverge from those of Yuliani & Rahmatiasari (2021) and Al-Gamrh et al., (2020), who assert that good corporate governance (GCG) strengthens the relationship between investment policy (IOS) and financial distress.

The regression coefficient *B* for the moderating effect of LEV and GCG is -14.817, indicating a negative direction and a significance level of 0.001 (<0.05). This supports the fifth hypothesis (H5), implying that GCG effectively reduces the impact of funding policies on financial distress. This result aligns with agency theory, which posits that audit committees play a critical role in minimizing residual loss, bonding costs, and monitoring costs within firms. By overseeing management alongside the board of commissioners and independent board members, the audit committee mitigates conflicts of interest between management and shareholders. As Rahardjo & Wuryani (2021) emphasize, shareholders' authority to oversee management—particularly in funding policy decisions—ensures alignment with the firm's vision and mission.

GCG's role in mitigating the adverse effects of leverage on financial distress highlights its ability to balance obligations and income generation, positively impacting financial health. According to Tron et al., (2023), GCG implementation supports income growth, improving the firm's financial condition. Competent management is essential to applying GCG principles effectively, thereby minimizing financial distress caused by unmet debt obligations. These findings align with the research of Sakinah (2018) and M. Zhou et al (2021), which demonstrate that GCG moderates the relationship between funding policy (LEV) and financial distress.

The regression coefficient *B* for the interaction between TATO and GCG is 5.898, with a significance level of 0.072 (>0.05), leading to the rejection of the sixth hypothesis (H6). This suggests that GCG does not strengthen the influence of operating policies on financial distress. These findings contradict agency theory, which posits that proper and rigorous monitoring can prevent conflicts of interest between agents and shareholders. In this case, management's failure to effectively utilize assets and minimize operational costs prevents high total asset turnover (TATO) from translating into significant profits.

The implementation of GCG within firms can involve effective performance monitoring by the board of directors and audit committee. Larger boards are associated with reduced financial distress risks, as their diversity in expertise and interests contributes to more informed and balanced decision-making. Additionally, a more independent board positively impacts financial stability, as independent directors, who are not directly linked to management, provide objective oversight and enhance accountability (Truong, 2022).

The relationship between total asset turnover and financial distress is multifaceted, influenced by both internal and external factors. The practice of GCG in moderating this relationship extends beyond financial aspects to include ethics, transparency, and accountability. These findings contrast with Putri & Wulandari (2021), who concluded that GCG strengthens the influence of operational policies (TATO) on financial distress. The complexity of these dynamics underscores the need for further research to explore the broader implications of GCG in mitigating financial distress through operational policies.

CONCLUSION

Based on the findings and discussion, this study concludes that financial distress is influenced by funding policies and operating policies, while investment policies do not have a significant impact. The optimal implementation of good corporate governance (GCG) ensures stable corporate performance and mitigates risks, particularly those related to debt, thereby reducing the likelihood of financial distress. However, in the sample of manufacturing firms analyzed, the application of GCG remains suboptimal. This is evidenced by the inability of management to effectively utilize fixed assets and develop robust sales strategies, which adversely impacts profitability and increases the risk of financial distress.

This study is subject to several limitations. The sample consists exclusively of manufacturing firms, totaling 187 companies, which limits the generalizability of the findings to all firms listed on the Indonesia Stock Exchange (IDX), particularly those in other sectors. Additionally, the independent variables examined are restricted to investment policy (IOS), funding policy (LEV), and operating policy (TATO). Other potential factors contributing to financial distress remain unexplored.

It is recommended that firms prioritize the optimal implementation of GCG to minimize financial distress risk. Future research should consider incorporating additional independent variables to provide a more comprehensive analysis of the factors influencing financial distress. This study explains only 36.2% of the variance in financial distress, suggesting the need for further exploration of other determinants. Researchers are also encouraged to include control variables, such as firm size, to better capture the effects of independent variables. Expanding the sample to include firms from various sectors could yield insights into sector-specific differences in the determinants of financial distress.

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