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Submission date: 11-Jan-2021 10:12AM (UTC+0700)

Submission ID: 1485505274

File name: 1987-Article_Text-3911-1-10-20201206.pdf (746.12K)

Word count: 5547

Character count: 31162

PalArch's Journal of Archaeology of Egypt / Egyptology

THE IMPLEMENTATION OF CORPORATE GOVERNANCE AND ENTERPRISE RISK MANAGEMENT: EVIDENCE IN CONCENTRATED OWNERSHIP CONTEXT

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Abid Djazuli, Citrawati Jatiningrum, Fauzi, Mujiyati -- The Implementation of Corporate Governance and Enterprise Risk Management: Evidence in Concentrated Ownership Context -- Palarch's Journal Of Archaeology Of Egypt/Egyptology 17(6). ISSN 1567-214x

Keywords: Corporate Governance, Enterprise Risk Management (ERM), Concentrated Ownership

Abstract

Good Corporate Governance (GCG) has not been able to solve agency problems in several countries which have a majority of concentrated ownership. Enterprise risk management (ERM) is one of the most popular strategies to mitigate the risks in a firm. This study aims to examine the relationship between CG and ERM in the context of concentrated ownership. The sample study obtained 115 observation banks who listed in Indonesia Stock Exchange, which have concentrated ownership. The resulting study using multiple linear regression statistics methods reveal that Independent Commissioners, Auditor Reputation, Audit Committee, Concentrated Ownership, and leverage have a significant relationship to ERM. While the size of the board of commissioners, the presence of RMC and firm size showed no significance. These results provide evidence that companies with concentrated ownership have a higher level of risk management disclosure. The greater the level of concentration of ownership in the company, the stronger the demand for identifying risks that may be faced, such as financial, operational, reputation, regulatory, and information risk. Thus, the regulator needs to improve the policy related to the implementation of GCG and RMC.

1. INTRODUCTION

The issue of corporate governance remains a growing discussion. Implementation of Corporate Governance among Asia countries, there is a need for more studies on the weakness of corporate governance implementation. Several studies indicated that many corporations in Asian countries majority are concentrated, which owned and controlled by families. Indonesian companies have concentrated ownership characteristics with poor and the low implementation of Corporate Governance among Asia countries [1] [2][3][4]. Countries that have weak corporate governance systems, especially in Asian countries, would like to be studied additional deeply. Corporate Governance has a sturdy relationship with the agency problem [5][6]. The main agency conflict arises because of the separation between principal and agent [7]. Based on the agency problems in the relationship between the principal as the owners of the company and the agent as managers the owner is difficulty in ensuring that the invested funds are not taken over or invested in projects that are not profitable, so they do not bring returns. Corporate governance is needed to reduce agency problems between principal and managers as the agent. However, the implementation of Good Corporate Governance (GCG) has not been able to solve the existing agency problems. The presence of Good Corporate Governance (GCG) is only used to raise the image of some companies by doing everything without thinking about the survival of the company. The failure of discussion in the implementation of Good Corporate Governance (GCG) in the Sarbanes Oxley Act further emphasizes the importance of implementing risk management within the company to prevent fraudulent financial operations. Enterprise risk management (ERM) according to COSO is a process that is influenced by management, board of directors, and other personnel of an organization, applied in strategy settings, and covers the organization as a whole, designed to identify potential events that affect organization, managing risk in the tolerance of an organization, to provide reasonable guarantees related to achieving organizational goals [8][9].

Many previous studies have examined the relationship between Corporate Governance and ERM. Several extensive reviews of past works of literature revealed that there is still conflicting findings with regard to the relationship between corporate governance and ERM, where [10] show that independent commissioners, board size, auditor reputation, complexity, financial reporting risk, leverage do not affect the existence of the risk management committee. In line with [11] stated that the size of the board of commissioners proxied by the number of board of commissioners in the company and the leverage proxied by using Debt to Asset Ratio (DAR) does not affect enterprise risk management disclosure. However, [12] gives the different result which conducted a study of the effect of corporate governance and ownership concentration on ERM disclosures. The results showed that the existence of RMC, auditor reputation, and ownership concentration affected ERM disclosure, while the independent commissioners and board of commisioners size did not affect ERM disclosures. Consistent findings with,

[13] there is a significant effect firm size, existence RMC, auditor reputation, and leverage on ERM. However, independent commissioners have no significant effect on ERM. The research of [14] also shows that the size of the board of commissioners and firm size has a significant effect on the enterprise risk management, while the risk management committee (RMC) does not affect the implementation of enterprise risk management.

According to the discussion above related with the mix findings in previous studies, this study aims to examine several of CG mechanism (board size, independent commissioner, audit committee, presence of RMC, auditor reputation) on the relationship between ERM. Therefore, this research examines companies with concentrated ownership context. The reason is that the higher the concentration level of ownership, the stronger the demand for identifying risks had may be faced, and effect to the implementation of ERM [15]. It also, such as financial, operational, reputation, regulatory, and information risks. The different research context, because in Asian countries that have very concentrated ownership and low implementation of Corporate Governance [2][4]. Therefore, [12] and [15] also give empirical evidence in ownership concentrated context. Ownership concentration affects the disclosure of Enterprise Risk Management (ERM). Also, this study is consistent with research conducted by Desender (2007) found that in companies with concentrated ownership, majority shareholders have a strong preference for controlling management, reducing agency costs, and increasing the supervisory role of the companies in which they invest.

2. LITERATURE REVIEW

Enterprise risk management (ERM) according to COSO is a process that is influenced by management, board of directors, and other personnel of an organization, applied in strategy settings, and covers the organization as a whole, designed to identify potential events that affect organization, managing risk in the tolerance of an organization, to provide reasonable guarantees related to achieving organizational goals [8][15]. ERM has been well implemented and developed in larger organizations such as banking, insurance, infrastructure, and resources. This is because large companies already have a historical link to asset risk management and actuarial research. Whereas for other industries, the implementation of ERM is still in the earliest stages of development. [16].

Board of Commissioners size originating from outside the Issuer or Public Company and fulfilling the requirements as an Independent Commissioner (OJK Regulation No.33, 2014). The existence of independent commissioners is intended to create a more objective and independent climate, and also to maintain "fairness" and be able to provide a balance between the interests of majority shareholders and the protection of the interests of minority shareholders, even the interests of other stakeholders (PBI No. 8/4 / PBI /

2006) [17]. In line with [11] documented that the size of the board of commisioners affects the implementation of ERM.

H1: Board of Commissioners size has a positive effect on ERM in concentrated ownership context

- *Independent Commissioners*

The proportion of independent members of the board of commissioners is said to be an indicator of the independence of the board. The presence of independent commissioners can improve the quality of supervision because it is not affiliated with the company so that it is free in decision making. This theory referred to the monitoring effect theory [18][13]. Independent commissioners are responsible for carrying out the supervisory function which can be assisted by the form the committees, including the remuneration committee, audit committee, nomination committee, and risk management committee. Companies with a high proportion of independent directors tend to pay more attention to risk and view the formation of the Risk Management Committee as an essential resource in helping them face the responsibility of overseeing risk management compared to companies with a low proportion of independent directors [10].

H2: Independent Commissioners has a positive effect on ERM in concentrated ownership context

- *Existence of the Risk Management Committee (RMC)*

According to signal theory, a company establishes a Risk Management Committee as its commitment to good corporate governance practices and in the hope of increasing the reputation and value of the company. Consequently, if the company forms a Risk Management Committee, the disclosure of Enterprise Risk Management will be even more extensive [13]. The government, through the regulation of BI No. 8/4 / PBI / 2006 concerning good corporate governance for Commercial Banks, only requires banks to form RMC as a risk supervisory committee. Apart from the tightly regulated banking industry, the formation of RMC in other industrial sectors in Indonesia is still voluntary.

H3: Existence of Risk Management Committee (RMC) has a positive effect on ERM in concentrated ownership context

- *Auditor Reputation*

Big Four auditors had an auditor reputation label that has reliable for audit quality. Big Four auditors as having an expertise that may be more helpful in assisting companies in implementing Enterprise Risk Management [19]. A

company that uses Big Four auditors will pressure for more extensive ERM disclosure. There is higher pressure on companies audited by the Big Four to implement and disclose ERM, and previous studies have found the influence of the Big Four as an external auditor with ERM adoption rates [19][12].

H4: Auditor Reputation has a positive effect on ERM in concentrated ownership context

- *Audit Committee*

Audit committees within the company will increase the effectiveness of the tasks carried out by internal audits and assist in the implementation of ERM in the development of policies and procedures as well as strategies implemented in follow-up audit actions [20]

H5: Audit Committee has a positive effect on ERM in concentrated ownership context

- *Concentrated Ownership*

The higher the concentration level of ownership, the stronger the demand for identifying risks that may be faced, such as financial, operational, reputation, regulatory, and information risks. Some previous studies were finding an effect between business risk and ownership concentration [12][15]. In line with [21] study, states that in companies with concentrated ownership, majority shareholders have a strong preference for controlling management, reducing agency costs, and increasing the supervisory role of the companies where they invest.

H6: Concentrated Ownership has a positive effect on ERM in concentrated ownership context

- *Firm Size*

Companies with large sizes generally tend to adopt Corporate Governance better than small companies. This statement related to the company's responsibility to stakeholders because of the broader basis of ownership. Also, the larger the company, the higher the risk it must face, including finance, operations, reputation, regulations, and information risk (KPMG, 2001). Consequently, large-sized companies will have intense demands to disclose ERM aimed at public transparency and identification of various risks that may be faced. This statement also supported by the results of the previous study by [22]. [13] and [17] which state that the size of the company has a positive effect on RMC

H7: Firm size has a positive effect on ERM in concentrated ownership context

- *Leverage*

Leverage is a ratio to measure how far a company uses its debt as investment financing. Higher the amount of debt used to finance investment is higher the company's dependence on creditors. Companies with high debt levels tend to be more speculative and risky. So that debt has higher power over the financial structure of the company. Research by [23] and [13] states that leverage influences ERM adoption. According to this research, the greater leverage tends to indicate that a company is more dependent on debt to pay its obligations so that the company faces a higher risk.

H8: Leverage has a positive effect on ERM in concentrated ownership context

3. RESEARCH METHOD

The data used in this study is secondary data obtained from Indonesia Stock Exchanges (IDX) through www.idx.co.id, which consists of audited financial statements and annual reports. The research population is all banking companies that have majority shareholders or ownership concentrated. The ownership concentrated company is shareholding of more than 50% [2][15]. The research sample is banking not owned by the government or interference from the government period of 2013 – 2017 (5 years of observation). Sampling method using purposive sampling.

3.1 Variables and Definition Variables

- Dependent variable

Dependent variables in this study are the disclosure of Enterprise Risk Management (ERM). Based on the COSO ERM Framework, Enterprise Risk Management Disclosure (ERM) is a disclosure of risks that have been managed by the company or disclosure of the company's efforts to control risk, consisting of 8 items, namely (1) internal environment, (2) goal setting, (3) identification of events, (4) risk assessment, (5) response to risk, (6) monitoring activities, (7) information and communication, and (8) monitoring [9][24]. ERM measured by ERM Disclosure Index, which is using the dichotomy approach. Each ERM item that disclosed is given a value of 1, and a value of 0 if not disclosed. Each item would be summed to obtain the ERM index of each company. Information about ERM disclosures obtained from annual reports and company sites. Enterprise Risk Management Disclosure Index (ERM) formulated as follows:

$$ERM = \frac{\text{The total number of items disclosed}}{108}$$

- Independent Variables

1.The Board of Commissioners size (BCOMSIZE)

The board of commissioners has a role in overseeing the implementation of fund risk management to ensure the company has an effective risk management program [12]. A large number of board of commissioners increases the

opportunity to exchange information and expertise to improve the quality of ERM [19][14]. The size of the board of commissioners measured by the total number of board members [11][14]

2. Independent Commissioner (INCOM))
The proportion of independent members of the board of commissioners is said to be an indicator of the independence of the board. The presence of independent commissioners can improve the quality of supervision because it is not affiliated with the company so that it is free in taking decisions. In this study, the independence of the board of commissioners was measured using the ratio of the number of independent commissioners to the total number of board members [11]

3. Existence of RMC (FIRMRMC)
This study RMC is measured using a dummy variable, i.e., if the company has a separate RMC from the risk monitor, it is rated 1, and vice versa is given a value of 0 if a risk monitoring committee joins the RMC. [13] [14]

4. Auditor Reputation (AUDREP)
The auditor's reputation is indicated by whether a company uses the Public Accounting Firm (KAP) as its external auditor who is a member of the Big Four KAP, which is an international KAP group. Auditor's reputation is measured using a dummy variable that is if the company uses a Big Four KAP given a value of 1 and vice versa has given a value of 0[13[17].

5. Audit committee (AUCOMTE)
An audit committee is several members of the company's board of directors whose responsibilities include helping the auditor remain independent. This research audit committee measured by the number of Audit Committees in the company [17].

6. The Concentrated Ownership (OWNCO), which is the majority of shareholding with more than 50% share ownership where this shareholding does not include companies whose majority ownership is owned by the government [15][25]

- Control Variables:

1. Firm Size. In this study, the firm size measured as the *natural logarithm* of the total asset of the firm at the end of the fiscal years. Firm Size = Ln Total of Asset [11][13]
2. Leverage is measured using the ratio of total debt to total assets. The company's financial leverage in this study measured by the following Leverage = (Total Liabilities) / (Total Assets) [13]

3.2 Analysis Method

This study uses classical assumptions to obtain the validity of multiple regression analysis. The classic assumption consists of several things, including the assumption of normality, the assumption that there are no symptoms of multicollinearity and autocorrelation, and the assumptions of homoscedasticity. If multiple linear regression satisfies some of these assumptions, it is a fit regression. Multiple linear regression is to examine the effect of two or more independent variables on one dependent variable [25]. The independent variables in this study are corporate governance mechanisms and concentration of ownership, while the dependent variable is enterprise risk management disclosure.

The regression models used in this study are as follows:

ERM = α + β1 COMSIZE + β2 INDCOM + β3 FIRMRMC + β4 AUDREP + β5 AUCOMTE + β6 OWNCO e ... ……………………………… (1)

Where:

α	= constant
β1-β5	= Regression Coefficient
ERM	= Enterprise Risk Management
COMSIZE	= Board of Commissioners Size
INCOM	= Independent Commissioner
FIRMRMC	= Existence of Risk Management Committee
AUCOMTE	= Audit Commitee
AUDREP	= Auditor Reputation
OWNCO	= Concentrated Ownership
e	= Error term, namely the level of error in the study

Multiple linear regression test is done using significance level 0.05. Hypothesis testing of multiple linear regression coefficients simultaneously carried out t-test at 95% confidence level and error rate in the analysis (α) = 5% [25].

CORPORATE GOVERNANCE

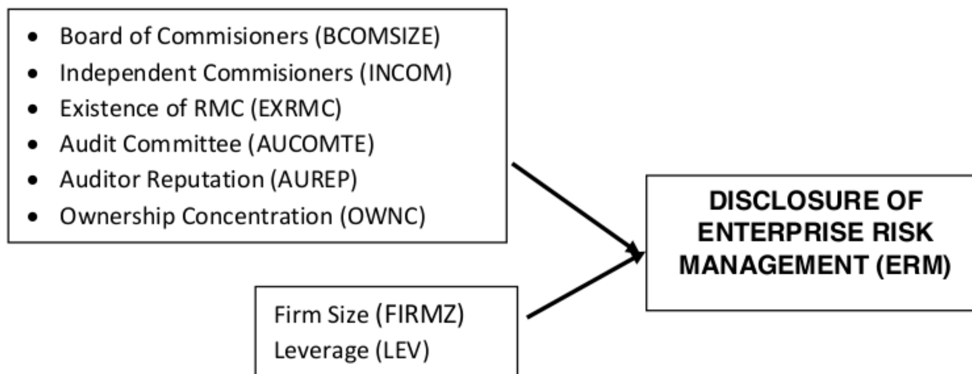

Figure 1.1 Research Framework

4. Findings and Discussion

Based on the criteria sampling, after sample selection procedure, 115 observations were obtained. After compiling data for all variables required, obtained 23 banks as sample study. Have complete. Thus, accordingly, five years of observation, there are 115 companies used to analyze.

Table 4.1 Descriptive Statistics

	N	Min	Max	Mean	Std. Dev.
ERM	115	76.	98	65.38	1.52
COMSIZE	115	2.00	8.00	4.66	2.08
INCOM	115	0.33	0.66	0.38	0.09
OWNC	115	50.04	80.20	58.32	6.53
FIRMRMC	115	0.00	1.00	1.02	0.03
AUCOMTE	115	3.00	5.00	3.05	0.33
AUDREP	115	0.00	1.00	1.04	0.19
FIRMZ	115	6.54	11.05	9.28	0.97
LEV	115	0.36	0.86	0.45	0.23
Valid N (listwise)	**115**				

Table 4.1 displays the descriptive statistics of the sample study. In this section, descriptive statistics of the study variable are shows the minimum, maximum, mean, standard deviation per variable. It shown that the nine variables; the maximum data is 80.20 for ownership concentration (OWNCO). The minimum data 0,00 for FIRMRMC and AUDREP because the data are dummy variable.

The results of the normality test using *Kolmogorov Smirnov* showed that Kolmogorov-Smirnov-Z was 0.741. This result shows that 0.741 is higher than 0.05; it means that the data in this study are normally distributed. Based on multicollinearity test shows that Independent Commissioners, Board of Commissioners Size, RMC Existence, Auditor Reputation, and Audit Committee, Ownership Concentrated, Firm Size, Leverage variables have tolerance values of more than 0.10 (10%) which means that the correlation between the independent variables is less than 95% and results from the calculation of variant inflation factor (VIF) indicates that having a VIF is less than 10, if the tolerance value is more than 0.10 or 10%, and the VIF value is less than 10, then there is no correlation between the independent variables or multicollinearity. The results of heteroscedasticity testing with plot graphs method shows that there is no clear pattern or test the data is spread, the spread points are above and below the number 0 on the Y-axis. Therefore, it concluded that the results of this study did not occur heteroscedasticity. The results of the autocorrelation test using the Durbin Watson (DW) value of 1,

985, this shows that is between the values of 1.833 - 2.167, which means that the Durbin Watson value has no autocorrelation or no autocorrelation occurs. Because the Durbin Watson value is 1.985, it concluded that in this study, there was no autocorrelation or autocorrelation did not occur.

Table 4.2 Coefficient (R^2)
Relationship Corporate Governance, Concentrated Ownership, and ERM

Model Summary

Model	R	R Square	Adjusted R Square	Std. The error of the Estimate
1	0.615[a]	0.572	**0.554**	0.3695

a. Dependent Variable: ERM

Based on table 4.2 showed that the adjusted R square value obtained at 0.554 which means that 55.4% of Enterprise Risk Management (ERM) disclosure influenced by Corporate Governance and Ownership Concentration, and is 44.6% (100% - 55.4%). Other factors influence enterprise disclosure Risk Management (ERM).

Table 4.3 F Significance
Relationship Corporate Governance, Concentrated Ownership, and ERM

ANOVA

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	2.29	8	1.205	12.586	**0.000[a]**
Residual	1.97	107	0.230		
Total	4.26	115			

a. Predictors: (Constant): BCOMSIZE, INCOM, FIRMRMC, OWNC, AUCOMTE, AUDREP, FIRMZ, LEV
b. Dependent Variable: ERM

Based on Table 4.3, it can the that the F calculated value is 12.586, with significant value 0.000. There is an indication that the relationship between corporate governance, ownership concentrated and ERM have high goodness of fit, suggesting the regression equation can use for further testing.

Tabel 4.4
Relationship Corporate Governance, Concentrated Ownership, and ERM

ERM = α +β1 COMSIZE+ β2 INDCOM+ β3 FIRMRMC+ β4 AUDREP+ β5 AUCOMTE+ β6 OWNCO e . (1)

Coefficients[a]

Model		Understand. Coef		Stand. Coef		
		B	Std.Error	Beta	t	Sig.
1	(Constant)	0.023	0.136		0.168	**0.008**
	BCOMSIZE	0.186	0.159	0.157	1.175	**0.151**
	INCOM	0.028	0.011	0.495	2.536	**0.018**
	FIRMRMC	0.007	0.039	0.024	0.178	**0.160**
	AUCOMTE	0.023	0.014	0.288	2.844	**0.002**
	AUDREP	0.065	0.032	0.297	2.720	**0.005**
	OWNC	0.278	0.124	0.310	2.232	**0.035**
	FIRMZ	0.014	0.005	0.011	1.188	**0.215**
	LEV	0.053	0.024	0.233	2.437	**0.004**

a. Predictors: (Constant): BCOMSIZE, INCOM, FIRMRMC, OWNC, AUCOMTE, AUDREP, FIRMZ, LEV

b. Dependent Variable: ERM

Hypothesis testing is tested by the t-test, as described in Table 4.4. Based on the table above shows the findings that Enterprise Risk Management (ERM) disclosure has a significant effect on independent commissioners (0.018), Audit Committee (0.002), Auditor reputation (0.005), Concentrated Ownership (0.035) and leverage (0.004), with p-value <0.05. Meanwhile, the Board of commisioners size (0.151), the existence of RMC (0,160) and firm size (0.215) show that results that have no significant effect on ERM or with p-value> 0.05.

Based on the results of H1 indicate that the size of the Board of Commissioners does not affect the disclosure of Enterprise Risk Management in the concentrated ownership context. The results of this study consistent with a previous study conducted by [12] and [11] where the Board of Commissioners' size did not affect Enterprise Risk Management (ERM) disclosures. This condition due to the ineffectiveness of the functions of the Board of Commissioners. The board of commissioners in several banks in Indonesia is have not competency, and the ability to evaluate and provide policies. Thus the role of the board of commissioners [illegible] inefective.[13] documented that the quality and educational background of members of the board of commissioners determine the quality of the supervisory function of the board. Also, in Indonesia, have variates of board sizes, the data show that the maximum number of boards is eight-person, and the minimum number is two-person, different banking capabilities ad[illegible]st this. Therefore, there is a need the regulation to regulates the number of the board of commissioners in Indonesia.

Based on the results of H2 testing reveal that the independent commissioner has a significant effect on the implementation of ERM in the concentrated ownership context. This research is in line with the research results of [13][15] and [11] They also prove that the independent board of commissioners in banking affects reducing the cost of debt because the independent commissioner is not an employee and is more independent, to improve the quality of supervision and monitoring.

Based on the results of H3 testing stated that the existence of RMC does not affect the disclosure of Enterprise Risk Management in the concentrated ownership context. These results are consistent with research by [12] [14] and [15] Risk Monitoring and the existence of an RMC incorporated from the Risk Monitor are associated with the existence of policies or regulations from the Government of Indonesia that for banking companies are required to establish an RMC. Thus, the existence of RMC, whether separate or not, shows no effect on ERM disclosure. This argument, because the separation function between the Risk management committee and the Risk monitoring committee has not run effectively. Therefore, this separation is only obedience with the existing regulations, and this proven in the results of ERM disclosure, has not been carried out to the maximum, most of the companies are mere disclose the risks set by the government. That is, the awareness of the company about the importance of risk management is still low; they only follow the rules. It means that the internal control function for the banking sector still considered low.

Based on the H4 test, the result stated that the Audit Committee has a significant effect on the implementation of ERM in concentrated ownership context. This result consistent with the statement that Audit committees within the company will increase the effectiveness of the tasks carried out by internal audits and assist in the implementation of ERM in the development of policies and procedures as well as strategies implemented in follow-up audit actions [20].

The results of the H5 test show support for the hypothesis that the Auditor's Reputation has a significant influence on ERM in concentrated ownership context. The results of this study are consistent with previous research conducted by [12] and [15] which stated that there is a significant effect between the existence of the Big Four with the adoption rate of ERM. Possible reasons are that the Big Four usually helps internal auditors evaluate and assess the effectiveness of risk management. This condition because the Big Four is considered to have the expertise to identify risks, thereby increasing the quality of the company's risk assessment and supervision. Also, there is higher pressure on companies audited by the Big Four to implement and disclose ERM. The research concluded that the existence of the Big Four plays an essential role in the management of corporate risk management activities.

According to the results of H6, showed that concentrated ownership has a significant effect on ERM in concentrated ownership or majority stakeholders context. The results of this study are consistent with previous studies conducted by [11] [15] and [19]. Concentrated Ownership affects the disclosure of Enterprise Risk Management (ERM) because companies with concentrated ownership or majority shareholders have a strong preference for controlling management, reducing agency costs, and increasing the supervisory role of the company in which they invest.

The results of H7 indicated that the findings are line with the previous research of [26] The finding also found that firm size has not affected the level of adoption of Enterprise Risk Management in concentrated ownership. Companies with large sizes generally have not tended to adopt Corporate Governance better than small companies. This statement related to the Indonesia companies has a low responsibility to stakeholders which should provide the broader basis of ownership [27]. In the condition of good CG, the larger company, the higher the risk it must face, including finance, operations, reputation, regulations, and information risk.

The result of H8. The finding found that leverage has a significant effect on implementation ERM in concentrated ownership context. This result consistent with the study by [13] [15] and [28], the greater leverage has indicated that a company is more dependent on debt to pay its obligations so that the company faces a higher risk.

5. CONCLUSION

This study aims to examine the application of CG in companies that have a majority shareholding. Companies with concentrated ownership or majority shareholders have a strong preference for controlling management, reducing agency costs, and increasing the supervisory role of the company in which they invest. The findings stated that Independent Commissioners, Auditor Reputation, Audit Committee, Concentrated Ownership, and leverage have a significant relationship to ERM implementation. However, the size of the board of commissioners, the presence of RMC and firm size showed no significance. This finding has a contribution to regulators and companies to improve the effectiveness of GCG implementation. Related to information risk, the regulator needs to improve the policy related to the regulation of the RMC.

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