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Voluntary Disclosure and Earning Responses Coefficient and with Corporate Social Responsibility as Intervening Variable

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ABSTRACT

Objective – This research aims to find out how corporate social responsibility as an intervening variable on voluntary disclosure and earning responses coefficient.

Methodology/Technique – The research sample was retrieved from LQ45 companies listed on the Indonesia Stock Exchange which consistently disclosure annual reports and sustainability reports for the period of 2017-2018. In analyzing the data, Structural Equation Modelling (SEM) with the support of SmartPLS (Partial Least Square) are used.

Findings – Results show that voluntary disclosure has a positive and significant effect towards earning responses coefficient while voluntary disclosure has a negative effect towards corporate social responsibility. Moreover, corporate social responsibility also shows a negative effect towards Earning responses coefficient. Voluntary disclosure with corporate social responsibility as an intervening variable also shows a negative effect towards Earning responses coefficient.Voluntary disclosure can explain the variability of corporate social responsibility construct of 13,2%. Meanwhile, voluntary disclosure and corporate social responsibility can explain the variability of earning response coefficient construct of 22,7%, so that those two values are categorized as weak.

Novelty – The results indicate that investors did not pay attention to the information of ccorporate social responsibility (CSR) that are shown in the annual financial reports. However, they give a positive response to voluntary disclosure of the company so that it effects the increase of Earning response coefficient.

Type of Paper: Empirical

Keywords: Voluntary Disclosure; Corporate Social Responsibility; Earning Responses Coefficient.

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JEL Classification: G40, G41, G49.

1. Introduction

Financial statements are important information for investors, creditors, and other businessmen in decision making. Information presented in the financial statement state the management performance of a company in which the profit becomes the measure of success reported in the income statement.

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The company needs to gain the trust of the investors to get a positive response from them. It matters to assess the performance of the company not only based on the profits gained. The company will always look for business strategies to get market response. One way that can be done is through corporate social responsibility (CSR). By implementing CSR, the company is expected to gain social legitimacy and to maximize its financial strength in the long run. Kotler and Lee (2005), CSR is a company's commitment to improve the welfare of the community through wisdom in business practices and the contribution of company resources. If there is a disharmony between the company value system, the company will lose its legitimacy which will further threaten the company's value (Lindblom, 1994 in Haniffa et.al. 2005). There is a positive relationship between disclosure (including voluntary disclosure) and the company's market performance (Lang & Lundholm, 1993). Meek et.al (1995) said that the market for voluntary disclosure is free disclosure in which management can choose the type of information to be disclosed that is considered relevant for decision making for the users. Haggard et.al (2008) revealed that voluntary disclosure increases investor access to company specific information and results in an informative stock price. This indicates that companies that implement CSR are expected to be responded positively by investors in making decisions. The rate of change in returns or stock prices in response to earnings information can be measured using earning response coefficients (ERC). To improve the quality of corporate earnings, there are several factors that can influence earning response coefficients such as corporate social responsibility, timeliness, earnings persistence, capital structure, systematic risk and company size.

Sayekti et.al. (2007) provided empirical evidence that the level of CSR disclosure information in the company's annual report negatively affects the earning response coefficient. This is in line with the research of I Putu Sudarma, 2015 who proved that voluntary disclosure impacts negatively on the earnings response coefficient. Meanwhile, I Made Narsa, 2017 stated the different results on the company's manufacturing sector and wholesale-retail trade sector. The level of information of CSR disclosure has a positive effect on the earnings response coefficient in the company's manufacturing sector. While the CSR information disclosure level affected negatively on earnings response coefficient at wholesale-retail trade sector of the company. Kim et. al. (2012) stated that the relationship between CSR reporting and performance and earning respond was an important research question because of the inconsistency of the results of previous studies. Based on the explanation above, the problem in this research is formulated as following does voluntary disclosure affect earnings response coefficient, does voluntary disclosure affect CSR, does CSR has an effect on earning response coefficient and does the voluntary disclosure through CSR has an effect on earnings response coefficient. The purpose of this research is to find out and analyze the effect of voluntary disclosure and corporate social responsibility on earnings response coefficient on LQ45 companies listed on the Indonesia stock exchange for the period of 2017-2018.

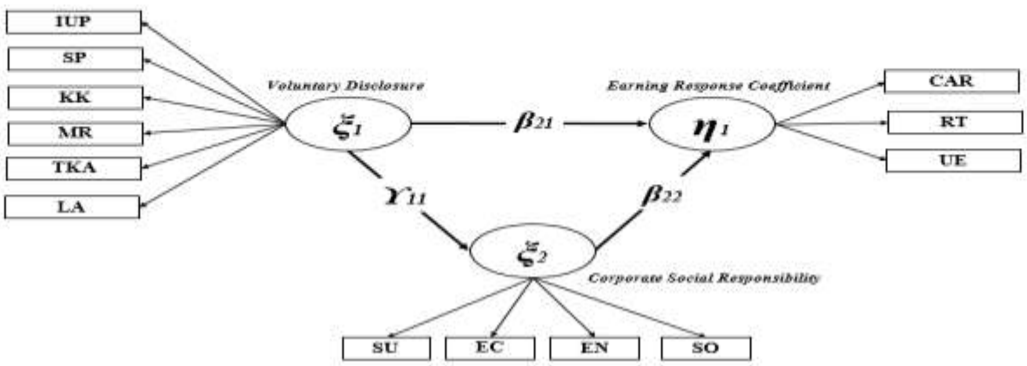
2. Literature Review

The relationship between investors and management gives rise to two problems namely information problem/asymmetry information and agency problem. With the emergence of these two problems, the role of annual financial statements has increased (Healy dan Palepu,2001). Based on legitimacy theory, the company has a contract with the community to carry out its activities based on the value of justice, and has to response to various interest groups to legitimize the company's actions. (Tilt, 1994 dalam Haniffa et.al 2005). Voluntary Disclosure is a free disclosure in which management can choose the type of information to be disclosed that is relevantly deemed for decision making for the wearer's parties (Meek et.al., 1995). There are three types of disclosure namely (Hendriksen, 2007) yaitu: (1) Adequate disclosure, (2) Fair disclosure and, (3) Full disclosure. It is often disclosed in the form ofan annual report. The annual report is one of the media used by the company to communicate directly with investors. According to Na'im and Rakhman (2000), the benefits of voluntary disclosure acquired by the companies are included: increasing the company's credibility, helping investors understand the business management strategy, attracting the attention of analysts to increase market accuracy, lowering market surprises and market information.Corporate social responsibility is a mechanism for an organization to voluntarily integrate environmental and social attention into its operations and interactions with stakeholders which exceeds the responsibility of the legal organization (Darwin, 2004).There are two theories used to predict the relationship between CSR performance and CSR disclosure, namely economic based theory and social political based theory (Clarkson et.al, 2008). Companies that implement CSR are expected to gain social legitimacy and maximize their financial strength in the long run. Corporate social responsibility is defined as a business commitment to contribute to sustainable economic development through the work of employees as well as their representatives, their families, the community as well as the general public to improve the quality of life in a way that is beneficial for both business and development (The World Business Council for Sustainable Development in Silalahi, (2014).CSR implementation affects the company's financial performance, this is consistent with Robinson and Pearce (2005) statement in which CSR implementation create savings so that it can increase profits.

Profit is believed to be the main information presented in the company's financial reports (Lev, 1989). In other words, the profit is reported to have a power of response. Strong market reaction to profit information is reflected from the high coefficient of profit response. Thus, in contrast, the market action to profit information will be reflected from the low earning response coefficient (ERC). It indicates the profit reported whether it is less or not qualified. The investor will give a good reaction to the company that is assessed to be able to maintain the corporate profit in the future. By using the earnings response coefficient, the information in the profit can be measured.Earning Response Coefficient is a large measure of abnormal return of a stake in response to the unexpected earnings component reported by the company that issued the stock (Scoot in Suryani 2017). Earning Response Coefficient measures how far the return stock in responding to profits reported by the company. In other words, there is a variation in the relationship between the company's profit and return.

3. Methodology

The population of this research was LQ45 companies listed on the Indonesia stock exchange. Samples were selected based on purposive sampling as many as 15 companies were selected that meet the criteria. Explanatory research was used in this research (Cooper and Bloomberg, 2008). Futher, the empirical analysis model used was Structural Equation Modelling with the SmartPLS (Parsial Least Square) program ver.3 (Chin, 1998). Design analysis used PLS (Partial Least Square) which showed the effect of voluntary disclosure on earning response coefficient through corporate social responsibility on LQ45 companies. Moreover, the component based structural equation model or variant visualized can be seen in the following figure.



Picture 1.Structural Equation Model

Notation:

ξ1	= Voluntary Disclosure	EC	= Economic Topic
ξ2	= CSR	EN	= Environment Topic

$\eta 1$	= Earning Response Coefficient	SO	= Social Topic
IUP	= Companies general information	CAR	= Cumulative Abnormal Return
SP	= Companies strategy	RT	= Annual Return
KK	= Financial performance	UE	= Unexpected Earning
MR	= Risk management	$\Upsilon 11$	= Coefficient $\xi 1$towards $\xi 2$
TKA	= Accounting policy review	$\beta 21$	= Coefficient $\xi 1$ towards$\eta 1$
LA	= Others	$\beta 22$	= Coefficient $\xi 2$ towards$\eta 1$
SU	= Universtal Standard		

Table 1 below indicated the measurement of the variables, scaling with related references of voluntary disclosure, Corporate Social responsibility and earning response coefficient.

Table 1. Operational Variables

Variable	Concept	Dimension	Indicator	Scale
Exogeneous: Voluntary Disclosure(X)	The disclosure that is not required by the regulation in which the company is free to choose the type of information to be disclosed to support the decision making (Sehar, et all: 2013)	Company's general information Company's strategy Risk management Accounting policy review Others	Company's general indicator Company's strategy indicator Financial performance indicator Risk management indicator Accounting policy review indicator Other indicators	Ratio
Exogeneous: Corporate Social Responsibility (Y)	Mechanisms for an organization to voluntarily integrate attention to the environment and social into its operations and interactions with stakeholders, which exceeds the responsibility of the organization in the field of law (Darwin, 2004)	Universal standard Spesific topic standard	Universal standard indicator Economic topic indicator Environmental topic indicator Social topic indicator	Ratio
Endogeneous: Earnings Response Coefficient (Z)	The power of stock prices in responding the companies' profits. (Brown, and Wayner, 1989 in Suryani, 2017)	Regression coefficient between stock price proaction and accounting profit	Proaction of stock price by measuring Cumulative Abnormal Return Proaction of accounting profit by measuring Expected Earning (EU). Proaction of additional annual return variables	Ratio

4. Results and Discussion

Two types of models formed in the structural equation model are the measurement model and the structural model. Two path diagram models were obtained, namely standardized model (PLS algorithm) and t-values model (bootstrapping).The testing ofthe measurement model consists of convergent validity and discriminant validity. The convergent validity includes an indicator of validity, construct reliability, and the Average Variance Extracted value. The results of the loading factor validity output for voluntary disclosure, CSR, and earnings response coefficient are ≥ 0.6. The t statistic's value for the correlation between indicators with the voluntary disclosure, CSR, and earnings response coefficient is above the requirement of 0.2. Thus, all of the indicators have significant validity.

The testing of convergent validity in which CSR and earnings response coefficient have a composite reliability value > 0.70. The value of Cronbach alpha is > 0.70, as well as the value of AVE is > 0.50. Thus, the whole of the construct can be said reliable. The testing of discriminant validity with a cross-loadings value between the indicators and the construct can be said having a good discriminant validity. Evaluation of the strength of predictive models of the exogenous latent conjugations by using Stone's-Geisser Q2 for Corporate Social Responsibility construct is 0.073 > 0 and Voluntary Disclosure is 0.008 > 0. It means that the latent construct of CSR has a good predictive relevance for the latent of earnings response coefficient construct.

The testing of the measurement model and the structural model can be seen from the value of Goodness of Fit (GoF) of 0.395. This value indicates that the combined performance of the model enters the moderate category falls into a large category.

Hypothesis Testing

From the application of SmartPLS Bootstrapping, the influence of voluntary disclosure with earnings response coefficient and voluntary disclosure with CSR and CSR on the earnings response coefficient can be seen in the table below.

Tabel 2. Path Coefficient Construct

	Original Sample (O)	**Sample Mean (M)**	**Standard Deviation (STDEV)**	**T Statistics (IO/STDEVI)**	**P Values**
VD -> ERC	0.240	0,218	0,179	1,341	0,046
VD ->CSR	-0.364	-0.363	0.181	1.903	0.048
CSR -> ERC	-0.442	-0.384	0.260	1.699	0.042

Source : Application of Run SmartPLS Bootstrapping

Fist Hypothesis H1: Voluntary disclosure has a positive effect on earning response coefficient.

From the table 2 above, it can be seen that Voluntary disclosure with the earnings response coefficient has a positive coefficient parameter of 0.240. These results proved that voluntary disclosure has a significant positive effect on earnings response coefficient and first hypothesis is accepted.

Second Hypothesis H2: Voluntary disclosure has a positive effect on corporate social responsibility

Voluntary disclosure with CSR has a parameter coefficient of-0.364. It can be seen from the table 2 above. This result indicates that the voluntary disclosure has a significant negative effect on CSR in which the second hypothesis is rejected.

Third Hypothesis H3: Corporate social responsibility has a positive effect on earning response coefficient.

From table 2 above, it can be seen that the influence of CSR with the earnings response coefficient has a parameter coefficient of-0.442. These results indicate that CSR has a negative effect and an impact on the earnings response coefficient so that third hypothesis is rejected.The amount of voluntary disclosure influence on CSR and earning response coefficient are represented in the table below:

Table 3. R Square (R2)

	R Square	**R Square Adjusted**
CSR	0.132	0.101
ERC	0.227	0.170

Source : Application of Run SmartPLS Algorithm

The influence of voluntary disclosure on CSR is 13.2%. This indicates that if the company does not conduct CSR activities then the company does not do voluntary disclosure in the annual report. As for the influence of voluntary disclosure of earnings response, coefficient is 22.7%. These results indicate if the company conducts CSR will be positively responded by the market indicated by the increasing earnings response coefficient. Voluntary disclosure can explain the variability of corporate social responsibility of 13.2% and Voluntary disclosure is able to explain the constructed variable of earning response coefficient is 22.4%. Referring to Chin (1998) these two grades are included in the weak category.

5. Conclusion

Based on the results of research, it can be concluded that voluntary disclosure effect positive and significant on earnings management with the percentage of 22.7%, while voluntary disclosure negatively affects CSR. In addition, the CSR relatively influences the profit response coefficient. The results of this research also proved that the voluntary disclosure through CSR also negatively affect the response of profit coefficient. Voluntary disclosure can explain the variability of CSR construct by 13.2%, while the Voluntary disclosure and CSR can explain the variability of the earnings response coefficient construct by 22.7%. The result of this research indicates that the investors do not appreciate the CSR information which is disclosed in the financial statement. However, the company will appreciate the voluntary disclosure indicated by the increase on earnings response coefficient.

The Implication for Management Study

The implications of this research are to provide information to the management study about the consistency in disclosing voluntary disclosure and corporate social responsibility in the annual report. Moreover, the sustainability report indicated can increase the corporate profit response coefficient. This research also contributed to the company's awareness to pay more attention to all aspects especially for environmental impact and employees' welfare in conducting its business. It is hoped that the company is not only seeking for profit. It is proven by the disclosure that the company will be more positively responded by the market because they are considered caring for the environment and the welfare of employees.

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