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## **Corporate Social Responsibility and Factors Affecting It: An Empirical Evidence from the Indonesian Capital Market**

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**Abstract:**

**Purpose:** This study aims to evaluate the influence of family ownership and profitability on corporate social responsibility disclosure with firm size as a control variable in manufacturing companies listed on the Indonesia Stock Exchange.

**Design/Approach/Methodology:** Implementing a purposive sampling method, this study ended up with 32 manufacturing companies as a sample for the 2014-2018 periods (i.e., 160 observations).

**Findings:** By using OLS regression, the findings show that profitability has a positive influence on CSR disclosure, meanwhile for family ownership does not. Moreover, firm size as a control variable influences positively on CSR disclosure.

**Practical Implications:** With its limitation such as the relatively low number of samples, this study contributes to providing empirical evidence on factors influencing CSR disclosure in an emerging market context, i.e., Indonesia.

**Originality/Value:** There is not a similar research using data from Indonesia neither the firm size as a control variable in the proposed model.

**Keywords:** CSR, family ownership, profitability, firm size.

**JEL code:** G32, M41.

**Research type:** Research article.

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## **1. Introduction**

Corporate Social Responsibility (hereafter, CSR) has become a global trend in the last decade with the increasing level of public concern on social and environmental issues. Particularly for Indonesian listed companies, CSR activities are disclosed in an annual report called Sustainability Reporting. This report reveals the company's economic, environmental and social policies, and company performance in the context of sustainable development. It is indicating that good companies are not only concerned with economic benefits but also have concerns for environmental sustainability and social issues (Suyono, 2011; Aguinis and Glavas, 2012; Arnold and Valentin, 2013; Suyono and Farooque, 2018).

The public concern of the importance of practicing CSR disclosure increases with the increasingly widespread public awareness of products that are environmentally friendly and are produced by paying attention to social and human rights principles. (Ioannou and Serafeim, 2012; Jamali and Karam, 2018; Jamali *et al.*, 2017; Suyono and Farooque, 2018).

The disclosure of CSR activities in Indonesia is also motivated by several cases regarding the negative impact of corporate activities on the environment and society such as on the cases of PT Vale Indonesia, PT., Freeport Indonesia, etc. These cases occurred due to the company's lack of attention to the environment and society by over-exploiting existing resources not according to established rules (Suyono, 2011; Suyono and Farooque, 2018).

Moreover, a study by Sharma (2013) states that companies in Indonesia have a lower quality of CSR compared to companies in Singapore and Thailand. The results of the study explained that Thailand became the country with the highest quality CSR scored at 56.8 out of a total of 100, Singapore is 48.8, while Indonesia and Malaysia are 48.4 and 47.7 respectively. The assessment criteria are based on several indicators from the Global Reporting Initiative (GRI) framework, namely corporate governance, the economy, the environment, and social affairs. Based on the results of this research, the government and industry stakeholders and the involvement of academics to continue to study the factors that influence the CSR disclosure have a very important role to ensure the reporting of sustainable CSR as a key to governing business in a better way.

Many previous studies have examined the effect of CSR disclosure on company performance (Shauki, 2011; Waagstein, 2011; Suyono, 2011; Ararat *et al.*, 2018; Fanti and Buccella, 2018). Conversely, only limited literature that presents the influence of company performance on CSR Disclosure, such as Nawaiseh *et al.* (2015) in Jordan, Wakid *et al.* (2013), Hermawan and Mulyawan (2014), Dhiyaul-Haq and Santoso (2016), and Nasution *et al.* (2018) in Indonesia. Nawaiseh *et al.* (2015) found that ROE is positively related to CSR disclosure while ROA does not have a significant relationship. This finding is in line with the results of Wakid *et al.*

(2013) in Indonesia. In another side Hermawan and Mulyawan (2014) concluded that there is very little correlation between company performance and the quality of CSR disclosure in Indonesia, which indicates that CSR disclosure is intended to maintain the company's reputation in front of shareholders, not to allocate a portion of company profits in CSR activities.

Furthermore, Dhiyaul-Haq and Santoso (2016) also proved that profitability (Return on Assets) and family ownership do not have a significant effect on the CSR disclosure by Islamic Commercial Banks registered in the Financial Services Authority during the period 2010-2014 in Indonesia. Similarly, Nasution *et al.* (2018) found that profitability is not significantly related to CSR disclosure in Indonesian public companies.

Based on the evaluation from some of the previous studies showing varied and inconsistent results, this study tries to reexamine the effect of family ownership and profitability on CSR disclosure with firm size as a control variable in the Indonesian context. The main focus of this study is to evaluate the link between company's financial performance which is measured by ROA as a proxy of profitability and CSR disclosure by considering the presence of family ownership and firm size as a control variable, in the Indonesian context.

## **2. Theoretical Framework and Hypotheses Development**

### **2.1 Theoretical Framework**

Stakeholder theory states that all stakeholders have the right to obtain information concerning the company activities that can influence their decision making (Deegan, 2004). Stakeholder theory reveals that a company does not only operate for its own sake but must also benefit its stakeholders (Suyono and Farooque, 2018). Thus, the existence of a company is strongly influenced by the support given by all stakeholders. Therefore, the company must maintain the relationship with its stakeholders by accommodating their desires and needs, especially stakeholders who have the power to the availability of resources used for the company operational activities such as labor, markets for company products and others. One strategy that companies use to maintain the relationship with their stakeholders is by disclosing social and environmental information (Carol, 1991; Chittoor *et al.*, 2015; Khanna and Rivkin, 2001; Ramaswamy *et al.*, 2017; Cech *et al.*, 2018) where in the Indonesian context, it uses sustainability reporting (Suryanto *et al.*, 2017).

Deegan (2004) suggests that based on stakeholder theory, managers are expected to carry out activities that are considered important by their stakeholders and report back on these activities to them. This theory states that stakeholders have the right to be provided with information about how organizational activities affect them (for example pollution, sponsorship, security initiatives, etc.), even if they choose not to

use that information and even when they cannot directly play a constructive role in supporting the sustainability living of the organization.

In other words, legitimacy theory recommends carrying out CSR activities in response to environmental pressures related to social, political, and economic forces. Therefore, companies try to find a balance point in running their business with the wishes of the surrounding community (Deegan, 2002; Akhmad, 2004; Sarkar, 2010; Gomez-Mejia *et al.*, 2011; Block and Wagner, 2014; Liu *et al.*, 2017). Gray (2001) suggested that the theory of legitimacy is a condition or status, which exists when a company's value system is congruent with the value system of the larger social system in which the company is a part. When a potential difference exists between the two value systems, there will be a threat to the legitimacy of the company (Suyono and Farooque, 2018).

The strength of the theory of organizational legitimacy in the context of CSR in developing countries is as follows (Barkemeyer, 2007):

- a. The capability to put profit-maximizing motives makes a clearer picture of a company's motivation to increase its social responsibility.
- b. Organizational legitimacy can include cultural factors that shape different institutional pressures in different contexts.

Therefore, CSR is a genuine effort by business entities to minimize negative impacts and maximize the positive impact of its operations on all stakeholders in the economic, social, and environmental sphere in order to achieve sustainable development goals (Block and Wagner, 2014; Liu *et al.*, 2017). Moreover, Deegan (2002) states that corporate motivation for CSR disclosure includes:

- 1) Meet and comply with legal rules
- 2) Economic rationale, it is related to building an image and supporting a competitive advantage
- 3) As a form of accountability and responsibility
- 4) Fulfill the loan requirements
- 5) Meet the expectations of the community
- 6) Get legitimacy
- 7) Manage several stakeholder groups
- 8) Withdraw funds from investors
- 9) Fulfill and implement codes of ethics in the industry
- 10) Meet the policies in disclosure, and
- 11) Award in reporting.

The different characteristics possessed by each company causes a different significance level of CSR disclosure in the annual report. A study conducted by Bansal *et al.* (2018) found evidence that family ownership strengthened the role of independent directors to increase CSR disclosure.

Companies with family ownership constitute the majority in Indonesia (Suyono, 2018). Family businesses have an important role in the economy, both local and regional because they can provide permanent economic stability. Family ownership is non-diversified share ownership and is committed to generating strong incentives for certain families to monitor the company (Anderson *et al.*, 2003). Furthermore, Anderson *et al.* (2003) explain that companies with family ownership do not just place their family members in the positions of CEO, commissioner or other management positions. This company is generally owned in the majority by certain families or the ownership of shares is concentrated in certain families.

According to Martinez *et al.* (2007) and Suyono (2016) companies that have a concentration of family ownership are believed to have a much better company performance than companies that are not based on family ownership. This is because companies controlled by families can professionalize their management and governance when they feel they are under market supervision and when they are accountable to minority shareholders.

Profitability assessment is the process of determining how well business activities are carried out to achieve strategic objectives, eliminating waste and presenting timely information to carry out the continuous improvement. There are several performance measurements of company profitability where each measurement is related to sales volume, total assets, and own capital. Overall these three measurements will allow an analyst to evaluate the level of earnings concerning the sales volume of a certain number of assets and investments of the company owner (Mafudi and Suyono, 2018).

Profitability ratios measure a company's ability to generate profits from business activities carried out. As a result, investors can see how efficiently a company is using assets and in carrying out its operations to generate profits. Return on Assets (ROA) is the ratio of net income to total assets used to measure returns on total assets after interest and taxes. Positive ROA shows that of the total assets used to operate, the company can provide profits for the company.

Firm size is the size of the company as seen from the value of equity, the value of the company or the total assets (total assets) of a company. The greater the assets, the greater the capital invested, while the more sales there will be more money in the company. Thus, the size of the company is the scale of the size of assets owned by the company.

## **2.2 Hypotheses Development**

### **2.2.1 Family Ownership and CSR Disclosure**

The family business is a business that is owned and/or managed by several people who have a family relationship, both husband and wife and offspring, including kinship (Anderson *et al.*, 2003; Suyono, 2018). Furthermore, Suyono (2018)

revealed that most of the Indonesian listed companies are owned majority/dominant by the family of the founder of the company, and this founding family is involved in the company managerial.

Company ownership arises from a comparison of the number of shareholders in the company. A company can be owned by an individual, family, the public, government, foreign parties, or managers (Suyono, 2011). From the stakeholders' perspective, CSR disclosure is the chosen tool to show the company's concern for the community's environment. According to Suyono and Farooque (2018) if the company has majority ownership of shares controlled by the family, then the company will be more supported in carrying out CSR disclosures. This is inseparable from the company that most of the shares owned by the family usually more often face the problem of information asymmetry. Thus, companies with large family ownership will be encouraged to disclose information voluntarily and widely.

Theoretically, Hirigoyen and Poulain-Rehm (2014) revealed a relationship between proactive stakeholder involvement and CSR of family business. Disclosure of social responsibility for companies with family share ownership is an important factor that is seen as the need to form an identity and project a positive image and to preserve corporate heritage (Young *et al.*, 2008). Therefore, family business owners consider company unrest or customer complaints as elements that can damage their business so they tend to have high involvement in CSR activities.

Empirically, a study conducted by Bansal *et al.* (2018) found evidence that family ownership strengthens the role of independent directors to increase CSR disclosure. Based on arguments as above, the first hypothesis in this study can be formulated as follows:

*H<sub>1</sub>: Family ownership influences positively on CSR disclosure.*

### **2.2.2 Profitability and CSR Disclosure**

Profitability is the company's ability to manage assets owned to generate profits (Mafudi and Suyono, 2018). High profitability shows good company performance, and with high profits the company has enough funds to collect, classify and process information to be more useful and can present better disclosures. The legitimacy theory asserts that companies should seek legitimacy from stakeholders by revealing more about social activities and the environmental impact on profits obtained (Degaan, 2004; Agrawal and Sahasranamam, 2016).

Therefore, profitable companies tend to try to show that the profits obtained are also allocated to carry out social activities and environmental preservation. In addition, Agrawal and Sahasranamam (2016) also shows that the higher the profit of a company, the higher the extent of CSR disclosure. This is because companies tend to try to show evidence that profits are followed by activities that restore environmental conditions or contribute to social responsibility. Hermawan and Mulyawan (2014) stated that several

previous studies have confirmed mixed results in explaining the relationship between profitability variables and CSR disclosure. Mafudi and Suyono (2018) find that profitability has a positive association with CSR. Similar findings were also obtained from the study of Wakid *et al.* (2013). Referring to the results of the research, the second hypothesis can be formulated as follows:

*H2: Profitability has a positive effect on CSR disclosure.*

### **3. Research Methodology**

#### **3.1 Sampling of the Study**

This research is an empirical study on manufacturing companies listed on the Indonesia Stock Exchange (IDX) in the period 2014-2018. The criteria for sample selection are as follows:

- 1) manufacturing companies listed on the Indonesia Stock Exchange during the study period;
- 2) manufacturing companies that are not delisted from the Indonesia Stock Exchange during the study period;
- 3) manufacturing companies that have positive profits during the study period;
- 4) manufacturing companies that have share ownership by the family group during the study period.

From 146 manufacturing companies listed on the Indonesia Stock Exchange, 32 companies are selected as a sample, so that for 5 years (2014-2018) 160 observations are obtained.

#### **3.2 Measurement of Variables**

##### **3.2.1 Family Ownership**

Family ownership is non-diversified share ownership and is committed to generating strong incentives for certain families to monitor the company (Anderson *et al.*, 2003). The family ownership variable referred to in this study is the percentage of company stock ownership by a certain family from the total shares outstanding (Suyono and Farooque, 2018).

##### **3.2.2 Profitability**

The company's profitability in this study is measured by using the Return on Asset (ROA) ratio with the following formula (Mafudi and Suyono, 2018):

$$ROA = \frac{\text{Net Income}}{\text{Total Assets}} \times 100\%$$

### 3.2.3 Firm Size

Firm size is measured by using Natural Logarithms (Ln) of total assets (Suyono and Farooque, 2018).

### 3.2.4 CSR Disclosure

The standard used to measure CSR disclosure is the Global Reporting Initiative (GRI) index. The GRI standard is chosen because it is more focused on the standard disclosure of various economic, social, and environmental performance of the company to improve the quality, and utilization of sustainability reporting. In the GRI-G 3.1 standard (GRI, 2013) performance indicators are divided into 3 main components, namely economic, environmental, and social, including labor practices and work comfort, human rights, society, and product responsibility. Thus, the total performance indicators in GRI-G 3.1 are 84 items. The formula for calculating the Corporate Social Responsibility Disclosure Index (CSRDI) is as follows (Suyono, 2011; Suyono and Farooque, 2018):

$$CSRDI = \frac{\sum X}{N} \times 100\%$$

where:

CSRDI : corporate social responsibility disclosure index  
 $\sum x$  : Number of CSR disclosure items by the company ( $\leq 84$ )  
N : Total items based on GRI-G3.1. (84)

## 3.3 Data Analysis

Before the *ordinary least square* (OLS) as main analysis, this study presents the test of descriptive statistics, correlation matrix, and classical assumption of regression which consists of normality, multicollinearity, autocorrelation, and heteroscedasticity. Then, data analysis is done by using OLS with the following equation:

$$CSR = \beta_0 + \beta_1 FAM + \beta_2 PROF + \beta_3 SIZE + \varepsilon \quad (1)$$

where:

CSR= corporate social responsibility disclosure

FAM= family ownership

PROF= profitability which is measured by Return on Assets (ROA)

SIZE= firm size

$\beta_0$  = a constant

$\beta_1 - \beta_3$  = Regression coefficients

$\varepsilon$  = error

## 4. Finding and Discussion

### 4.1 Descriptive Statistics and Classical Assumption of Regression

Table 1 below shows the descriptive statistics of the variables in this study. The mean value of the dependent variable of CSR is 0.3691 ranging from 0.13 to 0.62. Moreover, the mean values for family ownership (FAM), profitability (PROF), and firm size (SIZE) are 0.6365, 7.0149, and 14.4161 respectively.

**Table 1.** *Descriptive Statistics*

|      | N   | Min   | Max   | Mean    | St. Dev |
|------|-----|-------|-------|---------|---------|
| CSR  | 160 | 0.13  | 0.62  | 0.3691  | 0.07569 |
| FAM  | 160 | 0.14  | 0.96  | 0.6365  | 0.21399 |
| PROF | 160 | 0.08  | 26.15 | 7.0149  | 5.31656 |
| SIZE | 160 | 11.40 | 18.34 | 14.4161 | 1.66711 |

Before the *ordinary least square* (OLS) as main analysis, this study presents the test of descriptive statistics and classical assumption of regression which consists of normality, multicollinearity, autocorrelation, and heteroscedasticity.

Normality test in this study uses the Kolmogorov-Smirnov method. Residual values are said to be normally distributed if the significance value of Standardized Residuals  $> 0.05$  ( $\alpha$ ). The normality test results show Asymp. Sig is 0.145 which is higher than 0.05 meaning that all data are distributed normally. Multicollinearity test is done by looking at the value of Variance Inflation Factor (VIF) of each independent variable on the dependent variable. If the VIF value is less than 10 then the model is declared not to contain multicollinearity problem. The results of multicollinearity testing of VIF values for the FAM, PROF, and SIZE variables are 1.323, 1.078, and 1.213 respectively which are lower than 10. It means that there is no multicollinearity problem in the model. Heteroscedasticity test is a test that aims to test whether the regression model occurs variance, namely variance from residuals of one observation to another. Heteroscedasticity test results with Park Glejser show the significance value of FAM, PROF, and SIZE of 0.134, 0.296, and 0.481 respectively which are higher than 0.05. It means that there is no heteroscedasticity problem in the model.

The autocorrelation test in this study uses the Durbin-Watson test (DW test) where the DW value of 1,937 is between the dU (1,759) and 4-dU (2,241) values, so that the research model is free from autocorrelation problems.

### 4.2 Results of OLS

Table 2 below presents the OLS regression results explaining the link between CSR disclosure (CSR) and family ownership (FAM), profitability (PROF), and Firm size

(SIZE) as a control variable. PROF as an independent variable has a positive and significant influence on CSR, meanwhile, FAM does not. Moreover, SIZE as a control variable has a positive and significant influence on CSR.

PROF has a positive significant explanatory power in determining CSR at p 0.003 with a coefficient value of 0.032. Similarly, SIZE appears to have a significant positive effect on CSR at p 0.001 with a coefficient value of 0.019. In another side, FAM shows no significant effect on CSR. Based on the OLS result, the regression model is as follows:

$$\text{CSR} = 0.003 + 0.039 \text{ FAM} + 0.032 \text{ PROF} + 0.019 \text{ SIZE} + \varepsilon$$

**Table 2.** *Result of OLS*

| Model | Unstandardized Coefficients |            | Standardized Coefficients | t     | Sig.  |
|-------|-----------------------------|------------|---------------------------|-------|-------|
|       | B                           | Std. Error | Beta                      |       |       |
| 1     | (Constant)                  | 0.003      | 0.062                     | 0.162 | 0.803 |
|       | FAM                         | 0.039      | 0.032                     | 1.627 | 0.136 |
|       | PROF                        | 0.032      | 0.001                     | 3.697 | 0.003 |
|       | SIZE                        | 0.019      | 0.004                     | 4.786 | 0.001 |

**Note:** *Dependent Variable CSR; F: 14.369, Sig. 0.000; Adjusted R Square 0.411*

### 4.3 Discussion

The first hypothesis in this study states that family ownership has a positive effect on the disclosure of corporate social responsibility. The OLS results show that family ownership has no significant effect on CSR disclosure, so the first hypothesis is not supported. Thus, the findings in this study fail in proving the concept of stakeholder theory which views that CSR disclosure is the tool chosen to show the company's concern for the society's environmental issues. According to Ararat *et al.* (2018) in a company whose majority shares are owned by the family, the company will be more supportive of the implementation of CSR disclosures. The findings in this study also do not confirm the argument of legitimacy theory which indicates that to obtain legitimacy, companies with high family ownership will carry out more social and environmental activities so that they influence internal and external parties who have an interest in the company.

The findings in this study are more in line with arguments in the theory of market efficiency (Fama, 1970) which states that the problems that occur in companies that are mostly owned by families are usually related to the problem of disclosure of information that is not done in full. Fama (1970) argues that if disclosure of the information is not carried out in full, it will cause information asymmetry. The asymmetry of information is interpreted by the existence of different perceptions between families who have shares in the company with the community. What companies do as CSR is often responded to not as CSR by the public. For example,

the case of CSR from PT., Indal Aluminum Industri Tbk in Indonesia, which directly industrial waste does not pollute the environment, so when the company is involved in handling the ecosystem will be considered by stakeholders as an obligation, not a concern.

Furthermore, Barnea and Rubin (2010) argued that companies with a percentage of family ownership would be interested in investing in CSR activities if it is believed they would get a lot of benefits from these activities. So, companies with a family ownership structure are generally more or less motivated to disclose additional information on corporate social responsibility disclosure activities if they feel they will not benefit too much. As an example of a company's implementation, some of the company's social responsibility disclosure funds come from return earnings, which means that it will reduce dividend rights for investors. Shareholders who are also a family of management will certainly influence management to reduce CSR activities to obtain greater individual profit.

The main objective of family shareholders according to Lahouel *et al.* (2014) is the continuity of their business and maintaining their reputation. Research conducted by Lahouel *et al.* (2014) shows that family ownership does not affect the disclosure of corporate social responsibility. Based on these explanations, the results of this study are also in line with the findings of a previous study conducted by Dhiyaul-Haq (2016) which also shows evidence that family ownership has no significant effect on disclosure of corporate social responsibility.

The second hypothesis of this study states that profitability has a positive effect on CSR disclosure. The OLS results show that profitability has a significant influence on CSR disclosure meaning that the second hypothesis is proven. According to Wakid *et al.* (2013) and Mafudi and Suyono (2018) companies with a high level of profitability tend to disclose more CSR information, because companies that have the ability to generate high profits, usually also have a lot of funds, including to make disclosures of social responsibility to reduce social pressure and negative views from the market.

The acceptance of the second hypothesis means that this research supports the theory of legitimacy which indicates that to obtain legitimacy, companies with high profitability seek to gain legitimacy from parties associated with the company to show evidence that the profits obtained are allocated to activities that support the surrounding environment. The results of this study are in line with the findings of a previous study conducted by Wakid *et al.* (2013) and Mafudi and Suyono (2018) which also shows evidence that profitability has a significant effect on disclosure of corporate social responsibility. In another side, it contradicts with Nawaiseh *et al.* (2015) found that ROE is positively related to CSR disclosure while ROA does not have a significant relationship. Likewise, firm size is not significantly related to CSR disclosure. This finding is in line with the results of Wakid *et al.* (2013), in Indonesia. Similarly, the finding of this study is not in-line with Hermawan and

Mulyawan (2014) concluded that there is very little correlation between company performance and the quality of CSR disclosure in Indonesia.

Moreover, the finding for firm size (SIZE) as a control variable shows its significant influence on CSR disclosure. It could be interpreted that a company with larger size makes it easier to get information on it so the company will disclose more extensive information, causing a greater level of CSR disclosure to be carried out. It supports previous studies, such as Wickert *et al.* (2016), Hermawan and Mulyawan (2014), Dhiyaul-Haq and Santoso (2016) and Nawaiseh *et al.* (2015) which states that company size has a positive effect on CSR disclosure. This research also supports the theory of legitimacy which indicates that larger companies will carry out more activities so that they have a greater influence on society. Companies with large size also have more shareholders who have attention to the social programs undertaken. Therefore, the bigger the company the greater the level of CSR disclosure carried out.

## **5. Conclusions**

This study aims to evaluate the influence of family ownership and profitability on CSR disclosure with firm size as a control variable. By using purposive sampling method, this study ended up with 32 companies as a sample for 2014-2018 period (i.e., 160 observations). The OLS results show that profitability has a positive association with CSR disclosure, meanwhile, family ownership does not. Moreover, firm size as a control variable has a positive influence on CSR. Based on the findings it is recommended that companies with significant family ownership should incur additional costs devoted to CSR activities to further enhance the company's reputation in front of all stakeholders.

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