

STAKEHOLDER POWER, SUSTAINABILITY REPORTING, AND CORPORATE GOVERNANCE : A CASE STUDY OF MANUFACTURING INDUSTRY AT INDONESIA'S STOCK EXCHANGE

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Abstract: *This research explains about the way the stakeholder power can affect the implementation of sustainability reporting and the corporate governance at a manufacturing industry in Indonesia listed on Indonesia's Stock Exchange. The results of this study are expected to provide an overview to prospective foreign investors who are interested in investing in Indonesia public companies which related to organizational behavior and governance style. However, there was less company that reported sustainability reporting continuously from 2007 up to 2016. This becomes a special and interesting concern to be investigated as the awareness phenomenon for the industries in Indonesia. With specified criteria found 60 observation data for 10 years and used multiple linear regression. The result showed that Government Control and Audit Control affected the implementation of Sustainability Reporting while the Internal control and shareholder control had no effect. The special note for shareholder control had a negative coefficient and it became a phenomenon for future research. Another finding was that the implementation of Sustainability Reporting and Government Control had an effect on good corporate governance.*

Keywords: *Stakeholder Power, Sustainability Reporting, Corporate Governance, Government Control, Audit Control.*

JEL Classification: *G30, G34, M14, M420.*

Introduction

In the last three years, Indonesia has made a great achievement in economic development by changing the consumptive policy into the productive policies in the period of Jokowi-JK Working Cabinet (Schwarz, 2015). Along with the economic growth from 2012 to 2017, some problems in the manufacturing industry such as infrastructure, certainly the workforce and labor problems, even though the company continues to grow. Until the research finding was done by United Nations Industrial Development Organization (UNIDO) showed that the global manufacturing industry at quartal III in 2012 grew only 0.2 percent compared to the previous years (Lestari and WSU, 2017).

At present many companies in countries such as France, Germany, Japan, the United Kingdom, and the United States, report environmental and social issues related to the company's commercial activities to their stakeholders (Burhan and Rahmanti, 2012; Ogundare, 2013) Likewise for manufacturing companies in Indonesia (Deswanto and Siregar, 2017). Global Reporting Initiative (GRI), as it provides a common ground for sustainability reporting, Brown, de Jong, and Levy, (2009) and has been very successful in terms of the adoption rate, comprehensiveness, prestige, and visibility (Loh, Thomas, and Wang, 2017). In Indonesia, one of the reporting models is Sustainability Reporting based on the Global Reporting Initiative (GRI)

(Ball and Bebbington, 2008). This awareness makes the role of the company very important in every progress towards sustainability (Gray, 1996). In 2005 there were only 10 companies, but in 2016 it had risen above 120 companies. Awareness of reporting on Sustainability Reports needs to be appreciated because it is not mandatory but still voluntary disclosure (Quick, 2008). This awareness can be caused by internal pressure such as company shareholders or the company's internal control system while external pressure can also occur and be carried out by the government and external auditors (Lu and Abeysekera, 2014; Agyei-mensah, 2016).

In the last three years, Indonesia has made a great achievement in economic development by changing the consumptive policy into the productive policies in the period of Jokowi-JK Working Cabinet (Schwarz, 2015). Along with the economic growth from 2012 to 2017, some problems in manufacturing industry such as infrastructure, certainly the workforce and labor problems, even though the company continues to grow. Until the research finding done by *United Nations Industrial Development Organization* (UNIDO) showed that the global manufacturing industry at quartal III in 2012 grew only 0.2 percent compared to the previous years (Lestari and WSU, 2017).

The impact of this pressure, investors reacted positively to the environmental performance achieved by the company reported in the Sustainability Report as part of the implementation of good corporate governance and able to increase company value. This is an interesting question, is it possible for manufacturing companies in Indonesia, that internal and external pressure through control activities can affect the reporting process or SR that they make voluntarily and whether it also has an influence on the implementation of Good Corporate Governance in the company. That was to answer if good corporate governance for all stakeholders cannot be underestimated (Lu & Abeysekera, 2014). A good company's system will ensure some vital points; they are openness and transparency to the shareholders and the regulator on risk management in a company (Elliott and Elliott, 2007). Openness and transparency to the shareholders will be made minimizing the asymmetry of information (Agyei-mensah, 2016).

1 Statement of a problem

The sustainable company's growth is reported through the voluntary disclosure done by a company in Indonesia; year by year, it becomes a trend for a company to inform the economic, social, and environmental performances, Deswanto & Siregar, (2017) and it becomes an awareness and a compliant for all stakeholders (Ball and Bebbington, 2008). For example, a company in China informs the economic, social, and environmental performances that had been done by the public company in 2008 after the issuance of social responsibility guidance or sustainability reporting from Shanghai Stock Exchange (SSE) in 2006 (Qiu, 2017). The sustainability reporting guidance also grows gradually such as a guidance from GRI (*General Reporting Index*) as suggested by Loh, Thomas, & Wang, (2017) also (Li *et al.*, 2018).

Disclosure of Sustainability Reporting in Indonesia is based on regulations relating to environmental and social responsibility in Law Number 40 of 2007 concerning Limited Liability Companies and until 2016 only 120 companies published Sustainability Reporting (Kurniawan, Sofyani and Rahmawati, 2018). In its

development, it has not been consistent in terms of publication of reports. Is it possible for company stakeholders in Indonesia to have an influence on disclosure of sustainability reports, as has been revealed in research conducted on companies in China by (Lu and Abeysekera, 2014).

Auditors are professionally influential in guiding their clients in initiating and promoting new accounting practices (e.g., social responsibility accounting) (Ahmad, Hassan and Mohammad, 2003). Although, Lu and Abeysekera,(2014) found that audit control could not affect the sustainability reporting disclosure. Nevertheless, according to Barrett (2005), the sustainability reporting disclosure could be well-arranged if there was an independent auditor who participated in the composition. The ownership of control in a company is the most important factor for the information of environmental disclosure (Haladu and Haliru Beri, 2016). However, the study in China revealed that the stakeholder power from the government had an impact on the sustainability reporting disclosure (Lu and Abeysekera, 2014).

Stakeholder perspective, which recognizes the ability of the government to influence corporate strategy and performance via regulations (Freeman, Wicks and Parmar, 2004). The results of the research conducted by Liu and V. Anbumozhi, (2009) found that the Chinese government had positive and significant influence on environmental disclosures. Meanwhile government control via regulations has no effect on voluntary disclosures on companies in Indonesia (Basuki and Patrioty, 2011).

Disperse corporate ownership increases pressure for management to disclose voluntary information (Ullmann, 1985). Previous studies have examined the power of shareholders to influence corporate social and environmental disclosure as part of Sustainability Reporting (Lu and Abeysekera, 2014). Government share ownership has an influence on voluntary disclosures for companies in Malaysia (Said, Zainuddin and Haron, 2009). Although voluntary disclosure for companies in Malaysia is still categorized as weak (Zain, Mustafa and Tamoi, 2006). In Indonesia, publication of sustainability report has started to become a trend, and has become from the interests of shareholders. Other factors are driven by the annual award of sustainability reports initiated by the National Center for Sustainability Reporting (NCSR) (Tarigan and Samuel, 2015).

This reflects that the stakeholder power lacks intervention or lacks control for company's internal party. It is important to be noted that corporate governance has a relation to the internal control (Agyei-mensah, 2016). Lack of good corporate governance in a country, such as the companies listed on Ghana's Stock Exchange, has resulted in a bad performance and a failure in a company (Agyemang and Castellini, 2015). Meanwhile, (Tristiarini¹, Utomo¹ and Setiawanta¹, 2019) have found that the corporate reputation measured by using corporate responsibility and corporate governance has a significant influence to market value.

The research on the relationship between sustainability reporting and corporate governance or corporate governance and the disclosure of sustainability reporting had been done by Mahmood, Kouser, Ali, Ahmad, & Salman (2018). They stated that the elements of corporate governance specifically were the size of the Board of directors, professionalism of the board of directors; even, the female director could affect and

increase the disclosure of sustainability reporting). However, Said, Zainuddin and Haron,.(2009) did not find such relationship at the company in Malaysia.

The disclosure of company's internal information and the company's elements is expected to give a motivation in achieving good company's performance for the attainment of good corporate governance (Lu and Abeysekera, 2014). By the existence of the problems occurred in manufacturing industries, the research gap found in this research, and the phenomena happened in international setting, then interested in investigating the empirical test on the stakeholder power toward the implementation of sustainability reporting and good corporate governance in the manufacturing industry listed on Indonesia's Stock Exchange that has reported their Sustainability Reporting transparently.

2 Methods

This research was conducted in several manufacturing companies listed on Indonesia's Stock Exchange within a period of 2007-2016. This research model used two models. The first model was aimed at testing the direct impact of Government Control, Auditor Control, Shareholder Control, and Internal Control toward Sustainability Reporting. Meanwhile, the second model was aimed at observing the implementation of Sustainability Reporting and Government Control toward corporate governance.

The control variable used here was the company size by considering that larger companies has implemented the principles of good corporate governance and disclosed the sustainability reporting. The company size in this research was measured by using natural logarithm from the company's total asset (Lu and Abeysekera, 2014; Mahmood *et al.*, 2018). The stakeholder theory focuses on the expectation of a certain interest group and the company that is persistent to widely serve the interest group will create a better value time by time (Harrison and Wicks, 2013)

This group has a variable characteristic and an impact level toward the company's activity (Lu and Abeysekera, 2014). According to Ullmann (1985), the characteristic and the impact level can be manifested as the stakeholder power and they have a capacity to affect the managerial decision strategy in form of control for resources needed by the company. Therefore, the strength of stakeholders consists of government control, auditor control, shareholder control and internal control that are considered capable of influencing the implementation of sustainability reporting and good corporate governance practices.

Tab. 1 : Measurement for each variable

No	Variabel	Measurement
1	Audit control*,** (independent variable)	1 for companies audited by big four and 0 for the opposite
2	Internal control** (independent variable)	(Actual disclosure / Total possible disclosure)
3	Government Control* (independent variable)	1 for companies owned by the government and 0 otherwise
4	Shareholder control* (independent variable)	Percentage of shares owned by the largest shareholder at the end of the year
5	Sustainability Reporting* (dependent/independent variable)	Disclosure Quantity in SR
6	Corporate Governance***(dependent variable)	Percentage of Managerial Ownerships
7	Firm Size* (control variable)	Natural logarithm of total assets

Source: Lu and Abeysekera, (2014)*; Agyei-mensah, (2016)**; Morck, Shleifer and Vishny, (1988)***

Based on the measurement of the variables in Tab. 1 above, the research model developed consisted of two models with the following equation :

$$ISR = \beta_0 + \beta_1GC + \beta_2AC + \beta_3SC + \beta_4IC + \varepsilon \dots\dots\dots(\text{Model I}) \quad (1)$$

$$CG = \beta_0 + \beta_5ISR + \beta_6GC + \varepsilon \dots\dots\dots(\text{Model II}) \quad (2)$$

A research done by Freeman (2004) stating that a perspective from the stakeholders admits the government’s capability to affect the company’s strategy and the performance through a regulation and also (Lu and Abeysekera, 2014). Government control has an effect on the disclosure implementation done by the company (Liu and V Anbumozhi, 2009). So, the hypothesis as follows:

H1: Government control can affect the implementation of sustainability reporting.

As a research was done by Taylo (1992), proving that the existence of a positive relationship between the auditor and the company’s disclosure in a gas and oil industry in Australia. In a study done in Malaysia, Ahmad, Hassan and Mohammad (2003) also found that the company audited by Big-5 auditor disclosed more environmental information in their annual report. Thereby, the hypothesis as follows:

H2: Auditor control can affect the implementation of sustainability reporting.

Keim (1978) states that the distribution of the company’s ownership becomes less concentrated; if the demand is put in a company by the shareholders, it becomes more. Disperse corporate ownership increases the pressure to disclose information on social responsibility (Ullmann, 1985b). Thereby, the hypothesis as follows:

H3: Shareholder control can affect the implementation of sustainability reporting.

The agency conflict is explained in the agency theory and it is proposed by Jensen and Meckling (1976) also believe that the agency theory also explains the reason why the manager discloses the internal control information voluntarily, and reported

through sustainability reporting so the stakeholders will understand the internal control of a company. Therefore, the hypothesis as follows:

H4: Internal control can affect the implementation of sustainability reporting.

The previous study also stated that corporate governance had a relationship to the disclosure or the implementation of sustainability reporting Mahmood, et al (2018). Theoretical arguments alone cannot unambiguously predict the relationship between management ownership (as corporate governance driver) and market valuation (Morck, Shleifer and Vishny, 1988). So, the hypothesis as below:

H5: The implementation of sustainability reporting can affect corporate governance.

A government will provide an intervention to the company's internal party if the company's internal party does an action that can damage the stakeholders as a case happened in China (Lu and Abeysekera, 2014). It is not only happened in China, but it is also happened in both developed countries and developing countries. Theoretically, the hypothesis as follows:

H6: Government control can affect corporate governance.

3 Problem solving

The classical assumption test referred to a definition proposed by Ghozali (2016) can be seen in Tab. 2.

Tab. 2 : Data Quality Test (Classic assumption test)

No	Variabel	Model I			Model II		
		VIF	Tolerance	t Glasjer	VIF	Tolerance	t Glasjer
1	GC	1,094	0,914	-1,794*	1,022	0,979	-0,671*
2	IC	1,049	0,953	0,484*			
3	AC	1,063	0,941	1,087*			
4	SC	1,094	0,905	-1,483*			
5	ISR	1,028	0,973	0,471*	1,015	0,985	0,238*
6	CG				1,014	0,986	1,047*

*. > 0,05;

Source : (Author's Result)

Based on Tab. 2, the significance value in the ANOVA table obtained a value of 0.000 that can be concluded that the two models used in this research were good. The value for the Kolmogorov-Smirnov normality test was 0.444 in the first model and 0.177 in the second model. It showed that both values exceeded a value of 0.05 and indicating that the data were normally distributed and appropriate to be used. Other classical assumption tests such as multicollinearity test If the VIF value is less than 10 and or the Tolerance value is more than 0.01 then it can be conclusively concluded that no multicollinearity problem has been proven from the VIF table column and Tolerance. Heteroscedasticity, if the significance value (Sig.)> 0.05 (glasjer collum) then there are no symptoms of heteroscedasticity, based on the table above the government control variable (GC) and shareholder control (SC) are still experiencing problems and are part of the limitations in this study.

Tab. 3. Model Fit of ANOVA^b

Model I	Sig
Regression	0.0000
Model II	Sig
Regression	0.0000

Source : (Author's Result)

Based on Tab. 3, the significance value in the Model Fit of ANOVA^b table obtained a value of 0,000 both for model I and model II, it can be concluded that the two models used in this study were good. To know whether an independent variable can affect the dependent variable positively or negatively, it can be seen from the t-test as follows:

Tab. 4 : Regression Results

Variabel	Model I		Model II	
	UCB	t statistik	UCB	t statistik
(Constant)	6,741	7,534	8,238	13,168
GC	0,679	2,282**	1,491	4,267***
IC	0,216	0,534		
AC	2,235	5,494***		
SC	-0,002	-0,222		
LnA	0,033	0,512	1,074	13,623***
ISR			0,571	1,677**
CG		7,153		64,576

Noted : *** Significant 1%; ** Significant 5%; * Significant 10%;
UCB = Unstandardized Coefficients Beta

Source : (Author's Result)

Based on Tab. 4, it can be explained that the first hypothesis can be accepted. It had been obtained a UCB value of 0.679, the t-statistic value of 2.282, at significance value below of 5%. The second hypothesis can be accepted since it had a UCB value of 2.235, the t-statistic value of 5.494, at significance value below of 1%. The third hypothesis could not be accepted since it had a UCB value of -0.002 and the t-statistic value of -0.222 with significance value above 10%. The fourth hypothesis could not be accepted since it had a UCB value of 0.216, the t-statistical value of 0.534 at significance value above 10%. The fifth hypothesis can be accepted since it had a UCB value of 0.571, a t-statistic value of 13.623, at a significance value below of 5%. The sixth hypothesis can be accepted since it had a UCB value of 1.491, the t-statistical t value of 4.267, and significance value below of 1%.

Tab. 5. Determinant Coefficient

Description	Adjusted R Square
Model I (Y1)	0,343
Model II (Y2)	0,764

Source : (Author's Result)

From the adjusted R Square at tabel 5 can be explained that the influence of Government Control (GC), Internal Control (IC), Auditor Control (AC) and Shareholder Control (SC) as model I, gives a value of 0.343 which can be interpreted

that Dependent latent variables can be explained by independent latent variables of 34.3%, while 65.7% is explained by other variables outside the study. And also at model II adjusted R Square gives a value of 0.764 which can be interpreted that Dependent latent variables can be explained by independent latent variables such as Government Control (GC) and Sustainability Reporting (ISR) of 76.4%, while 23.3% is explained by other variables outside the study

4 Discussion

First hypothesis of this research *accepted* and finding is in line with a statement by Freeman, Wicks, & Parmar (2004), stating that the perspective of the stakeholders who admit the government capability in affecting the company's strategy and performance through a regulation. In addition, this research finding is relevant to the finding by Liu and Anbumozhi (2009), stating that China's government can affect the disclosure of sustainability in form of accountability report toward their environment. Second hypothesis *Cannot accepted*, but the result is not relevant to the construction of the hypothesis as stated by Ahmad, Hassan and Mohammad (2003) which finding that a company audited by Big-5 auditor discloses more environmental information in their annual report and the society tends to see that a bigger audit company such as Big Four can be fairer and more independent (Choi and Kim, 2010).

Third hypothesis *could not be accepted*, it means that the corporation pays full attention to social responsibility (Qian and Xing, 2016). Even though the company's owners receive the information on the regulation of social responsibility disclosure, they could not perform the regulation optimally. Fourth hypothesis *could not be accepted*, it can be stated limitedly on the company sample that the effectiveness of internal control based on the perspective of stakeholder theory X. Li *et al.*, (2018) in the manufacturing companies in Indonesia was not able to be a good and optimal way in the process of sustainability reporting. Although the company's management had more freedom in choosing the method of accounting estimation (Hogan and Wilkins, 2008).

Fifth hypothesis *can be accepted*, it can be concluded that the implementation of sustainability reporting strongly affects the GCG dominantly. Since there are compulsory principles to be disclosed in the sustainability reporting such as equity, comparable, accurate, sequential based on appropriate time, and accountable, an entity that discloses the sustainability reporting can reflect that the entity implements good corporate governance (Lu and Abeysekera, 2014; Janggu *et al.*, 2014; Mahmood *et al.*, 2018). Sixth hypothesis *can be accepted*, it can be concluded if a governance control increases, GCG will also increase. It is because of the performance of an entity gives an effect to the economic performance in a country (Mantari and Nuryasman, 2017). Thereby, the company's internal party should be demanded to implement a correct and good corporate governance based on the principles of good corporate governance.

Conclusion

This study presents the current investigation towards the implementation of the issuer's sustainability reporting in the framework of legitimacy and the stakeholders in the companies existed Indonesia. The empirical findings provided an important perception of the effect of stakeholder power toward the sustainability reporting and GCG. Audit control Choi and Kim (2010) and governance control (Liu and

Anbumozhi, 2009; Freeman, 2004) were the variables that could affect the implementation of sustainability reporting and governance control (Lu and Abeyssekera, 2014; Mantari and Nuryasman, 2017). In addition, the implementation of sustainability reporting was the factor that could affect good corporate governance. This research finding is strongly consistent with the legitimacy theory due to the tendency of a company to comply the public supervision, such as a big company owned by the government and the company audited by the famous public accountant such as an auditor that belongs to the big four auditor.

This research also provides some unexpected yet thorough findings. As an example, the involvement of Big Four in financial audit also makes a substantial difference in the implementation of sustainability reporting. These findings provide a practical implication for the policymaker and other relevant stakeholders. When the Indonesian government and its institutions, as both a regulator or a facilitator, have not issued the regulation and the guidance yet in the process of composing the sustainability reporting, only several companies listed on Indonesia's Stock Exchange that have a willingness to voluntarily disclose the process of company's sustainability. Therefore, the Indonesian government needs to perform the sustainability attempt by providing guidance for the regulation and detailed guidance on the content and the level of sustainability reporting implementation. It aims to help the company in order to be able to communicate their social and environmental actions to the regulatory agency and other stakeholders.

This study provides a contribution in the literature about social and environmental accounting by enlarging the scope of the research that still exists at the social and environmental disclosure in the company's sustainability reporting for developing countries context i.e. Indonesia. Continuous evolution and increasing importance of sustainability concepts and practices among individuals, organizations and communities around the world it seems that it needs development conceptual approach to the theory of sustainability management for management applications, especially for public companies in Indonesia (Starik and Kanashiro, 2013).

However, this research finding should be interpreted by considering some limitations in this research. First, there were few numbers of the sample used in this research are limited. It can limit the finding implementation to the company that is not listed in this research. Secondly, even though the extensive attempt on the determinant choice and the accurate proxy development for various variables had been done, subjectivity could not be avoided. Thirdly, it was due to inadequacy number of companies that disclosed the sustainability reporting periodically year by year. The future research can consider other determinant factors that have more potency and uses a greater number of samples.

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