CHAPTER I

INTRODUCTION

1. Research Background

In 2020 the world was shocked by an outbreak of a disease called Coronavirus Disease 19 (Covid-19). The World Health Organization (WHO) declared Covid-19 as a disease outbreak on March 11, 2020. As a result of the Covid-19 pandemic, public awareness to invest in the capital market has begun to increase (Syahrizal Sidik, 2021). According to Pahlevi (2022), the number of capital market investors has increased by 93% in 2021. Otoritas Jasa Keuangan (OJK) or the Financial Services Authority recorded a total of 7.49 million investors by the end of 2021. In 2017, the number of capital market investors was recorded at 1.12 million. This number increased by 44% to 1.82 million in 2018. Furthermore, the number of investors increased another 53% to 2.48 million in 2019. In 2020, the number of investors increased by 56.2% to 3.88 million despite the pandemic.

Based on Siregar (2022) stock investors in the capital market of the Indonesian Stock Exchange (IDX) on December 10, 2021 increased by 99.09 percent of Single Investor Identification (SID) from the number at the end of last year. From the soaring increase in the number of investors, the financial statements on the stock trading exchange are useful information that can be used by stakeholders regarding their plans to make investments in capital market. This is a form of the company's disclosure principle to make open access to financial statement reports that go to all stakeholders.

In addition, the disclosure of the company’s financial statement reports is also influenced by the operation of enterprises in protecting the natural environment gaining increasing importance in the modern market economy. As stated by Trisnawati (2014), corporate environmental responsibility is a form of corporate social responsibility that supports business goals. A company must be able to take into account social and environmental factors implemented when planning and managing its activities. This is to explain the company's responsibility to protect the environment. Therefore, disclosure of the company will be a means for shareholders to obtain information about the financial and non-financial activities of an enterprise. For owners of capital, disclosure of the company can be the basis for assessing the company's performance.

The urgency of corporate disclosure was motivated by a phenomenon that occurred in 2006, namely the Lapindo Mudflow disaster in Sidoarjo, East Java, Indonesia. There are two general theories from geologists to answer the cause of the mudflow. The first opinion was obtained from the analysis that the mudflow was caused by an error in the gas drilling belonging to PT. Lapindo (Davies et al., 2008). The second opinion states that the mudflow was caused by the earthquake that hit Yogyakarta two days earlier, May 27 2006, and was not triggered by drilling activities (Mazzini, et al., 2007). The impact of this tragedy was that hot mud floods began to inundate rice fields, residential areas and industrial areas (Elika et al., 2017). As a result of the disaster, PT. Lapindo provided a form of social care and moral responsibility by buying land and houses for the drowning survivors. This is a social responsibility of PT. Lapindo (Amiruddin, 2018).

In addition, Malaysia which is a cognate country with Indonesia, is also very concerned about the implementation of Corporate Social Responsibility (CSR). However, the pattern that emerges in Malaysia is that CSR is more focused on concern and awareness in waste disposal. In this case, the supervision carried out by the Malaysian government is the environmental impact due to waste disposal, land burning, soil erosion or environmental damage. Companies are encouraged to disclose environmental conditions in their financial statements (Ahmad & Sulaiman, 2004). Therefore, CSR being carried out is not an obligation for companies, but Malaysia is quite orderly in that there is transparency in company reports in implementing CSR. As a result, Malaysian companies are active in CSR activities not only to comply with regulations, but especially to gain corporate image and competitive advantage (Mohd Razali et al., 2018).

These cases indicate that in both Indonesia and Malaysia, the corporate disclosure governance is still not well run, and it should be a concern for both authorities. Corporate Governance (CG) is about how public companies are structured and directed (Monks & Minow, 1995). CG is a system to direct the management of the company professionally based on the principles of transparency, accountability, responsibility, independence, fairness and equality and also the implementation of a good CG commitment depends on the company's mission of creating competitiveness to attract investors and issuers (IDX).

In Indonesia in 2013, the Financial Services Authority (OJK) with International Finance Corporate decided to establish a Corporate Governance Task Force (CGTF) to compile a road map for corporate governance in Indonesia. As for CG in Malaysia, the corporate governance guide was first published in 2009 by Bursa Malaysia to help companies listed on the exchange to better understand the listing requirements. So, corporate governance can be linked to Corporate Social Responsibility (CSR). A good financial statement is a report that not only presents the company's financial position, but also presents the company's accountability report to the company's environment.

Corporate responsibility towards the environment is also referred to as CSR of companies that carrying out CSR can easily ensure the continuity of the company's operations. In addition, companies will benefit more by conducting CSR practices and disclosures (Wiyuda & Pramono, 2017). The environment itself plays an important role in organization and internal accounting of both environmental and social environment of a company's activities or operations.

Aspects of CSR are aspects considered in business (Aburaya, 2017). Especially in the age of globalization, countries build their economies through industrial activities that process their own natural resources. Corporate advantages in an economy cannot be separated from the negative impacts of its operations. One of them is the environmental impact, such as pollution and ecosystem destruction as a result of manufacturing activities that generate industrial waste (Syuad Iman et al., 2021)

Allah SWT says in the Qur'an surah Ar-Rum verse 41

ظَهَرَ ٱلْفَسَادُ فِى ٱلْبَرِّ وَٱلْبَحْرِ بِمَا كَسَبَتْ أَيْدِى ٱلنَّاسِ لِيُذِيقَهُم بَعْضَ ٱلَّذِى عَمِلُوا۟
لَعَلَّهُمْ يَرْجِعُونَ

"Corruption has appeared throughout the land and sea by [reason of] what the hands of people have earned so He may let them taste part of [the consequence of] what they have done that perhaps they will return (to righteousness)."

This verse indicates how Allah has warned humanity to behave and take care of the environment as their responsibilities or else they will get harm by their own captivity.

Moreover, He states in the Qur'an surah Al-Maidah verse 2 which indicates how humanity must corporate in good deeds.

وَتَعَاوَنُوا عَلَى الْبِرِّ وَالتَّقْوَىٰ ۖ وَلَا تَعَاوَنُوا عَلَى
الْإِثْمِ وَالْعُدْوَانِ ۚ وَاتَّقُوا اللَّهَ ۖ إِنَّ اللَّهَ شَدِيدُ الْعِقَابِ

“And cooperate in righteousness and piety, but do not cooperate in sin and aggression. And fear Allah; indeed, Allah is severe in penalty.”

Also, in the Qur'an it is clearly stated that for Muslims, carrying out this help is an obligation and compulsion. The two verses explain that the Qur'an also explains the necessity to do good which is interpreted from the perspective of company as social responsibility and prohibits destructive actions on nature, especially as a result of the existence of corporations.

Although the phenomenon of CSR disclosure has been emerging for more than 2 (two) decades, research on CSR disclosure practices seems to be concentrated in the United States, the United Kingdom, and Australia. Research conducted in other countries such as Canada, Germany, Japan, New Zealand, Malaysia, Indonesia and Singapore are still relatively few (Hackston & Milne, 1996). Various studies that have been carried out have also shown mixed results. The variability of these results is partly because the model developed is a very simple one and the measurements used are also inconsistent (Sembiring, 2005).

CSR is a form of voluntary reporting as a form of social and environmental responsibility. It is very necessary so that stakeholders and the community know all forms of corporate responsibility to society and the environment (Sari & Marsono, 2013).

Good Corporate Governance (CGC) is a set of rules governing the relationship among shareholders, management of a company, creditors, governments, employees, stakeholders, and other internal and external matters relating to its rights and obligations, or in other words a system that directs and controls the company. Good Corporate Governance is included in the company's mechanism to make corporate governance more controlled. This mechanism aims to reduce the spread of agency problems (Xue & Hong, 2016). Good corporate governance is key to achieve success and corporate performance (Stuebs & Sun, 2015).

There are 4 (four) main components needed in the GCG concept, namely fairness, transparency, accountability, and responsibility. These four components are important because the implementation of the GCG concept is consistently proven to improve the quality of financial statements (Chtourou et al., 2001). In terms of studying good corporate governance based on Gillan (2006) facilities are displayed in two sides: The company's internal and external facilities.

The main concern of internal mechanisms is the board of directors, which oversees the operational and management processes, while external mechanisms include ownership structure, minority shareholder protection, and legal infrastructure (Gillan, 2006). The internal mechanism according to Elsye Hatane et al. (2019) is influenced by several internal company factors, one of which is the Board of Directors (BOD) and the Audit Committee (AC).

As claimed by Azmy et al. (2019) BOD is one of the parties in a company as the executor of the company's operations and management while the audit committee is an important attribute that can affect the value of the company. Leksono and Butar Butar, (2018) state that the CSR of 22 companies listed in Indonesia depends on the audit committee and also the characteristics of the company. The audit committee's primary role and responsibility is to ensure that corporate governance principles, particularly transparency and openness, are consistently and appropriately applied by senior management (Tjager et al., 2003).

Individuals elected as members of the Audit Committee must meet a number of audit committee criteria that can be examined through description, which contains Gender, Education and Expertise (Leksono and Butar Butar, 2018).

Corporate governance mechanism is a procedure and a clear relationship between the parties who took the decision and the parties who supervise or control the decision-making (Tricker, 2015). The board of directors is usually seen as the main mechanism of corporate governance and an important means by which shareholders oversee management activities (John & Senbet, 1998). Ratnawati (2019), state that board of directors' size is recognized as having an important role in the corporate governance process, so that they may have an impact on managers' risk taking behavior. Board diversity is also have an affect on risk taking decision, in which the more diverse directors will made variety of risks in decision making process through variety of viewpoints.

Audit committees are identified as effective means for corporate governance that reduce the potential for fraudulent financial reporting. Audit committees oversee the organization's management, internal and external auditors to protect and preserve the shareholders' equity and interests (Al-Baidhani, 2014).

According to previous research from Zaid et al. (2019) board size was positively and significantly associated with CSR disclosure, whereas gender diversity was positively, but not significantly, associated with CSR disclosure. Based on M. A. Harjoto et al. (2018), it is found that board education background is positively related to CSR. They also suggest that a diversity of educational backgrounds results in different priorities for ultimate business goals in board discussions and decision-making.

According to Pitenoei et al. (2022), audit committee gender diversity has a significant positive effect on the level of corporate responsibility disclosure. As claimed by Barroso-Castro et al. (2017), board education diversity has been documented to be a valuable resource for making strategic decisions such as: decisions regarding CSR disclosure. Based on Mohammadi et al. (2021), financial expertise of audit committee members has a significant effect on CSR.

This research refers to previous one. There is from (Zaid et al., 2019) with the title of "The Effect of Corporate Governance Practices on Corporate Social Responsibility Disclosure". Their study examines corporate governance practice on CSR disclosure. The contribution of this study is the board size variable and board gender variable. Besides, this study adds board education on another variable. The adding of Education variable on BOD is from Shatnawi et al. (2022).

Futhermore, this study refers to Pitenoei et al. (2022) with the title of "Audit Committee and CSR Disclosure: Does the Gender Diversity of Audit Committee Members Matter?". Their study examines the association between audit committee gender diversity and CSR disclosure. The contribution to this study is the AC gender.

The company's financial information as it is issued will assist the users of financial reports in making decisions. To practice good corporate governance, the audit committee must have sufficient knowledge and experience in accounting, finance and related regulations. Based on Blue Ribbon Committee (1999), the audit committee must have financial and accounting background. The Financial Services Authority requires at least one member of the audit committee to have an accounting and/or finance education and expertise. Audit committees work more effectively when members have financial and accounting experience. Therefore, this study adds AC education and AC expertise on another variables. AC expertise this study referes to is from Mohammadi et al. (2020).

In this study, the researcher want to juxtapose two country namely Indonesia and Malaysia. This is to determine the effect of corporate governance mechanism on the CSR disclosure. The researcher chose Indonesia and Malaysia as countries to be juxtapose because they have similarities in terms of natural resources and develop their economy and also the two countries have problems implementing

CSR, which is still low, due to the tendency that oil and gas companies only fulfill obligations (Tarjo et al. 2022). In this study the researcher chose energy sector because all companies have a responsibility towards the environment, especially companies in the energy sector which are directly responsible for the environment.

As said by Najeminur et al. (2021) the effectiveness of Corporate Social Responsibility (CSR) is considered to still need to be improved, this can be seen from the fact that there are still many companies that do not carry out programs as a form of social responsibility for the environment and society. This is because companies, especially in the energy sector, do not pay attention to environment and the community around the area, the company is too focused on pursuing profit targets so that environmental, social and economic impacts are ignored. In addition, the sampling is derived from the financial statements of the energy sector companies in Indonesia Stock Exchange and Bursa Malaysia by 2017 – 2021.

With this in mind, the researcher is interested in conducting a study entitled "The Effects of Corporate Governance Mechanism on the Disclosure of Corporate Social Responsibility (A Study Case on Indonesian and Malaysian Listing Companies)".

2. Research Question

Research questions are used as the foundation in explaining the problems in the background. They can be the basic assumptions for researcher to then formulate hypotheses, while the research questions in this research are:

1. Does the Board of Directors Size have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Indonesia?
2. Does the Board of Directors Size have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Malaysia?
3. Does the Board of Directors Education have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Indonesia?
4. Does the Board of Directors Education have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Malaysia?
5. Does the Board of Directors Gender have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Indonesia?

6. Does the Board of Directors Gender have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Malaysia?
7. Does the Audit Committee Gender have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Indonesia?
8. Does the Audit Committee Gender have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Malaysia?
9. Does the Audit Committee Education have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Indonesia?
10. Does the Audit Committee Education have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Malaysia?
11. Does the Audit Committee Expertise have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Indonesia?

12. Does the Audit Committee Expertise have positive significant effect on Corporate Social Responsibility Disclosure in the companies of Malaysia?

3. Research Objective

Research objective is an answer to research question as foundation in explaining the problems in the background, while the research in this research are:

1. To examine and find out the positive significant effect of Board of Directors Size on Corporate Social Responsibility Disclosure of energy sector companies listing in Indonesia.
2. To examine and find out the positive significant effect of Board of Directors Size on Corporate Social Responsibility Disclosure of energy sector companies listing in Malaysia.
3. To examine and find out the positive significant effect of Board of Directors Education on Corporate Social Responsibility Disclosure of energy sector companies listing in Indonesia.
4. To examine and find out the positive significant effect of Board of Directors Education on Corporate Social Responsibility Disclosure of energy sector companies listing in Malaysia.

5. To examine and find out the positive significant effect of Board of Directors Gender on Corporate Social Responsibility Disclosure of energy sector companies listing in Indonesia.
6. To examine and find out the positive significant effect of Board of Directors Gender on Corporate Social Responsibility Disclosure of energy sector companies listing in Malaysia.
7. To examine and find out the positive significant effect of Audit Committee Gender on Corporate Social Responsibility Disclosure of energy sector companies listing in Indonesia.
8. To examine and find out the positive significant effect of Audit Committee Gender on Corporate Social Responsibility Disclosure of energy sector companies listing in Malaysia.
9. To examine and find out the positive significant effect of Audit Committee Education on Corporate Social Responsibility Disclosure of energy sector companies listing in Indonesia.
10. To examine and find out the positive significant effect of Audit Committee Education on Corporate Social Responsibility Disclosure of energy sector companies listing in Malaysia.

11. To examine and find out the positive significant effect of Audit Committee Expertise on Corporate Social Responsibility Disclosure of energy sector companies listing in Indonesia.
12. To examine and find out the positive significant effect of Audit Committee Expertise on Corporate Social Responsibility Disclosure of energy sector companies listing in Malaysia.

4. Research Benefit

The following are the expected benefits of the research carried out:

1. Theoretical benefit

   This study is expected to provide a fairly important and comprehensive source of new thinking as academic evidence or literature that can be used as research for academics and businessmen interested in CSR and good corporate governance.

2. Practical benefit

   This research is hoped that it will be put to practical use as it will help companies, governments, researchers and investors to share their knowledge and perspectives on CSR and good corporate governance.

a. Company

The purpose of this study is to provide an overview of the impact of disclosure of corporate social responsibility, government ownership, or foreign ownership on company performance.

b. Government

The purpose of this study is to provide an overview for governments to understand how CSR disclosure regulations affect businesses and to enable governments to adopt or update these regulations. In addition, it is also important to understand how government ownership affects business performance.

c. Academics

This research is intended to be used as a brainstream, providing new insights, broadening knowledge, and becoming a consideration for further research for those exploring similar topics.

d. Investors

This research is expected to help investors analyze company performance.