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Effects of Stakeholder Engagement and Corporate Governance on Integrated Reporting Disclosure

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Abstract: Integrated reporting (IR), one of the latest developments in organizational reporting practices, collates important financial and non-financial information in an integrated and concise manner. This study aims to investigate the effects of stakeholder engagement and corporate governance on IR disclosure. In this study, stakeholder engagement was proxied by ownership concentration, the effective tax rate, leverage, and employee compensation, while corporate governance was proxied by the independent board of directors, frequency of audit committee meetings, and gender diversity. Using purposive sampling methods, the sample was selected from a population of companies listed on the LQ45 Index of the Indonesian Stock Exchange. A total of 22 companies that were consistently listed on the LQ45 index during the period 2013–2016 were selected. Panel data regression was employed to analyze the collected data. The results show that only employee compensation had a significant positive effect on IR disclosure while the other variables did not have any significant effect. The results of this study could be used to select the variables that companies must consider when preparing for their IR disclosure to stakeholder.

Keywords: corporate governance, gender diversity, integrated report, stakeholder engagement.

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INTRODUCTION

Corporate reporting is a responsibility of an entity to distribute the impact of activities and decisions to society and environment through transparent and ethical behavior (Jonikas, 2014). The responsibility of the organization not only responds to the negative factors affecting the organization's environment, but also evaluates more broadly the economy and the social impact.

An adoption of sustainability reporting (SR, hereafter) is considered as one of business initiatives that could be used for sustainable development. Three aspects of sustainability namely economic, environmental,

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and social are described as a corporate sustainability approach (Jonikas, 2014). SR has some weaknesses because it does not include financial reporting and fails to explain the relationship between sustainability issues with organization (Sirakaya-Turk et al., 2014). These weaknesses triggered the need of a new reporting approach namely, integrated reporting (IR, hereafter).

The IR is the latest development in organizational reporting practice which brings together material financial and non-financial information in an integrated and concise manner (IIRC, 2013). It is a single report that incorporates important elements of information that are now reported separately (financial, management, governance, remuneration, and sustainability). The IR comprehensively indicates the relationship among eight elements of the reporting, i.e. (1) strategic focus on future orientation, (2) connectivity of information, (3) stakeholder relationship, (4) materiality, (5) risk management practice, (6) consistency, (7) reliability and completeness, (8) consistency, comparability, and assurance. The IR explains how these elements can affect the ability of organizations to create and sustain value in the short, medium, and long term (IIRC, 2013).

The core concept of IR is to provide a single report that fully integrates corporate financial and non-financial information such as environmental, governance, and social issues (Eccles & Krzus, 2010; Eccles et al., 2011; PwC, 2013) based upon accountable and transparent information needed by stakeholders so that the company will eventually get support and legitimacy from its stakeholders. Moreover, IR emphasizes the importance of transparency in corporate reporting to gain public confidence (Eccles et al., 2011) and explains the impact of corporate decisions on the economy, social, and environment (Ashforth & Gibbs, 1990; Dowling & Pfeffer, 1975; O'Donovan, 2002).

In preparing the IR, the expectations and wishes of stakeholders were considered to establish its scope, boundaries, and applications (Deloitte, 2014). Therefore, some international guidelines such as the Institute of Social and Ethical Accountability, the Global Reporting Initiative (GRI) and the International Integrated Reporting Council put the stakeholder engagement as a key factor in the formation of the structure of IR (ACCA, 2017). Stakeholder engagement becomes critically important for IR as it can facilitate the identification and understanding of internal issues which generally cover stakeholder issues, concerns, needs, and expectations.

Every company needs to implement the concept of Corporate Governance (CG, hereafter), which contain a mechanism that can convince the principal of the agent's performance. CG is the process and structure in which a company's business is run by the management to improve the company's prosperity and accountability by taking into account the interests of its stakeholders for the sake of corporate sustainability. CG mechanisms can also provide a sense of trust to owners that the information disclosed in company reports made by the management is accountable information. Companies with good governance are more likely to disclose more voluntary information as an effort to meet the needs of stakeholders (Khan et al., 2013). Good Corporate Governance (GCG hereafter) implementation should be supported by corporate governance mechanisms, i.e., the General Meeting of Shareholders (AGMS) consisting of Directors, and Board of Director as the main organ of the company and assisted by audit committee, corporate secretary, and other committees within the company.

Internationally, over 1,000 companies have so far adopted IR practice (IIRC, 2016). However, research and literature related to the phenomenon of IR is very limited and focused on Anglo-American countries. Most countries in the other parts of the world do not require standard reporting in term of IR. In Indonesia, IR is still voluntary while financial reporting is mandatory (Suryono & Prastiwi, 2011).

The objective of this study was to provide empirical evidence on factors affecting the likelihood of a company to disclose IR. The object of this study was the companies belong to LQ-45 index in Indonesian Stock Exchange in the period of 2013–2016.

The study considered stakeholder engagement (proxied by ownership concentration, effective tax rate, leverage, and employee compensation) and corporate governance (proxied by independent board of director,

frequency of audit committee meeting and gender diversity in the board of director) in the model. Thus, there were seven variables to be considered in the multivariate statistical analysis. Based on literature review, the study began with hypotheses that all variables considered have positive effect on IR. The results of this study could be used for the selection of variables considered in the preparation of company's IR disclosure to stakeholder.

METHODS

The methodology adopted in this study was statistical analysis. The population of this study was selected public companies belongs to LQ-45 Index in Indonesia Stock Exchange for a period of 2013–2016. The companies belong to LQ-45 Index are considered the companies that practiced GCG because they have the highest market capitalization, the highest transaction value in the regular market for the last 12-month, good financial performance and high growth prospect. There were 60 companies belonging to this population.

A sample was chosen from this population using purposive sampling method. The criteria for choosing the sample are the companies consistently meet the criteria of the LQ-45 Index from 2013 to 2016. Samples that meet the criteria were 22 companies. Thus, the total number of samples were 88, i.e., 22 companies multiplied by 4 years. All the data were secondary in nature and most of them were collected from annual reports published in the period of 2013–2016 while the rest were from companies' websites.

The dependent variable of this study was IR disclosure. The IR disclosure is measured by a proxy using Integrated Reporting Score based on information provided by the company in the annual report (Lee & Yeo, 2016). This study utilized checklists designed by Abdifatah and Anifowose (2016) for their study which consists of eight main categories with a total of 52 items (question). The main categories are (1) strategic focus and future orientation, (2) connectivity of information, (3) stakeholder relationship, (4) materiality, (5) risk management practice, (6) consistency, (7) reliability and completeness, (8) consistency, comparability, and assurance.

The measurement of the IR disclosure is done by observing whether or not an item of information is provided in the annual report. If the item of information is not provided in the annual report, it is given a score of 0, and if the item of information is contained in the annual report, it is given a score of 1. IR disclosure score is computed as the ratio between the actual value earned by the firm compared to the total value based on the checklist.

Seven independent variables were considered in this study including Ownership Concentration (OC), Effective Tax Rate (ETR), Leverage (LEV), Employee Compensation (EC), Proportion Independent Board of Director (IBD), Frequency of Audit Committee Meeting (BDM), and Gender Diversity (GEN). The study was started with hypotheses that all variables considered in this have positive effect on IR. The following paragraph explains the definitions of each independent variables and the measurement method.

Ownership concentration (OC) is the largest share proportion owned by shareholders controlling the company which is measured by the largest share ownership percentage (Celenza & Rossi, 2013). The effective tax rate (ETR) is an effective corporate tax rate that reflects tax aggressiveness which can be calculated by dividing the income tax expense with profit before tax (Fernández-Rodríguez & Antonio, 2012). Leverage (LEV) is the company's ability to meet both short- and long-term financial obligations which can be seen through the leverage ratio, i.e., total liabilities divided by total assets (Suryono & Prastiwi, 2011). Employee compensation (EC) includes all payments (money or goods) to employees as remuneration from the company (Daft & Lane, 2010).

The independent board of directors (IBD) is a member of the board of directors who is not affiliated with the management, other members of the board of directors and the controlling shareholder, and is free from any

business relationship or other relationship that may affect his ability to behave independently (KNKG, 2006). This variable is measured by using the percentage of the number of independent directors divided by the total members of the board of directors. Previous study by Abdifatah and Anifowose (2016) shows significant positive association between the frequency of audit committee meeting (BDM) and the extent and quality of IR practice. Indonesia Stock Exchange requires that audit committee should hold at least four committee meetings in a year. Gender (GEN) diversity refers to the existence of women in the company, both as the board of director or as the directors. In this study score of 1 is given if there are women in the board and 0 (zero) if there are no women.

Data analysis employed a panel data model that is a combination of cross-section data and time-series data. Unlike the usual regression, panel data regression must go through the stages of determining the appropriate estimation model. Determination of model is done by applying Chow test, Hausman test and Lagrange multiplier test. Chow test was conducted to determine whether common effect model or fixed effect model is the appropriate model to estimate data panel model. Hausman test was employed to determine whether fixed effect model or random effect model is the appropriate model to estimate data panel model. Lagrange multiplier test is a test to determine whether random effect model is better than common effect model in order to estimate data panel models. The Lagrange multiplier test reveals that random effect model is appropriate to use. The results of the determination test were used to test the hypotheses.

RESULTS AND DISCUSSION

A panel data model, which is a combination of cross-section data and time-series data, was used to analyze the data collected from 22 companies during 2013–2016. The appropriate estimation model was selected through a series of tests, i.e., Chow test, Hausman test and Lagrange multiplier test. For this study, all three tests revealed that random effect model is the most appropriate to use for analysis.

The descriptive statistics of the IR and six independent variables collected from 22 companies listed in LQ45 index by Indonesian Stock Exchange are given in Table 1. To measure gender, a dummy variable is used. Following Kumar and Zattoni (2016), a value of 1 is granted if there are women in the board and 0 (zero) if there are none. The percentage of the sample having at least one woman on the board is shown in Figure 1. Table 1 indicates that the lowest standard deviation was found on EC while the most scattered data was on OC. As shown in Figure 1, 64% of the sample having at least one woman on the board and 36% having no woman on the board of directors.

Table 1 Descriptive Statistics

Variable	Mean	Max	Min	Std. Dev.
IR	69.9522	98.08	34.62	15.3554
OC	52.0524	85	10.17	18.2728
ETR	23.563	52.34	0.45	9.11782
LEV	43.0911	85.21	13.31	16.3365
EC	27.2805	29.83	23.98	1.33305
IBD	42.8814	83.33	28.57	12.9421
BDM	14.1136	59	4	13.9081

Source: Data Processed
Notes: IR, integrated reporting; OC, ownership concentration; ETR, effective tax rate; LEV, leverage; EC, employee compensation; IBD, proportion of independent board of director; BDM, frequency of board of director meeting

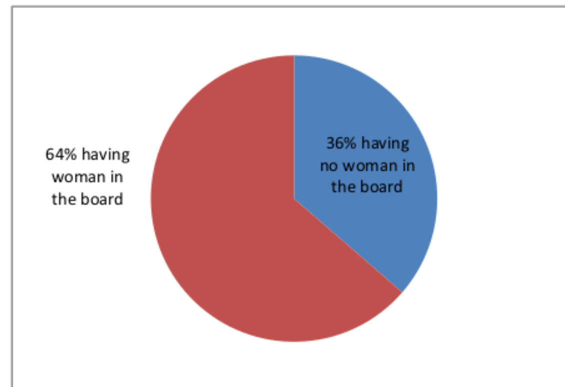

Figure 1 Gender Diversity

Table 2 Results of *t*-Test, *F*-Test and *R*-Square

Variable	Beta Coeff.	t-stat	P-value
IR	−47.220	−1.21	0.229
OC	−0.159	−0.88	0.379
ETR	−0.236	−1.80	0.075
LEV	−0.149	−1.10	0.271
EC	4.575	3.18	0.002
IBD	0.231	1.94	0.054
BDM	0.047	0.35	0.727
GEN	3.332	1.24	0.218
R-square: 0.122372			
F-statistics: 2.732980			
Prob *F*-statistics: 0.013527			

Source: Processed Data

The result of statistical tests including *t*-test, *F*-test and *R*-square on all variables is presented in Table 2.

Based on Table 2, the value of *R*-square is 0.1224. Thus, it can be concluded that the variable of OC, ETR, LEV, EC, IBD, BDM, and GEN are only able to explain the variability of the IR variable by 12.24%, while the other 87.76% is explained by other variables. The result of *F* test shows the value of *F* is equal 2.73 with *p*-value of 0.0135. Thus, it can be concluded that the OC, ETR, LEV, EC, IBD, BDM, and GEN simultaneously affect the IR.

The test results present in Table 2 shows that Ownership Concentration has a negative sign, thus does not affect IR. This result is contrary to the hypothesis made in this study and some previous publications. Darus et al. (2013) and Godos-Díez et al. (2014) suggested that there is a positive relationship between the concentration of ownership and the integrated disclosure report. However, this study agrees with Lourenço and Manuel (2013), which shows that there is no correlation between the concentration of shareholder ownership on the disclosure of the company environment.

Companies in Indonesia tend to be family companies, where it is normal that executives (boards and directors) are held by members of the family, given that company executives are selected by shareholders (who are also relative) in general meeting of shareholders. This situation makes the disclosure of integrated report is

considered as unimportant for the company. This happens because the information of ownership of shares that must be disclosed is a share ownership of more than 5% and ownership by corporate executives. The Company is not required to disclose ownership below that value because it is considered immaterial, except for the ownership of the board and directors which control the company. Therefore, it can be concluded that parties with high concentration of ownership can access the information needed directly to the company without going through the financial statements and annual reports. Furthermore, companies in Indonesia are also not required to disclose who the ultimate owner of the company is, so the public are not able to know who is at the top of the pyramid of ownership. Disclosure of this information is not required in company annual report although such disclosures may influence stakeholder decisions, especially investors of the firm.

The result of this study also reveals that effective tax rate does not affect IR. This finding is opposite to the study by Lanis and Richardson (2012) who concluded that tax aggressive companies tend to disclose additional information related to CSR activities in various fields in order to ease public attention and seek sympathy from the public. Positive correlation between ETR and CSR disclosure was also suggested by Zeng (2010). However, Davis et al. (2015) and Andrikopoulos and Kriklani (2013) studies concluded there was a negative relationship between ETR and CSR. This difference takes place because the treatment of companies that conduct tax aggressiveness depends on the countries. In some countries like Australia where Lanis and Richardson (2012) conducted their study, the company in their sample has been set by the country's tax authorities as a company that engages in tax aggressiveness. Therefore, this is in line with the theory of legitimacy, which indicates that if there is a discrepancy between the actions of the company and the expectations of society, the management of the company will make disclosure through annual reports to gain legitimacy.

The effect of leverage on IR as indicated by the statistical analysis in this study is not significant. It shows that the firm's leverage level does not affect the disclosure of the issuer's integrated report. This is in contrast to the research conducted by Andrikopoulos and Kriklani (2013), which states that there is a relationship between leverage with the disclosure of sustainability report of the company. A reason revealed by Kuzey and Uyar (2017) is that companies with high leverage is limited by the company's financial resources so that companies are more likely to focus on short-term goals than long-term goals. This is what makes the company regard sustainability reporting as a "luxury," rather than a long-term value-generating practice (Kuzey & Uyar, 2017).

Statistical test carried out in this study reveals that employee compensation has a positive effect on the disclosure of IR. This means that the greater the compensation received by company employee, the more disclosure of integrated report by the company. This study used the total part of the compensation received by employees in terms of basic salary and variable salaries in the form of annual bonuses, long-term incentives, and additional income nominally disclosed in the notes to the company's annual financial statements (Benoit, 2011). This finding is in line with the finding by Ogbonnaya et al. (2017), which states that employee satisfaction will motivate companies to disclose information about human resources in the company, where human capital is included in the integrated report. The results also agree with the survey conducted by Ernst & Young (2017) shows that employee is an important factor related to the sustainability of the company.

Employee satisfaction and employee engagement have a close relationship with IR (Ogbonnaya et al., 2017). According to Kruse (2012), if a company already has a good employee engagement, a situation where an employee is emotionally committed to the company and its goals, the company will have an edge. Employee compensation, as a measure of employee satisfaction with the firm, plays a role in shaping the involvement of company employees (Ogbonnaya et al., 2017). Employee engagement arises because they care and not just because they have to do something or to get compensation or to get promoted.

This study finds that there is no significant effect of proportion of independent board on IR. The result differs from the study conducted by Siregar and Rudyanto (2016) and Dharma and Nugroho (2013), which shows that there is an effect of the proportion of independent board on the quality of sustainability report disclosure. However, this study is in line with research conducted by Godoz Diez et al. (2013) which found that the proportion of independent board has no significant effect on the quality of corporate disclosure. The insignificant effect of independent board on IR may be due to relatively recent introduction of IR in Indonesia. The practice of IR has not gained attention from companies because the disclosure is not yet mandatory. This may also be due to the ability of independent boards to monitor the process of openness and information provision will be limited if the affiliated parties in the company dominate and control the board as a whole.

Based on the decision of the Financial Services Authority of Indonesia (OJK) Nomor 55/ POJK.04/2015 issued on December 23, 2015 (POJK, 2015) on the Establishment and Working Guidelines of the Audit Committee and Regulation of the Jakarta Stock Exchange, No: Kep-305/BEJ/07-2004 dated July 19, 2004, stating that audit committee meetings shall be held at least 4 times in a year or the Audit Committee shall convene meetings at least once every 3 (three) months.

The results of this study indicate that the number of audit committee meetings has no significance to the integrated report. This finding is not in agreement with the findings of other researchers. Jizi et al. (2014); Gantyowati and Nugraheni (2014) and Abdifatah and Anifowose (2016) who found that there was a positive correlation between the frequency of audit committee meetings and the company's voluntary disclosure. This difference in finding is made possible because the audit committee, in carrying out its function, cooperates with the company's internal control unit. This allows for ineffective meetings, where an issue discussed in audit committee meetings may actually be or may have been handled by the company's internal supervisor. Another possibility that causes the meeting to be less effective, is the duality of function in audit committee members. The dominance of votes from audit committee members concerned with personal or group interests may lead to ineffectiveness in audit committee meetings (Al-Najjar, 2012).

The empirical findings in the study indicate that the presence of women in the board of directors have no effect on the disclosure of the company's integrated report. The presence or representation of women in the company indicates that the company provides equal opportunities for everyone (no discrimination) so as to enhance the company's reputation (legitimacy). The result of this study differs from those of Lückerath-Rovers (2013); Fernandez-Feijoo et al. (2014), and Ben-Amar et al. (2017), who found that gender diversity positively influences the transparency of corporate disclosure, particularly sustainability issues, as an aspect of integrated report. Good corporate values can trigger companies to make more extensive disclosures. Other findings show that the presence of women in the board is also associated with greater transparency of information, especially on issues of sustainability (Ben-Amar et al., 2017; Fernandez-Feijoo et al., 2014).

It is a fact in Indonesia that women have difficulty when entering the business world (especially reflected in findings of this study). Environmental and cultural factors are more difficult factors than factors of the individual itself (the woman) in determining how certain it would be for her to reach the top management (Devillard et al., 2014). Even when women have been in business for a long time, sometimes their ability is still in doubt. A survey conducted by McKinsey & Company (Devillard et al., 2014) states that respondents, male executives, are not so sure if women can lead as effectively as men. Liberal feminism theory itself has emphasized the equality between men and women in self-development is related to women empowerment called by feminism (Whippman, 2016). Women empowerment makes women have confidence that their existence and decisions are not underestimated and equal with men. Some countries have implemented gender quota systems in the business organizations and politics to reduce this gap.

CONCLUSION

On the basis of the result of statistical analysis and examination on the influence of stakeholder engagement and corporate governance mechanism on the disclosure of integrated report of LQ-45 company listed in Indonesia Stock Exchange for a period between 2013 and 2016, the findings show that the only variable that has significant positive relationship with IR is the employee compensation. The other variables including the ownership concentration, effective tax rate, leverage, proportion independent board of director, the number of audit committee meetings and gender diversity have no effect on the disclosure of IR. The results of this study do not indicate that stakeholders have an influence on the disclosure by the company, and other parties in the company, such as the directors, board of directors and or other committees therein (which is part of the corporate governance mechanism) and have not contributed to the disclosure in the form of IR conducted by the company. The results of this study also reveal that the IR in Indonesia is fairly a new issue. Therefore, the company still has not paid attention to this new form of reporting. Not only that, IR and even sustainability reporting itself is still voluntary in Indonesia, therefore, the company feels no need to publish its report according to standard integrated report or sustainability report. But in some companies in the sample, the components contained in an integrated report have been disclosed in the company's annual report. This indicates that the company does not close the possibility of using integrated report in the future.

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