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Print ISSN: 2288-4637 / Online ISSN 2288-4645 doi:10.13106/jafeb.2021.vol8.no2.0933 The Effect of Corporate Governance on Corporate Social Responsibility Disclosure and Performance Dwi RATMONO1, Dian Essa NUGRAHINI2, Nur CAHYONOWATI3 Received: November 05, 2020 Revised: January 05, 2021 Accepted: January 15, 2021 Abstract This research aims to test the effect of corporate governance factors on corporate social responsibility (CSR) disclosure and its impact on a company's financial performance. The factors of corporate governance referred to in this research are foreign ownership, state ownership, number of board of commissioners, the proportion of independent commissioners, and educational background of commissioners' board. Based on the purposive sampling method, 194 companies were selected with a total of 582 observations. The data analysis used in this study was the Structural Equation Model (SEM) approach by using the alternative Partial Least Square (PLS) method. The results of this research indicated that state ownership, number of board of commissioners, and the proportion of independent commissioners had a significant positive effect on CSR disclosure. While the foreign ownership and the educational background of the commissioners' board have had an insignificant effect on CSR disclosure. Then, CSR disclosure had a significant positive effect on the companies' financial performance. The findings of this study suggest that the positive effect of the CSR disclosure on performance is because the disclosure is able to improve the company's reputation; the more social activities are carried out will improve the customers' loyalty as well as the support from other stakeholders which in turns will improve the company's performance. Keywords: Corporate Governance, CSR Disclosure, Financial Performance JEL Classification Code: M41, M14, L25 1. Introduction Based on the principles of sustainable development, an organization must create decisions not only based on economic or financial factors but also based on long- term social and environmental consequences. The main purpose of a company to gain profit only is increasingly left-behind. On the contrary, the triple bottom line 1First Author and Corresponding Author. Department of Accounting, Faculty of Economics and Business, Universitas Diponegoro, Indonesia [Postal Address: Jl. Prof. Sudarto No.13, Tembalang, Kec. Tembalang, Kota Semarang, Jawa Tengah 50275, Indonesia] Email: dwi.ratmono2@gmail.com 2Faculty of Economics and Business, Universitas Diponegoro, Indonesia. Email: dianessan@gmail.com 3Department of Accounting, Faculty of Economics and Business, Universitas Diponegoro, Indonesia. Email: nurcahyonowati@gmail .com © Copyright: The Author(s) This is an Open Access article distributed under the terms of the Creative Commons Attribution Non-Commercial License (https://creativecommons.org/licenses/by-nc /4.0/) which permits unrestricted non-commercial use, distribution, and reproduction in any medium, provided the original work is properly cited. (profit, planet, and people) concept is increasingly penetrating the mainstream business ethics. The concept states that business is not just looking for profit, but also the welfare of people, and ensuring the survival of the environment (planet). Both theoretical and empirical research that examined the impact of CSR disclosure on the company's financial performance has shown the evidence; however, these results are ambiguous. Research that showed a positive effect of CSR disclosure on the company's financial performance includes Russo and Fouts (1997), Surroca et al. (2010), Tang et al. (2012), DiSegni et al. (2015), Eldomiaty et al. (2016), Famiyeh (2017), and Kabir and Thai (2017). Whereas, a negative effect was found by Lee et al. (2009) and insignificant influence was found by McWilliams and Siegel (2000), Nelling and Webb (2009), and Chtourou and Triki (2017). Meanwhile, the study from Barnet and Salomon (2012) showed a U-Curve pattern. Reviewing empirical studies about CSR disclosure effect and financial performance, Lu et al. (2014) had observed several studies' results which indicated negative effect (6 studies), positive effect (38 studies), insignificant effect (21 studies), and U-curve pattern (18 studies). The positive effect of CSR disclosure on financial performance is found in the samples of companies in developed countries (Wang et al., 2015) and developing countries (Cahan et al., 2015; Ghoul et al., 2016). According to Huang and Watson (2015), the findings of positive effects must be handled carefully because these studies vary on key factors such as period, measurement of CSR disclosure, measurement of financial performance, failure to control variables or other methodological problems. For the Indonesian case, Kurnia et al. (2020) found that firms should implement higher carbon emission disclosure and good corporate governance to increase financial performance and firm value. Endiana et al. (2020) indicated that manufacturing companies in Indonesia are able to implement green accounting by allocating appropriate environmental costs by earmarking a portion to carry corporate sustainability management system (CSMS) implementation to improve financial performance. The result of Saraswati et al. (2020) showed that CSR disclosure was greater in government-owned companies but lower in companies that have politically connected board members. Machmuddah et al. (2020) showed that the disclosure of CSR has a positive and significant effect on firm value, and profitability moderates the effect of CSR disclosure on firm value Most CSR practices in developing countries in Asia come from Western thought, which practices different types of corporate governance, business systems, institutions, and cultures from Asian countries. Besides, many developing countries in Asia face other challenges such as poverty and wealth inequality, education disparities, vulnerability to natural disasters, and so on (Kabir &Thai, 2017). Indonesia is a developing country where many companies have recently developed international trade and manufacturing relations with their counterparts from developed Western countries. Besides, Indonesia is a very attractive country for its unique political and legal environment. Therefore, it is quite interesting to study corporate CSR from developing countries, especially in Indonesia. Different from previous studies, this research measures CSR disclosure in aggregate, that is all aspects of CSR disclosure, which is expected to explain more thoroughly about CSR. The determinants of CSR disclosure have been extensively investigated but still, show inconsistent results. This research aims to study the effect of corporate governance factors on corporate social responsibility (CSR) disclosure and its impact on the company's financial performance. Factors of corporate governance studied in this research are ownership identity (foreign and state ownership) and the characteristics of board of commissioners (number of board of commissioners, board of commissioners' independence, and educational background of board of commissioners). 2. Literature Review and Hypotheses Development The separation of ownership and control in a company creates the agency problem (Jensen & Meckling, 1976). Managers who involve in daily operations have better information than shareholders. Shareholders also do not have the ability to observe the managers directly. This information asymmetry creates problems if the managers' goals are not in accordance with the shareholders' goals. To minimize information asymmetry in the principal-agent relationship, besides corporate governance, companies can use the annual report (company information disclosure). The annual report usually includes financial statements and management reports that contain their achievements and performance in one year. Furthermore, the company can also carry out CSR disclosure. In agency theory, CSR and corporate governance mechanisms are one way to reduce agency conflicts, resulting in reduced agency costs and information asymmetry. It is expected that the better and more transparent CSR disclosures can reduce the agency problems faced by the company. Foreign ownership is usually considered as a better monitoring signal in the developing countries, which could influence both the implementation and the disclosure of CSR activities. Foreign stakeholders are important stakeholders of the company. In line with the agency theory, foreign board members and cross-listing help companies to raise their accountability through increased CSR disclosure. That is, foreign shareholders, increase the disclosure of CSR by reducing information asymmetry. Investing in other countries causes the risk of increasing information asymmetry. It occurs especially if one invests in developing countries where they have a different rule of law. On the contrary, CSR investment could decrease the information asymmetry, because it is a way for a company to differentiate themselves and to provide the signal of trust (Siegel & Vitaliano, 2007). Therefore, investing in a socially responsible company is a way to reduce the risk of foreign investments. Foreign ownership was found to be positively associated with CSR ratings. Foreign investors are also likely to be long-term oriented, given the fact that most of them are institutional investors. Foreign investors will pressure firms to adopt socially responsible practices because of their desire to signal to their clients that these investors are reliable and responsible firms (Oh et al., 2011). Empirical studies suggesting the positive influence of foreign ownership on the disclosure of CSR are Oh et al. (2011), Khan et al. (2013), and Haniffa and Cooke (2005). Therefore, the hypothesis is formulated as follows: H1a: Foreign ownership has a positive effect on the disclosure of CSR. Intervention from the government might produce some pressure on the company to disclose additional information since the government is the trusted board by the public. Eng and Mak (2003) found that the government's ownership is related to increasing self-disclosure. Lower managerial ownership and significant government ownership are associated with increased disclosure. Mohammed and Abdullah (2004) Governments in many emerging markets control critical resources and increasingly play a significant role in setting rules to create norms for the CSR behavior of organizations. The institutional theory views governments as societal institutions with coercive power to regulate the behavior of organizations through laws and regulations. Government shareholders have a strong incentive to push for high social performance since enhancing financial performance might not be their primary objective. Besides, there is a close relationship between the manager, BUMN (State Owned Company), and the government authority. As the owner of BUMN, government tends to provide special rights in allocating the resources to BUMN. Companies in which the directors hold a higher proportion of equity shares (owner-managed companies) disclosed significantly less CSR information, while companies in which the government is a substantial shareholder disclosed significantly more CSR information in their annual reports. The previous working relationship also encourages public officials to deal with BUMN in a better way. BUMN managers tend to have more opportunities to approach and engage with the public officials to obtain the better condition for the growth and the development of the company. To do that, the managers could use CSR disclosure to develop the company's positive image (Kabir & Thai, 2017). Therefore, it is hypothesized as: H1b: The ownership of the government has a positive effect on CSR disclosure. The board of commissionaires plays a role in preventing managers to take opportunistic actions to encourage their personal interests. The board of commissionaires also supports the manager in formulating strategies and their implementation. The members of the board of commissionaires contribute to strategic decision-making by providing access to resources that have become the mainstay of the company (Hillman & Dalziel, 2003). It is expected that the contribution of the board of commissionaires in making strategic decisions also considers the interests of all stakeholders (Tran et al., 2020). The role of the board of commissionaires is not only for the interest of the shareholders but also for other stakeholders. CSR disclosure influences the stakeholder in different ways and it has different objectives. The decision of the bigger board of commissionaire could pay more attention to the demand of the stakeholders than a smaller number of board of commissionaires. With more resources provided for the role of consultation and monitoring, which in this case is the board of commissionaires, it is expected that the CSR could run more effectively and the CSR disclosure could be better. Hence, a hypothesis about the number of board of commissionaires is formulated as follows: H2a: The number of board of commissionaires has a positive effect on CSR disclosure. The independence of the board of commissionaires affects the CSR disclosure through the increasing quality of monitoring (Gardazi et al., 2020). It is mainly because the independent commissionaires (or externals) are not involved in the daily management of the company, it eventually helps them to provide more objective recommendations. They do not have a financial interest in the company (Coffey & Wang, 1998). Compared to the board of directors who usually pay more attention to the short -term objectives of the economy, an independent commissionaire rather has a different incentive, value, and time horizon (Donnelly & Mulcahy, 2008; Post et al., 2011). They tend to take longer-term perspectives and pursue sustainable development. Therefore, it is expected that the independent commissionaires pay more attention to the CSR disclosure and the long-term benefits. H2b: The proportion of independent commissionaire has a positive effect on CSR disclosure. The function of an effective board of commissionaires needs adequately qualified individuals, high intellectual capacity, and sufficient experience. The members of the board with higher qualifications could provide rich innovative sources of ideas to develop policy initiative with deep analysis and thoroughness needed to offer unique perspectives on strategic issues (Singh & Deeksha, 2015). Based on the sustainable development principles, it is understood that an organization must make a decision not only based on the factor of economy or finance but also based on the consequence of the social and sustainable environment. Board of commissionaires with higher educational background, especially in the field of economy and business are highly aware of the importance of sustainable development principles and the importance of implementing the activities of CSR. Those with an educational background in economy and business are also aware of the importance of the disclosure of CSR activities which will create a positive image that encourages the pursuit of achieving good corporate financial performance. With such awareness, the board of commissionaires would encourage the managers or directors to pay more attention to the importance of CSR activities and their disclosure. In the research conducted by Esa and Zahari (2016), it is found that the educational background of the board of commissionaires and the directors have a significant relationship with the disclosure of CSR. Golec (1996) found that managers and CEOs holding an MBA degree are significantly better than those who do not possess such a degree. Therefore, based on this perspective, it is stated a hypothesis that: H2c: Educational background of the board of commis- sionaires has a positive effect on CSR disclosure. For shareholders, CSR disclosure may increase the reputation of the company and its short-term competitiveness (McWilliams & Siegel, 2001) or even in the long term, such as investment in the wealth of the employees and high-quality products (Greening & Turban, 2000; Surroca et al., 2010). The company could also decrease the cost of legal expenses by maintaining the relationship with the government as well as with the community. Increasing corporate reputation by increasing CSR disclosure might create a good relationship and make the company receive better treatment from the government. It is because the government has a motivation to promote the CSR policy to fulfill their social objective. Research that has shown the positive effect of the CSR disclosure towards corporate financial performance include Russo and Fouts (1997), Surroca et al. (2010), Aguinis and Glavas (2012), Tang et al. (2012), Di Segni et al. (2015), Eldomiaty et al. (2016), Famiyeh (2017), and Kabir and Thai (2017). The positive influence of CSR disclosure on the corporate financial performance is found in the sample of the company in developing countries (Wang et al., 2015) and developed countries (Cahan et al., 2015; Ghoul et al., 2016). H3: The disclosure of corporate social responsibility (CSR) has a positive effect on financial performance. 3. Research Method 3.1. Types and Data Collection Methods This research took the non-financial company listed on the Indonesian Stock Exchange (IDX) from 2015 to 2017 as the research objects. The population of the research was 408 companies. The sample in this study was selected using the purposive sampling method. The criteria were companies listed on the IDX and their shares actively traded during 2015–2017 and they issued annual reports during the 2015–2017 periods. The companies should provide complete information needed to measure each variable. 3.2. Research Variables The variables used in this study consisted of endogenous variables and exogenous variables. The endogenous variables in this study were the corporate's financial performance and the disclosure of corporate social responsibility (CSR) while the exogenous variables were factors of corporate governance. This study applied controlled variables such as company size, leverage, and industry type to control the factors that systematically affect the company's financial performance. To measure company performance, this study applied several proxies based on Kabir and Thai (2017), namely return on equity (ROE), return on assets (ROA), return on sales (ROS), Tobin's Q and stock returns (RET). All proxies were measured in the t year. The measurement of CSR disclosure in this study was based on the research of Raar (2002) and Gunawan (2010) to measure the quantity and quality of CSR disclosures in financial statements. For measurement of quantity (how much), this study provided a score between 1 to 5. For quality measurement (how to express), this study provided a score between 1 to 7, depending on how the companies describe the CSR information. All data was taken from the annual reports which explicitly mention the CSR report section. This study applied t-1 data for CSR disclosure variables. The factors of corporate governance in this study were foreign ownership, state ownership, the number of board of commissioners, the independence of the board of commissioners, and the educational background of the board of commissioners measured using t-1 data. This study used the percentage of foreign shareholder equity as a proxy for foreign ownership (Douma et al., 2006; Khan et al., 2013; Kabir & Thai, 2017). The percentage of ownership share by the state was used as a proxy for state ownership (Boubakri et al., 2009; Xu et al., 2014; Kabir & Thai, 2017). The number of commissioners owned by the company was used as a proxy for the number of board of commissioners. Board of commissioners' independence was measured by the proportion of independent commissioners on the board of commissioners (Liu et al., 2015; Khan, 2013; Lima & Sanvicente, 2013; Kabir & Thai, 2017). Regarding the educational background of the board of commissioners, this study applied a proxy for educational background in finance. The educational background of the board of commissioners was measured by the proportion of board members who hold a degree in finance (Darmadi, 2013; Esa & Zahari, 2016). 4. Results and Discussion 4.1. Descriptive Statistics Based on the result of statistic descriptive analysis, it could be recognized that the variable of foreign ownership measured by the percentage of the equity of the foreign shareholder shows a minimum value of 0% (zero percent) and a maximum of 99.78%. The mean value of the foreign ownership variable is 31.09% and its standard deviation is 30.87%. The value that occurs quite frequently (modus) in this variable is 0%. It means that many of the companies in Indonesia do not have foreign shareholders. With the median value of 20%, it shows that half of the sample companies only have a percentage of foreign shareholders less than 20%. 4.2. Result of hypothesis testing To test the hypothesis about the relationship developed in this model, the value of p-value becomes the basis of the significance of the relationship between the exogenous and endogenous variables. This research applies the level of significance of 5%. $p\text{-value} < 0.05$ is said to be significant on the alpha 5% which means the hypothesis is supported on the alpha of 5%. The number of Path coefficients and p-value of this research, using WarpPLS 5.0 for hypothesis 1 through 6 is seen on the output Path Coefficients and p-value that can be seen in the following Table 2. The test result on the beta parameter coefficient on the relationship between foreign ownership and CSR disclosure shows a negative coefficient of −0. 090 with a p-value of 0. 055 ($p\text{-value} \geq 0.05$) which means insignificant at alpha 5%. The test result of this hypothesis indicates that foreign ownership has an insignificant effect on CSR disclosure and H1a Table 1: Descriptive Statistics which suggests that foreign ownership has a positive effect on CSR disclosure is not supported. The result of the test in this research is not in line with agency theory where foreign ownership is usually regarded as a monitoring signal that may affect both the implementation and disclosure of CSR activities. The test result on the beta parameter coefficient on the relationship between state ownership and CSR disclosure shows a positive effect of 0.154 with a $p\text{-value} < 0.001$ ($p\text{-value} < 0.05$) which means significant at alpha 5%. The test result of this hypothesis indicates that state ownership has a positive effect on CSR disclosure, and thus H1b which proposes that state ownership has a positive effect on CSR disclosure is supported. This finding is in line with Lau et al. (2014) who confirmed that state ownership has a positive effect on CSR disclosure. The result of the test on the beta parameter coefficient on the relationship between the number of board of commissionaires and CSR disclosure shows a positive effect of 0.282 with a $p\text{-value} < 0.001$ ($p\text{-value} < 0.05$) which means significant at alpha 5%. The test result indicates that the number of board of commissionaires has a positive influence on CSR disclosure, and thus H2a which states that the number of board of commissionaires has a positive effect on CSR disclosure is supported. This finding is in line with Esa and Ghazali (2012), Siregar and Bachtiar (2010), and Said et al. (2009) who confirmed that the number of board of commissionaires gives a positive influence on CSR disclosure. Variables n Minimum Maximum Mean Std. Deviation FO 582 0 99.78 31.09 30.87 SO 582 0 90.03 5 17.58 NC 582 2 10 4.49 1.72 IC 582 0.25 1 0,4 0.1 EC 582 0 1 0.54 0.25 ROE 582 −0.57 0.66 0.07 0.14 ROA 582 −0.21 0.43 0.04 0.08 ROS 582 −3.8 1.32 0.04 0.37 Q 582 0 8262.49 18.44 343.01 RET 582 −1 72 2.22 8.3 SIZE 582 22.21 32.92 28.86 1.57 LEV 582 0.01 1,98 0.45 0.21 FO: Foreign ownership; SO: State ownership; NC: The number of board of commissionaires. IC: Proportion of independent commissionaires; EC: Educational background of the board of commissionaires; ROE: Return on equity; ROA: Return on assets; ROS: Return on sales; Q: Tobin's Q; RET: Return on share; SIZE: Size of the company;

LEV: Leverage. Table 2: Result of Hypothesis Testing Hypothesis Path coefficients p-value Conclusion H1a: The effect of the foreign ownership on the Corporate Social Responsibility (CSR) disclosure −0.090 0.055 Not supported H1b: The effect of the state ownership on the Corporate Social Responsibility (CSR) disclosure 0.154 < 0.001 supported H2a: The effect of the number of the commissionaire board on the Corporate Social Responsibility (CSR) disclosure 0.282 < 0.001 supported H2b: The effect of the proportion of the commissionaire board on the Corporate Social Responsibility (CSR) disclosure 0.119 < 0.001 supported H2c: The effect of the educational background of the commissionaire board on the Corporate Social Responsibility (CSR) disclosure −0.080 0.080 Not supported H3: The effect of the Corporate Social Responsibility (CSR) disclosure on the performance of corporate finance 0.094 0.026 supported The test result on the beta parameter coefficient of the relationship between independent commissionaires' proportion and CSR disclosure shows a positive influence of 0.119 with a p-value < 0.001 (p-value < 0.05) which means significant at alpha 5%. The test result of this hypothesis indicates that the proportion of independent commissionaires has a positive influence on CSR disclosure, and thus H2b which states that independent commissionaires proportion has a positive effect on CSR disclosure is supported. This research finding is in line with Khan et al. (2010) who discovered that a company that has a proportion of independent commissionaires is able to improve the disclosure of CSR to maintain the reputation and to realize the sustainable development of the company. The result of the test on the beta parameter coefficient on the relationship between the educational background of the board of commissionaires and CSR disclosure indicates a negative impact of -0.080 with a p-value of 0.080 (p-value ≥ 0.05) which means insignificant at 5%. The test result of this hypothesis shows that the educational background of the board of commissionaires does not have an effect on CSR disclosure, and thus H2c which states that the educational background of the board of commissionaires has a positive effect on CSR disclosure is not supported. This test result is not in line with agency theory. However, the result supports research done by Haniffa and Cooke (2005). The more diverse educational background of the board of commissionaires will tend to produce more innovative problem-solving. The differences in the educational background will lead the board of commissionaires to see problems from various perspectives based on their knowledge. The result of the test on the beta parameter coefficient on the relationship between CSR disclosure and financial performance of the companies shows a positive effect of 0.094 with a p-value of 0.026 (p-value < 0.05) which means significant at alpha 5%. The test result of this hypothesis indicates that CSR disclosure positively affects the company's financial performance, and thus H3 which states that CSR disclosure has a positive effect on the company's financial performance is supported. This finding is in line with Siregar and Bachtiar (2010). 5. Conclusion Based on the analysis results of data obtained, conclusions that can be drawn from this research are: Foreign ownership does not have a significant effect on CSR disclosure. It is due to the lower level of foreign ownership resulting in the inability of the foreign investors to carry out greater monitoring. The foreign shareholders are also unable to influence both the implementation and disclosure of CSR activities done by the management. State ownership has a significant and positive influence on CSR disclosure. It is because the companies that have an association with the government (companies with high state ownership) tend to pursue social and political goals and maximize profits. The disclosure of CSR is used to pursue the goals; where in addition to realizing their social purposes, companies will also be able to experience the benefits of CSR in the forms of either short-term or long-term benefits. The number of board of commissionaires has a significant and positive effect on CSR disclosure. The larger number of the board of commissionaires will make the monitoring process (including the monitoring of CSR disclosure in the annual report) better. However, if the number of the board of commissionaires is overly large, the monitoring process will be ineffective. A larger board of commissionaires may also contribute to broader and beneficial discussions on CSR and its long-term benefits. The proportion of independent commissionaires has a significant and positive influence on CSR disclosure. Companies with a proportion of independent commissionaires are capable of improving the CSR disclosure to maintain their reputation and to realize the companies' sustainable development. It is mainly because independent commis- sionaires tend to provide recommendations that aim not only for short-term objectives but also for the long-term. The educational background of the board of commissionaires has an insignificant effect on CSR disclosure. It is possibly due to this research only defines the educational background specifically on business and economy (finance), whereas there are possibilities that the educational background of the board of commissionaires which is relevant to the companies' type of industry is more required to support the companies' business viability. Disclosure of CRS provides a significant and positive effect on a company's financial performance. The positive effect of the CSR disclosure on performance is because CSR disclosure is able to improve the company's reputation; when more social activities are carried out will improve the customers' loyalty as well as the support from other stakeholders (including the investors) which in turns will improve the company's performance. There are several limitations to this research, they are: The limited availability of annual reports since the period of observation is considered as new, 2017, that many companies have not uploaded their annual reports yet, into either the IDX website or the companies' websites. This research employs the quality of CSR disclosure as one of the measuring instruments of CSR disclosure which applies a limited scoring system in accordance with the previous studies. Several suggestions for future research are: For future research, it is expected to use a broader measurement of CSR disclosure, such as based on GRI 4. It is expected for future research to add more independent variables that possibly affect the CSR disclosure such as audit committee as the complementary of the monitoring function and media exposure in regard to the current digitalization era. References Aguinis, H., & Glavas, A. (2012). What we know and don't know about corporate social responsibility: A review and research agenda. Journal of Management, 38, 932–968. https;//doi. org/10.1177/0149206311436079 Barnett, M., & Salomon, R. (2012). Does it pay to be really good? Addressing the shape of the relationship between social and financial performance. Strategic Management Journal, 33(11), 1304–1320. https://doi.org/10.1002/smj.1980 Boubakri, N., Cosset, J. C., & Guedhami, O. (2009). From state to private ownership: Issues from strategic industries. Journal of Banking and Finance, 33(2), 367–379. https://doi. org/10.1016/j.jbankfin.2008.08.012 Cahan, S. F., Villiers, C. D., Jeter, D. C., Naiker, V., & Staden, C. J. V. (2015). 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