Conference Paper

Corporate Governance and Disclosure Level in Mining Companies: Evidence from Regulation Changes in Indonesia

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Abstract

This study aims to know the influence of company disclosure after the regulation of Minister of Energy and Mineral Resources Number 7 Year 2012 and Regulation of Minister of Finance Number 75/PMK.011/2012 in Indonesian mining companies. The data used in this study come from mining companies listed on the BEI 2010–2014 with a total of 184 mining companies. The analysis technique used is the method of multiple linear regression analysis with the help of software STATA 14.0. Our first prediction is that firms with better governance mechanism will have higher level of disclosure. Regression results indicate that after the government regulations on mining companies, corporate governance practices and ownership structures have no effect on the level disclosure of mining companies in Indonesia.

Keywords: *disclosure, corporate governance, ownership structure*

1. Introduction

Environmental, social and corporate governance are important and integral aspects of company performance. However, the literature about the impact of corporate governance aspects on sustainability disclosure is still relatively small and, so far, it is focused primarily on developed countries (Michelon & Parbonetti, 2012). Developing countries markets have a tendency to show weak corporate governance and sustainability (Lenssen et al., 2011).

Disclosure of financial statements becomes important to be a measure of the shareholders' trust in the company. Gunawan et al. (2009) examine corporate disclosures in the company's annual report listed on the Indonesian stock exchange over the 2003-2006 period and found that companies in sensitive industrial environments, such as mining, tend to disclose more environmental information than other industries.

In Agency Theory, it is explained that it is difficult to trust that management (agent) will always act in the interests of the principals, so that it requires supervision from the shareholders (principal). Agency conflicts arise because people tend to be self-centered, so then it generates conflict as some interests have to be met. The existence of this agency conflict can, of course, lead to agency cost. Ashbaugh, Collins, and Lafond (2009) find that agency costs can also occur due to information asymmetry because shareholders cannot observe manager behavior directly. So, to reduce the asymmetric information between management and shareholders, the company must increase its openness (Lang & Lundholm, 1993)

This is in connection with the Regulation of Minister of Energy and Mineral Resources Number 7 Year 2012 and Regulation of the Minister of Finance Number 75 / PMK.011 / 2012 concerning the increase of added value of minerals and the determination of exported goods subject to the export duty tariff, whose content prohibits the export of raw materials or minerals before it has been first processed. So, the mining company must do the processing before it is exported. In the processing activities, the company must issue additional costs, labor and capital from investors to support operational activities before goods are ready to export. The activity involves investors, so the company must show the credibility of financial statements and the quality of financial information to convince them. In this case, the company can perform disclosure to reduce the information asymmetry that creates agency problem.

Improving corporate disclosure requires good corporate governance to supervise and monitor. Corporate governance can also provide control benefits to board of directors, commissioners, audit committees and ownership structures. In the case of the ownership structure, the study measures the percentage ownership of shares owned by parties other than management (commissioners and directors) whose ownership is above five percent of the total shares, which is as ownership of blockholders.

Previous research has generally focused on examining the influence of ownership structure on firm value or firm performance (Claessens, Djankov, Fan & Lang, 2002; Morck, Shleifer, & Vishny, 1988; Thomsen, Pedersen, & Kvist, 2006), but empirical studies investigating influences of ownership structure on corporate disclosure in emerging markets is relatively rare, especially in Indonesia. One previous study investigating the influence of ownership structure on corporate disclosures considers the possibility of non-linear relationships between ownership structure and corporate disclosure (Chau & Gray, 2010). The study found that firms tend to be reluctant to disclose information if this behavior jeopardizes their competitive position in the industry (Darrough & Stoughton, 1990; Dye, 2001; Verrecchia, 2001). This research is expected to provide benefits or information for investors to invest in mining companies after the emergence of ministerial regulations of ESDM in Indonesia.

2. Literature Review and Hypothesis

Disclosure is defined as providing the amount of information required for optimal operation of efficient capital markets (Suhardjanto & Wardhani, 2010). Annual report is a medium for companies to convey company information in the form of financial condition and other information to shareholders, creditors and other stakeholders. According to Suhardjanto and Wardhani (2010), the information disclosed in the annual report can be grouped into two, namely mandatory disclosure and voluntary disclosure.

Agency theory relates to the agency conflict that arises when the objectives of the principal and the agent are actually different, where the principal has difficulty to verify what the agent actually does. This happens because principals and agents have different risk preferences, so they choose different actions (Eisenhardt, 1989). Managers may act against the interests of the lender. The lender will anticipate this behavior by raising the interest rate on the loan. As a result, managers have an incentive to not act against the interest of the lender, by entering into the terms of the agreement under which the manager agrees to limit the additional loan when it is outstanding (Scott, 2012).

To reduce the asymmetric information between management and shareholders, the company must increase its openness. Disclosure may be provided through mandatory disclosure and voluntary disclosure (both financial and non-financial information). Companies should take the initiative to disclose matters other than required in legislation, but which can assist the decision-making process by stakeholders (Juniarti & Sentosa, 2010).

In increasing disclosure to reduce agency problem, good corporate governance is required in this case in which there can be a supervising and monitoring system. Corporate governance is a process and structure applied in running a company with the main objective to increase shareholder value in the long term by still paying attention to the interests of other stakeholders.

Disclosure is also closely related to the ownership structure in order to reduce agency conflict. The ownership structure is divided into managerial ownership, blockholder ownership and government ownership. Based on these studies, low managerial ownership and significant government ownership can increase voluntary disclosure. This study takes ownership of blockholders, because blockholder ownership is a shareholder whose ownership is at least 5% of the company's shares. Juniarti and Sentosa (2010) argue that potential shareholders are expected to have greater power in monitoring management, because their performance is closely related to the company's financial performance. This opinion is supported by Anderson, Mansi, and Reeb (2003), Chau and Gray (2010) and Lenssen et al. (2011).

The effectiveness of Corporate Governance is determined by how the Corporate Governance mechanism works within the company (Utami, Suhardjanto, & Hartoko, 2012) as well as any corporate governance structure. But if the mechanism or process is not working properly, the ultimate goal of protecting the interests of shareholders and stakeholders will never be achieved (Eng & Mak, 2003). In this case, the company must also understand the existence of agency theory in the interest of the agent with the principal, so that it takes the practice of Corporate Governance to supervise and monitor the activities of the agent as the company management of the principal.

Corporate governance itself can also provide control benefits for boards of directors, boards of commissioners, audit committees, ownership structures and financial disclosures. Therefore, corporate governance practices in the research use assessment of aspects such as boards of commissioners, boards of directors, audit committees and independent commissioners (Harford et al., 2012). Therefore, the authors assume that:

The audit committee is one of the committees established by the board of commissioners as one of the additional organs required in the implementation of good corporate governance principles. Audit committees arise as a result of supervisory role and the board of commissioners are generally inadequate. The importance of the audit committee in an open company is corroborated by Circular Letter of the Chairman of Bapepam no. Se-03 / PM / 2000 about the Audit Committee. This provision requires any public company or issuer to have an audit committee (Major, 2012).

Hypothesis 1: Audit committee size has a positive association on disclosure level

In a two-tier system, the roles of the board of commissioners and the board of directors are clearly separated. The board of commissioners will oversee the execution of the work performed by the board of directors. In a two-tier system, it is very clear that there is a difference between the function of taking and implementing the policy with the supervisory function. The decision-making function and its execution are carried out by the board of directors, while the oversight function of the policies carried out by the board of directors is done by the board of commissioners. In carrying out its vast duties, the board of commissioners may establish various committees to assist it to function more effectively. Utama (2012) states that there are two types of council committees. The first type is a committee that plays an important role in providing input to management and the board of commissioners on business decision-making that is important to the company, for example the strategic planning committee. The second type deals with monitoring or oversight functions of the board, such as audit committees, remuneration committees and nomination committees. These committees can specifically enhance the accountability of the board as they provide independent oversight of the various activities of the boards.

Hypothesis 2: Board size has a positive association on disclosure level

Companies tend to respond to the regulation in a positive way to increase their compliance to the regulation as well as to increase their reputation. In general, we expect that, after the implementation of the new regulation, the companies will increase their disclosure level in their annual report. The formal hypothesis is:

Hypothesis 3: Mining companies will have higher level of disclosure following new regulation imposed.

3. Research Methodology

The population and samples in the study are mining companies listed on the IDX in the period 2010-2015. This includes all financial data and annual reports. The total sample in this research is 184 mining companies.

3.1. Variable of disclosure

The data processing is done in two stages. The first stage is in the form of scoring on the disclosure of items in the annual report as conducted by Botosan (1997), while the second stage is testing the hypotheses.

3.2. Variable of corporate governance practice

In determining the Corporate Governance Practices there are two ways of analysis in entering the formula, as follows:

1. BOARDSIZE = BD + BC

   BOARDSIZE is an analysis of Corporate Governance Practices which is the sum total of board of directors (BD) and board of commissioners (BC) of a company.

2. AUDITSIZE = ∑AUDITCOMMITTEE

AUDITSIZE is an analysis of Corporate Governance Practices which is the sum total of the company's audit committee.

3.3. Variable of ownership structure

The next independent variable is the Ownership Structure, which is proxied by the large percentage of the ownership shareholders (blockholder). According to Eng and Mak (2003) and Thomsen et al. (2006), ownership of blockholders is the proportion of ordinary shares held by major shareholders (i.e. 5% or more of share ownership). A higher percentage of large shareholders shows more concentrated ownership.

4. Empirical Analysis

4.1. Descriptive statistics

Descriptive statistics provide information about the general description of the variables that will be tested. Concerning the description of the variables used in the study, *DISCLOSURE*, corporate governance practices (to be proffered through *BOARDSIZE and AUDITSIZE), the proxy ownership structure goes through BLOCKHOLDER, FIRMSIZE, LEVERAGE* and *ROA*. These descriptive statistics provide information on the minimum values, maximum values and mean (mean) values of each research variable. Descriptive statistics in this study can be seen in the following table:

Table 1: Descriptive Analysis.

Variables	Mean	Median	Minimum	Maximum
DISCLOSURE	0.625	0.600	0.486	0.829
BOARDSIZE	9.114	9.000	4.000	15.000
AUDITSIZE	3.071	3.000	2.000	5.000
BLOCKHOLDER	1.033	0.897	-0.875	3.476
FIRMSIZE	14.845	15.139	9.085	18.230
ROA	4.996	1.705	-22.000	49.910
LEVERAGE	0.616	0.740	-39.990	17.750

Table 1 above shows the results of descriptive statistics of research variables from observation year 2010 to 2014, each variable amounted to 184 companies engaged in mining.

Table 2: Pearson Correlation.

Variables	[1]	[2]	[3]	[4]	[5]	[6]	[7]
[1] DSCORE	1.000						
[2] BOARDSIZE	0.256***	1.000					
	(0.000)						
[3] AUDITSIZE	0.173**	0.172**	1.000				
	(0.019)	(0.020)					
[4] BLOCKHOLDER	-0.031	0.074	-0.017	1.000			
	(0.678)	(0.317)	(0.822)				
[5] FIRMSIZE	0.176**	0.319***	0.071	-0.245***	1.000		
	(0.017)	(0.000)	(0.340)	(0.001)			
[6] ROA	0.022	0.223***	0.158**	-0.012	0.189***	1.000	
	(0.765)	(0.002)	(0.032)	(0.868)	(0.010)		
[7] LEV	0.008	-0.122*	0.004	-0.236***	0.254***	0.036	1.000
	(0.914)	(0.099)	(0.960)	(0.001)	(0.001)	(0.624)	

Pearson correlation test is a test that measures the dependence and direction of the linear relationship between two random variables (real-valued vector) (Zhou et al., 2016).

4.2. Regression analysis

This study performs an empirical analysis to assess the effect of disclosure on corporate governance practice and ownership structure in mining companies listed on the Indonesian stock exchange from 2010 to 2014. This study uses Ordinary Least Square (OLS) regression model using STATA / MP 14.0 for doing regression analysis.

4.2.1. The influence of disclosure on corporate governance practice and the company's ownership structure

The following is the regression equation compiled by the author:

$$\textit{DISCLOSURE} = \alpha + \boldsymbol{\beta}_1.\text{BOARDSIZE} + \boldsymbol{\beta}_2.\text{ACSIZE} + \boldsymbol{\beta}_3.\text{BLOCK} + \boldsymbol{\beta}_4.\text{SIZE} + \boldsymbol{\beta}_5.\text{SIZE} + \boldsymbol{\beta}_6.\text{ROA} + \boldsymbol{\beta}_7.\text{LEV} + e$$

The results in Table 3 show that BOARDSIZE and AUDITSIZE as proxies of Corporate Governance have a positive significant influence on disclosure (DISCLOSURE). This is in accordance with the statement of Hartoko et al. (2012) where, in a company, to

Table 3: Regression Analysis.

Variables	Predicted Sign	DISCLOSURE	
		(1)	(2)
BOARDSIZE	+	0.006***	0.006***
		(2.68)	(3.16)
AUDITSIZE	+	0.021*	0.021***
		(1.89)	(2.68)
BLOCKHOLDER	-	-0.002	-0.002
		(-0.27)	(-0.33)
SIZE	+	0.004	0.004
		(1.18)	(1.15)
ROA	-	-0.000	-0.000
		(-0.89)	(-0.98)
LEV	+	0.000	0.000
		(0.07)	(0.11)
CONSTANT		0.441***	0.441***
		(7.46)	(7.22)
Year Dummies		Included	Included
Industries Dummies		Included	Included
Number of Observations		184	184
R-Squared		0.098	0.098
Adjusted R-Squared		0.045	0.045
F		1.872	2.113

improve a good corporate disclosure requires good corporate governance and conduct supervision and control of the board of directors, board of commissioners, audit committee, ownership structure, and financial disclosure.

However, BLOCKHOLDER as a proxy of the ownership structure has no significant effect on disclosures, which is in accordance with the results of Chau and Gray (2010), which also find non-linear relationships between corporate disclosure and blockholder ownership. So, in this case, the ownership structure has no effect on many of the least disclosures made by the company.

$$DISCLOSURE = \alpha + \beta_1.\text{BOARDSIZE x AFTER} + \beta_2.\text{ACSIZE x AFTER} + \beta_3.\text{BOARDSIZE} + \beta_4.\text{AFTER} + \beta_5.\text{BLOCK} + \beta_6.\text{ACSIZE} + \beta_7.\text{FIRMSIZE} + \beta_8.\text{ROA} + \beta_9.\text{LEV} + e$$

The results in Table 4 show the regression result from post implementation of Regulation of Minister of Energy and Mineral Resources Number 7 of 2012 and Regulation of the Minister of Finance Number 75 / PMK.011 / 2012, whereby the proxy corporate governance post the emergence of rules represented by BOARDSIZE x AFTER and

Table 4: Regression Analysis Post Emergence of Regulations related to Mining Companies.

Variable	Predicted Sign	DISCLOSURE		
		(1)	(2)	(3)
BOARDSIZE x AFTER	-	-0.000		0.000
		(-0.10)		(0.06)
AUDITSIZE x AFTER	-		-0.017	-0.017
			(-0.91)	(-0.90)
AFTER	+	0.005	0.052	0.050
		(0.12)	(0.88)	(0.79)
BOARDSIZE	+	0.006*	0.006**	0.006
		(1.83)	(2.47)	(1.60)
AUDITSIZE	+	0.024**	0.033**	0.033**
		(2.57)	(2.32)	(2.25)
BLOCKHOLDER	-	-0.001	-0.001	-0.001
		(-0.16)	(-0.19)	(-0.18)
FIRMSIZE	+	0.005	0.005	0.005
		(1.24)	(1.30)	(1.30)
ROA	-	-0.001	-0.001	-0.001
		(-1.53)	(-1.52)	(-1.54)
LEV	-	-0.000	-0.000	-0.000
		(-0.37)	(-0.44)	(-0.44)
CONSTANT		0.425***	0.397***	0.398***
		(6.17)	(5.13)	(5.12)
Number of Observation		146	146	146
R-Squared		0.101	0.104	0.104
Year dummies		Included	Included	Included
Industries Dummies		Included	Included	Included
R-Squared _a		0.035	0.038	0.031
F		1.776	1.750	1.628

AUDITSIZE x AFTER has no significant effect on disclosure (DISCLOSURE). Regulation of the ESDM minister and finance minister whose content prohibits the exporting of raw materials or mineral seeds before being processed in advance causes mining companies to process before they are exported and the processing activities of the company must incur additional costs, labor and capital from investors for support operational activities before goods are ready for export. When agents feel this information jeopardizes their competitive position in the marketplace, they will tend not to disclose the information (Darrough & Stoughton, 1990; Dye, 2001; Verrecchia, 2001).

5. Conclusions

Based on the test results that have been obtained and the discussion that has been explained in the previous chapter, several things can be concluded, as follows. Prior to the adoption of the ministerial rules about the audit committee, whether or not it has many, it may at least influence the extent of the disclosures of firms by providing oversight to company managers, which means Hypothesis 1a is accepted, while post-implementation of ministerial regulation about whether, at least, audit committee has no effect on the disclosure of a company. The size of the board is the sum of the board of commissioners and the board of directors. Prior to the emergence of the Minister of Energy and Mineral Resources Regulation No. 7 Year 2012 and Regulation of the Minister of Finance No. 75 / PMK.011 / 2012, the size of the board has a significant influence on disclosure, which means Hypothesis 1b is accepted. However, the regulatory readings indicate that the size of the board no longer has an effect on corporate disclosure. Before the Regulation of the Minister of Energy and Mineral Resources Number 7 Year 2012 and Regulation of the Minister of Finance Number 75 / PMK.011 / 2012, many of the ownership structures had no significant effect on the mining company disclosure activities, which means Hypothesis 2 is rejected. This is consistent with the findings by Chau and Gray (2010) who found a non-linear relationship between corporate disclosure and blockholder ownership.

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