Influence of corporate governance and profitability to corporate CSR disclosure

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ABSTRACT
Corporate social responsibility (CSR) is a corporate responsibility to environment and stakeholders. Related to this activity, there is a disclosure of CSR activity. For Indonesian corporation, it is regulated by Capital Market Supervisory Agency. There are several things that might have influence to CSR disclosure, such as corporate governance and profitability. We used board independence and institutional ownership to study the relationship of corporate governance to CSR disclosure. For profitability we used return on equity. In measuring CSR disclosure, we develop CSR disclosure index that is based on Global Reporting Initiatives indicators. There are several mixed results for these study. Our research showed board independence and institutional ownership do not have influence to corporate CSR disclosure, while profitability is influential and significant in 1%.

Keywords: CSR, CSR disclosure, board independence, institutional ownership, profitability

1. INTRODUCTION

Corporate social responsibility (CSR) is a corporate responsibility to environment and stakeholders. Since the introduction of triple bottom line concept (Elkington, 1998), many investors consider CSR as one of their investment decision. Parallel with this investor behavior in regards of CSR, corporation also conducting their CSR activity.

CSR activity make a corporation not operate only for a single bottom line concept, where corporation was only operate to increase their value. CSR has both social and economic consequences for corporation. In practice, there are many kind of CSR activities conducted by corporation. Of course this various kind of CSR activities due to difference of business and difference of preferred action by corporation. As for Indonesian corporation, government trough Capital Market Supervisory Agency regulate the importance of CSR disclosure in the financial report. With this regulation, there is an increasing number of Indonesian corporation disclose its CSR activity (Lucyanda and Siagian, 2012).

Research on relation of corporate governance to CSR disclosure in this paper will be focused on institutional ownership and independence of board. Although ownership could be looked from three different perspectives: director ownership, block ownership and institutional ownership (Htay et al., 2012) we will only focusing on institutional ownership. While profitability measurement used in this research is return on equity (ROE).

Several research have been conducted to study the relationship between corporate governance and profitability to CSR disclosure and activity. In regards of relationship between board independence and CSR disclosure, the result is inconclusive. Htay et al. (2012) found the independency of board is influenced CSR disclosure and significant in 5%, while Meryawati (2011) and Lucyanda and Siagian (2012) both found there is no significant relation between board independence and CSR disclosure. In study of institutional ownership and CSR disclosure, Fauzi et al. (2007), Gamerschlag et al. (2011), Meryawati (2011), Htay et al. (2012) and Lucyanda and Siagian (2012) found there is no significant impact of institutional ownership to CSR disclosure. Meanwhile, research by Saleh et al. (2010) found there is a significant relationship in 1% between percentage of institutional ownership to CSR disclosure.

Similar with findings in corporate governance relation to CSR disclosure, mixed result also found in previous study regarding influence of profitability to CSR disclosure and activity. Mallin et al. (1995), Cummings (2000), Meryawati (2011), Htay et al. (2012) and Lucyanda and Siagian (2012) found that profitability is influential to firm CSR disclosure in 1% significancy. While Wagner (2002), Wahba (2008), Mulyadi and Anwar (2011 and 2012) and Hatta (2012) found there is no significant relation between profitability to CSR disclosure and activity.

2. LITERATURE REVIEW AND RESEARCH METHODOLOGY

2.1 CSR disclosure

CSR is one of corporation's responsibility to its stakeholder and also a voluntary contribution by corporation to sustainable development (Crane and Matten, 2007). There are three dimensions of corporate responsibility: economic responsibility, legal responsibility and social responsibility. CSR activity is the third dimension of corporate responsibility, which is beyond legal responsibility.

Corporation can disclose its CSR activity in sustainability reporting, which is a corporate report related to its economic policy, social and environmental, impact and performance of corporation and its products in sustainable development context (Meryawati, 2011). Based on the content of sustainability reporting, CSR disclosure can be defined as the information disclose voluntarily by a corporation regarding its social and environmental impact and its relationship with corporate stakeholder (Campbell, 2004). The growing activity of CSR is reflected from increasing number of sustainability reports (Kolk, 2005).

Many different theories used to explain voluntary disclosure CSR activity of a corporation, one of theories is political cost theory. This theory explain that corporation is concerned with political consideration, such as: preventing taxes and other regulatory actions (Healy and Palepu, 2001). Due to each corporation specific characteristics, corporation face different intensities level of pressures from its stakeholder to disclose such information. We believe that these characteristics will determine the CSR disclosure, and in this research we divide these characteristics by three: independence of board (board and commissioner), ownership of corporation (institutional ownership) and profitability.

2.2 Agency theory

Separation of ownership and control can incur agency cost (Jensen and Meckling, 1976). Implementing a good corporate governance and also information disclosure can reduce this cost (Judge et al., 2003 and Cheung and Chan, 2004). In regards to board size and board independence, smaller size of board and independence from management will resulted in a positive impact on the monitoring function (Huther, 1997). Larger size of board is ineffective and will create ineffective coordination and communication, less cohesive and more difficulties in coordination (Yoshikawa and Phan, 2003).

Ownership and agency theory related to who has control to the management of corporation. In case of director ownership, director as the owner and have a direct control and monitoring to the management. If director has substantial amount of share ownership, director might not want to disclose the information to external parties (Htay et al., 2012). In institutional ownership, institutional investor play an important role in corporate monitoring due to their voting power and their ability to monitor executives (Le et al., 2006 and Ramzi, 2008). According to David and Kochhar (1996) and Lakhal (2005) concluded that there is a positive and significant relationship between institutional investor and CSR disclosure.

2.3 Independency of board

Previous study in corporate governance raised the importance of board independence. Higher proportion of independent non-executive directors/commissioner makes the board independent from management (Choe and Lee, 2003). Board of commissioner is board in charge to supervise the directors, or have equal function as non-executive directors (Lucyanda and Siagian, 2012). The greater number of commissioners will resulted in more effective supervision (Coller and Gregory, 1999).

Gul and Leung (2004), Byard et al. (2006) and Htay et al. (2012) found that higher proportion of independent board has a positive and significant impact to CSR disclosure. Meryawati (2011) and Lucyanda and Siagian (2012) found different result, their result showed there is no significant impact between independency of board to CSR disclosure.

Based on previous research on independency of board and CSR disclosure, we formulate our first hypothesis: “There is a significant influence of board independence to CSR disclosure”.

2.4 Institutional ownership

Institutional investor have incentives to monitor corporate decision making (Shleifer and Vishny, 1986). Institutional investor also increase firm value and reduce agency cost (McConell and Servaes, 1995 and Bhojraj and Sengupta, 2003).

In review of institutional investor’s motives in conducting CSR activity, Cropanzano et al. (2001) divide by three motives: instrumental, relational and morality motives. In instrumental motives, some institutional investor believe that social and environmental issues can be financially material (Aguilera et al., 2006). Therefore, CSR activity will create a competitive advantage which closely related to reputation of corporation and its share price (Clark and Hebb, 2005).

Although primary interest of institutional investor in CSR activity is instrumental motives, evidence also found in relational motives. For example: 11 out of 20 UK largest pension fund managers are members of the UK Social Investment Forum (Williams and Conley, 2005).

The potential conflicts between owner and manager is increase in a corporation with wide-distributed share (Gamerschlag et al., 2011). There is a higher probability of voluntary disclosure in widely held corporation (Fama and Jensen, 1983). Chau and Gray (2002) also pointed out that corporation with big shareholder (institutional investor or family-owned corporation) have little motivation to disclose information as they often have direct access to the management.

In previous study on relationship between institutional ownership and CSR disclosure, Fauzi et al. (2007), Gamerschlag et al. (2011), Meryawati (2011), Htay et al. (2012) and Lucyanda and Siagian (2012) found there is no significant impact of institutional ownership to CSR disclosure. Different with their result, Saleh et al. (2010) found there is a significant relationship in 1% between percentage of institutional ownership to CSR disclosure.

Based on previous research on institutional ownership and CSR disclosure, we formulate our second hypothesis: “There is not a significant influence of institutional ownership to CSR disclosure”.

2.5 Profitability

Corporate profitability is one of corporation's characteristic influencing CSR disclosure (Lucyanda and Siagian, 2012). Profitability is one factor enabling management to disclose CSR activity in high level of flexibility. The higher level of profitability, the greater CSR disclosure as they are interested in explaining trough CSR disclosure how they generate their profitability than less profitable corporation (Gamerschlag et al., 2011 and Hatta and Daryono, 2012).

Mixed result is found in previous study regarding influence of profitability to CSR disclosure and activity. Mallin et al. (1995), Cummings (2000), Meryawati (2011), Htay et al. (2012) and Lucyanda and Siagian (2012) found that profitability is influential to firm CSR disclosure in 1% significancy. While Wagner (2002), Wahba (2008), Mulyadi and Anwar (2011) and Hatta (2012) found there is no significant relation between profitability to CSR disclosure and activity.

Based on previous research on profitability and CSR disclosure, we formulate our third hypothesis: "There is a significant influence of profitability to CSR disclosure".

2.6 Data used and research methodology

2.6.1 Data used

In this research, we used listed corporation in Indonesia Stock Exchange with following criteria: (1) corporation disclosing full data of its good corporate governance policy, (2) corporation publish its annual report and financial report and (3) corporation disclose CSR report in its annual report.

To measure CSR disclosure, we employ CSR disclosure index based on Global Reporting Initiatives (GRI) indicator. GRI has three disclosure focuses: economic performance indicator, environment performance indicator and social performance indicator.

2.6.2 Research methodology

To test our proposed hypothesis, we used following model:

$$CSRDI = \beta 0 + \beta 1\ BI + \beta 2\ IO + \beta 3\ ROE + \varepsilon$$

Where BI is board independence, IO is institutional ownership and ROE is return on equity. IO and BI used to test the influence of corporate governance to corporate CSR disclosure, while ROE is used to test influence of profitability to corporate CSR disclosure.

3. RESULTS AND DISCUSSION

From the processed data, we found that there is only 3% of corporation with less than 30% of independent non-executive directors/commissioners. While the other 97% have more than 30% proportion of independent board. In terms of institutional ownership, 29% corporation have less than 5% of institutional investor and 71% of corporation have more than 5% of institutional ownership. If in corporate governance measurement (both board independence and institutional ownership) showed more corporation with higher independent board and higher institutional ownership, in profitability measurement the data is almost equal. Using 10% ROE as measurement, we found 56% corporation with ROE less than 10% and 44% of corporation have ROE higher than 10%.

The result of hypothesis testing could be found in Table 1. From table 1 it could be found that is only ROE that have positive and significant influence to CSR disclosure (which is significant in 1%), while IO and BI is not influential to CSR disclosure.

Table 1. Hypothesis testing

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	Constant	.460	.159		2.895	.005		
	ROE	.686	.249	.282	2.757	.007	.987	1.013
	IO	.241	.159	.154	1.511	.135	.992	1.009
	BI	.042	.221	.019	.189	.851	.994	1.006

Result on independency of board we found is supporting previous research by Meryawati (2011) and Lucyanda and Siagian (2012). Our result is not in accordance with research by Gul and Leung (2004), Byard et al. (2006) and Htay et al. (2012). Both Meryawati and Lucyanda and Siagian conducting their research by using Indonesian corporation as their research object, while different object used by Gul and Leung, Byard et al., and Htay et al. This result confirmed that in Indonesia corporation, there is no significant influence of board independence to CSR disclosure. Therefore, we reject our first hypothesis.

Result on institutional ownership we found is supporting previous research by Fauzi et al. (2007), Gamerschlag et al. (2011), Meryawati (2011), Htay et al. (2012) and Lucyanda and Siagian (2012) where all of them also reach the same conclusion that there is no significant relationship between institutional ownership and CSR disclosure. Therefore, we do not reject our second hypothesis.

Moreover, both result in corporate governance measurement (board independence and institutional ownership) is also supported our previous research (2011) that Indonesian investor still do not take account of corporate CSR activity as their investment decision. As it is not too influential for their share, board and institutional ownership do not rely heavily in corporate CSR disclosure. Our another previous research (2011) also found an inconsistent finding regarding whether corporate disclosure of Indonesian corporation matter to the investor or not.

In research of influence of profitability to CSR disclosure, we found that profitability is positively impacted corporate CSR disclosure and significant in 1%. This result is similar with what have been found by Mallin et al. (1995), Cummings (2000), Meryawati (2011), Htay et al. (2012) and Lucyanda and Siagian (2012).

4. CONCLUSION

Based on our research, we found that for Indonesian corporation corporate governance do not have a significant influence to CSR disclosure. From two corporate governance measurement we used (board independence and institutional ownership) both showed there is no significant impact to CSR disclosure. While for profitability, we found that profitability is influential to corporate CSR disclosure which is significant in 1%.

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