

CORPORATE SOCIAL RESPONSIBILITY : HOW DO INDONESIA'S PUBLIC COMPANIES RESPOND TO THIS DEMAND?

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ABSTRACT

Apparently, there is no other choice for the companies except to adopt the current public demand that is to implement corporate social responsibility (CSR). CLSA, in its survey shows that there are costs to be borne by companies that do not implement CSR. As the response of current public demand, Indonesian government through the Corporate Act No. 40, 2007 has mandated the companies which utilize natural resources to implement CSR. These companies should allocate certain cost to recover environmental and social aspect as a consequence of their action. The way the companies see the regulation will determines their response to the CSR Act. This study aims to describe how Indonesia's public companies respond to this act.

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I. INTRODUCTION

In line with the increasing of public awareness related to the sustainability of the world's next generation, the demand to conduct business ethically is also raising. Traditional paradigm views entities exist to create value to the shareholder. In their effort to create value, entities should not ignore their externalities which embed an obligation to redeem the impact of their operation to the environmental and social. As a consequence, focus of entities should not only to create value but a sustainable value which aimed to enhance wealth for shareholder and other legitimate parties.

The company success is not only assessed by the company's ability to create added value for its shareholders, but also the value added to every party affected directly or indirectly by the existence of the company. Measurement paradigm of the company's success has been switched from traditional financial bottom line to the triple bottom line in which include social and environmental performance measures (Norman & Chris, 2003)

According to Oekom Corporate Responsibility Review (2011), good sustainability ratings are increasingly being highlighted by companies in their external communications. Overviews of this kind can be found in a growing number of sustainability and business reports, and their mention in newspapers advertisements is no longer uncommon. Moreover, the researcher said that ratings thus make a positive contribution to the positioning and reputation of companies.

Demands of outside parties in respect to issues of social and environmental responsibility pour into the companies. It was also responded positively by Indonesian Government through a series of regulations as presented in Table 1 below, to support the implementation of social and environmental responsibility.

Table 1. List of Regulations to support CSR Implementation

No	Act no	Subject	Remarks
1	Kepmen Keu-RI No. 316/KMK 016/1994	Small Enterprise and Cooperation Development Program by Stated-Owned Enterprise (SOE)	
2	Kepmeneg BUMN No. Kep-236/MBU/2003	To support Kep Men Keu No 316/KMK 016/1994 i.e. Small Enterprise and Cooperation Development Program by Stated-Owned Enterprise (SOE)	Every company is mandated to allocate 1% up to 3% of after tax income to implement CSR

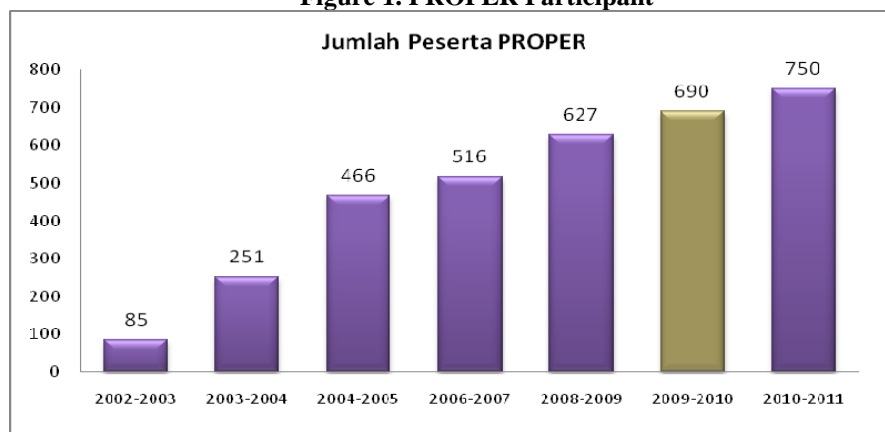
3	UU PT No. 40 Tahun 2007	Corporations	Article No. 74 stated that every company that runs its business activities related to the natural resources required to implement social and environmental responsibility. If it is not done, then the company is going to be punishable in accordance with the provisions of the legislation
4	UU No. 25 Tahun 2007	Foreign Investment Law	Law on foreign investment in Article 15 letter b is mentioned, every investor is obliged to implement corporate social responsibility. If not, then it can be subject to sanctions ranging from written warnings, restrictions on business activities, suspension of business activity and / or investment facilities, or revocation of business activities and / or investment facilities (Article 34 paragraph (1) of PM

(Source: Sukarmi, 2010)

Moreover, Indonesian Government through the Ministries of the Environment has been regularly, starting in 2002, held an annual program called PROPER (Performance Rating Company Program). Objective of this program is to assess performance of environmental management. The program involves three aspects of assessment that is liquid waste, emissions and waste management of B3, in addition to other aspects such as the implementation of the EIA, etc.

Company's enthusiasm to follow PROPER has been increased from year to year as depicted in Figure 1 below, unfortunately this did not parallel with awareness of public companies to report on sustainability reporting. Compared with the total companies listed on the Indonesia Stock Exchange (IDX) the proportion of companies that deliver sustainability reporting includes reports in social and environmental aspects, only 2.87%, 4.88% and 5.91% respectively for 2006, 2007 and 2008 (Sihotang and Subagio, 2010)

Figure 1. PROPER Participant



Source: PROPER Assessment Report 2010 [16]

Apparently, there is no other choice for the companies except to adopt the current public demand that is to implement corporate social responsibility (CSR). CLSA, in its survey shows that there are costs to be borne by companies that do not implement CSR. As the respond of current public demand, Indonesian government through the Corporate Act No. 40, 2007 has mandated the companies which utilize natural resources to implement CSR. These companies should allocate certain cost to recover environmental and social aspect as a consequence of their action.

This study aims to describe how the Indonesia's public companies respond to this act. The way they see the regulation will determines their responds in implementing CSR. Ones who see the law as government intervention, may just implement it formally, while companies who realize the positive side of the rule may enthusiastic in implementing CSR. Some indicators to

differ company's responds to the CSR Act are: the scope of CSR, board of directors' statement in adopting CSR as a part of the company's value/strategist, CSR disclosure and amounts (IDR) allocated for CSR.

II. LITERATURE BACKGROUND

A. *Corporate Social Responsibility*

There are some reasons why companies should implement CSR, especially in developing countries. First, growing concern that traditional development approaches were not effective, second, recognition of the impact of globalization and the increase of the flow of private capital into the developing world, and third, recognition that the private sector could make important contributions, which civil society and the public sector were lacking, including money, skills transfer, and in-kind contributions (Word Bank Document, 2006)

CSR is the company's commitment to account for the impact of its operations in the social, economic and environmental (L.Stuart and Mark, 2003) According to Welford (2009), CSR is about building relationships with customers, about attracting and retaining talented staff, about managing risk, and about assuring reputation. Meanwhile, at the same time, companies are required to enhance shareholder value. According to William (2011), corporate social responsibility programs attempt to merge two goals: adhering to high ethical standards while also enhancing profits. With CSR programs, companies find a way to integrate the needs of the community with programs and features that also boost its bottom line. It appears that the implementation of CSR does not interfere with the achievement of shareholder value, otherwise it will strongly support the achievement of shareholder value.

In his short research Adams et.al (2010) concludes that there is a harmonization between CSR and shareholder value. Companies which commit to implement CSR, indirectly was on the effort to achieve shareholder value. Therefore, CSR and shareholder value should not be viewed as something which opposite.

Many researches have also been proved the benefit of CSR implementation to the company performance. Among the results revealed that investors are ready to pay a premium for companies with good management of their relations with shareholders, clients and suppliers (Velde et.al, 2005) Firms with higher CSR scores enjoy significantly lower cost of equity capital (Sadok et.al 2010) Lu et.al (2009) indicate that CSR aspects of the "community involvement and environment" and "disclosure" dimensions have positive effects on financial performance, whereas the "employee and consumer interests" dimension positively influences non-financial performance. Moreover, Rettab et. al (2008) shows that CSR has a positive relationship with all three measures of organizational performance: financial performance, employee commitment, and corporate reputation. Further, Zur et.al (2009) suggests that an organization is able to better achieve a positional advantage and subsequent strong organizational performance through adoption of a corporate social responsibility (CSR).

Even though many research results have already proved the benefit of CSR implementation, but many companies are still skeptical with the CSR benefit, due to they perceive that CSR is expense that will reduce net income. Companies will gain positive impact if they perceive CSR as a long-term investment. Therefore by implementing CSR sustainably, companies will get a "place in the hearts and operational permits" from the community (Daniri, 2009)

B. *The Scope of Corporate Social Responsibility*

In the CSR's view, each company's processing embeds a responsibility to produce a positive impact to their society. Corporate social responsibility has a much broader scope, referring not just to specific efforts, but to a company's overall attitude toward its neighbors, customers, even the environment (Williams, 2009). Zur et.al (2009) proposed that four distinct and heterogeneous dimensions of CSR exist, i.e. an environmental capability, workplace capability, marketplace capability and societal capability. Regarding to environmental dimension, companies are required to manage their negative externalities, so that environment become safe to live in. The workplace capability dimension is focus on employee in which company is required to provide a safe and healthy workplace. To be sustainable, companies should maintain a long-term and ethical relationship with suppliers, customers and other business partners. Finally, companies are also required to involve short-term investments into the local community for the current generation as well as long-term investments into the local community for future generations.

Accordingly, the scope of CSR should represent the four dimensions of CSR, company cannot focus on part of the dimension but need to harmonize all the dimensions. Baker (2004) suggests that CSR scope is consist of union employee, customer, supplier, shareholder, local community, government and financial analyst.

C. *CSR Reporting*

Company need to communicate their achievement transparently to get a premium and reward from market (Baker, 2004). Corporate Act No. 40, 2007 explicitly requires that the companies engaged in natural resources have to carry out CSR (article 74 paragraph 1) and report their CSR on annual report (article 66 paragraph 2), nevertheless it is not followed by reporting standard. The reporting of CSR activities will vary among company's annual report. Usually, GRI requirement on CSR reporting was

adopted by Indonesia's public companies. According to Sihotang and Subagio (2010) only a few companies have submitted CSR reporting in their annual report. It is compared with the total companies listed on the Indonesia Stock Exchange (IDX).

The promulgation of CSR Act in Corporate Act No. 40, 2007 is expected to drive companies to disclose CSR on their annual report, but the goal presumably hard to achieve. First, due to there is no CSR Reporting Standard and second there is no evaluation about the objectivity of reporting by external parties. Companies tend to just fulfill the report requirement with less quality. Chapple and Moon (2005) in Utama (2007) reveal that only 24% of companies in Indonesia report their CSR activities which, in the study, are classified into 3 categories: community involvement, production process and labor relations which are socially accountable. The proportion of this is the lowest among other countries. Furthermore, among the companies reporting their CSR activities, the majority (73%) report low tide coverage (1-2 pages), 9% medium (3-10 pages), and 18% extensive (more than 10 pages).

According to Dan and J.Mack (2001) there are two primary reasons why traditional CSR programs have yielded only minimal benefits. First, CSR managers are usually given a fixed budget and encouraged to allocate the funds to a wide range of community-based charities, and second, corporate cash resources are allocated to social projects without taking advantage of the company's nonfinancial assets or thinking about how the social projects could directly support business objectives.

CSR is different with corporate philanthropy, which usually intended to enhance a company's image. Also, corporate philanthropy generally separate from a corporation's long-term business strategy, and has less effect on the organization's bottom line and ability to attract customers (Williams, 2011). Companies concern to implement CSR can be implied from where they put CSR program, is it under CSR strategist or corporate philanthropy program. By adopting CSR as part of company's strategist, companies intend to deliver information that they just not engaged activities for only self serving purposes (Meranus, 2010)

III. RESEARCH METHOD

A. *Indicators to Differ Company Response to the CSR Act*

In this research, data will be processed using descriptive statistic to show how the company's response to the CSR Act. The company's response to the CSR Act will be deferred through four indicators. The first indicator is CSR scope. According to Welford (2009) CSR is about building relationships with customers, about attracting and retaining talented staff, about managing risk, and about assuring reputation. Zur et.al (2009) suggests that CSR should cover for dimensions i.e. environmental, workplace, marketplace and societal dimensions. Therefore the scope of CSR of companies studied should include local communities, employee, work environment, customer and vendor. Companies that have a positive response will implement the CSR in a broader scope than those undertaken by companies who responded negatively.

The second indicator to differ company's response is the board of directors (BOD) statement that CSR become part of a strategy or value of the companies. Companies that perceive the CSR Act positively will integrate CSR in the companies' strategist [Dan and J. Mack 2001, Meranus 2010, Williams 2011]. While companies that perceive negatively, they may implement activities that are sporadic, short-term and merely to meet regulation. Hence, such companies do not adopt CSR as a part of the company's strategist.

The third indicator is CSR disclosure. Companies that view the CSR Act positively will disclose their CSR activities. While the companies that have a negative view on CSR Act ignore to make additional effort to disclose CSR in their annual reports. Refer to finding Chapple and Moon (2005) in Utama (2007) in this research, CSR disclosures are classified into three levels, i.e. low (1-2 pages), medium (3-10 pages) and extensive (more than 10 pages). Companies will be categorized into positive response if they have medium or extensive level of CSR disclosure, and negative response if the CSR disclosure level is low.

The final indicator to differ company's response is disclosure of CSR amount. The disclosure of amount of CSR in the annual report indicates the seriousness of the company to comply CSR Act. It is expected that companies who response positively will be willing to disclose information regarding the amounts of fund allocated to support CSR. Company that qualify at least three of the above four indicators will be categorized into a positive response group other than will be categorized into negative response group.

B. *Research Sample*

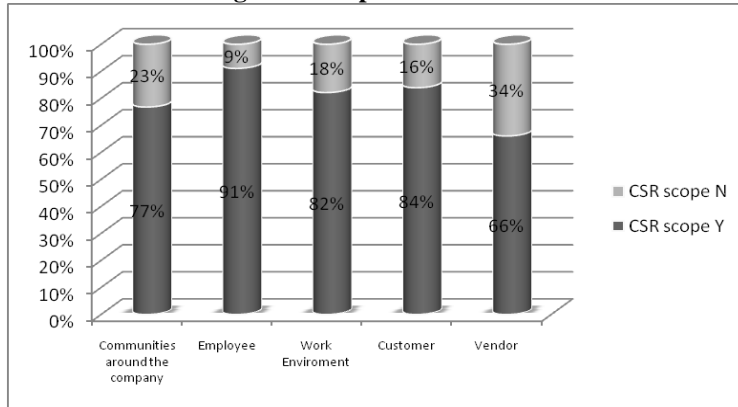
Since the purpose of this research is to describe how Indonesia's public companies respond to the CSR Act, which was promulgated in 2007, therefore research sample selected is two years after the promulgation that is year 2008 and 2009. Total companies that their annual report available on ICMD during 2008 and 2009 are 170 companies. Companies that run its business activities related to the natural resources and their annual report available during 2008 and 2009 are selected as a research sample. The selection result is obtained as many as 56 companies meet with the criteria as the research sample.

IV. DISCUSSION

A. Company Response to The CSR Act

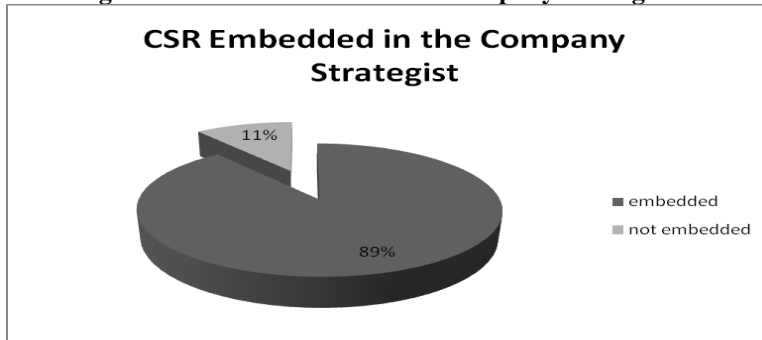
Since CSR Act has been promulgated, it seem, there is no choice for Indonesia's public companies except comply this act otherwise they will be punished. Though some companies still consider that the regulation is a liability for them, yet on the other hand they have an interest to comply with this demand. Figure 2 shows the response of the companies to the CSR Act from the scope of CSR. More than 50% of companies have a wider scope of CSR including local communities, employee, work environment, customer and vendor. The first priority of CSR scope is employee (91%), followed by customer (84%) and work environment (82%). The lowest priority is vendor (66%). The company concern to the internal scope is supported by Welford (2009) that suggest real investment in people and communities will help company to become self-sufficient and communities more sustainable. It is also consistent with the Hartanti finding (2003) in Utama (2007) that the majority of the disclosure is on the product, labor, and followed by community involvement, environment and the last one is energy.

Figure 2. Scope of CSR



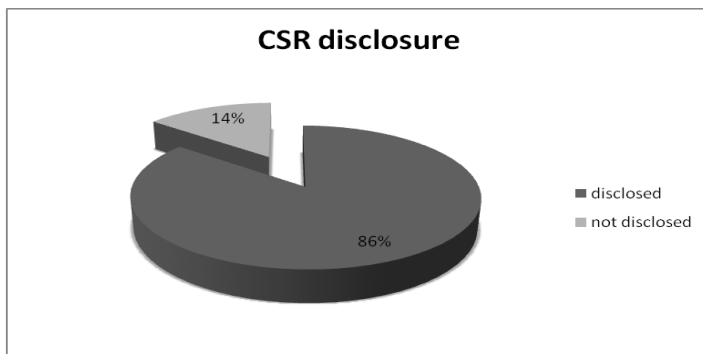
As much as 89% of the companies have already embedded the CSR into the companies strategist, it prove that CSR implementation is just not philanthropy or short term but it will be implemented continuously.

Figure 3. CSR Embedded in the Company Strategist



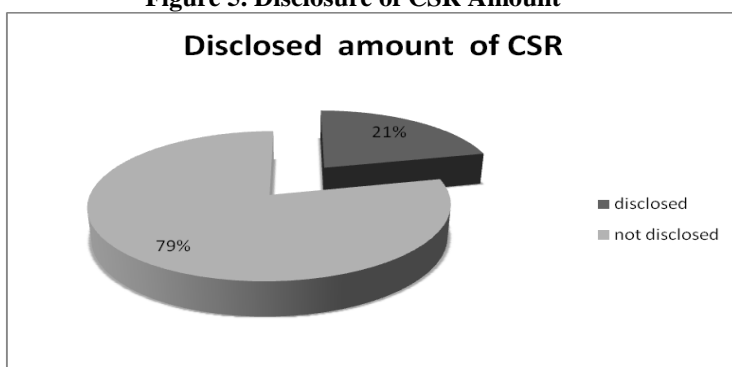
Company's concern to the CSR demand has also followed by CSR disclosure. This disclosure shows the company's policy, activities, and performance in implementing CSR. Only 14% do not report their CSR in their annual report, and the rest, amounting to 86% have already disclosed it, as presented in Figure 4. Companies which do not include CSR in their annual report indicate they have less concern to the current public demand. Some companies still consider that CSR is costly so they try not to implement it properly. Moreover there is no strong pressure from the outside parties to the companies that do not comply with CSR in their business practice, since the outside parties get benefit from the companies that do not comply with CSR through the low price (Utama 2007)

Figure 4. CSR Disclosure



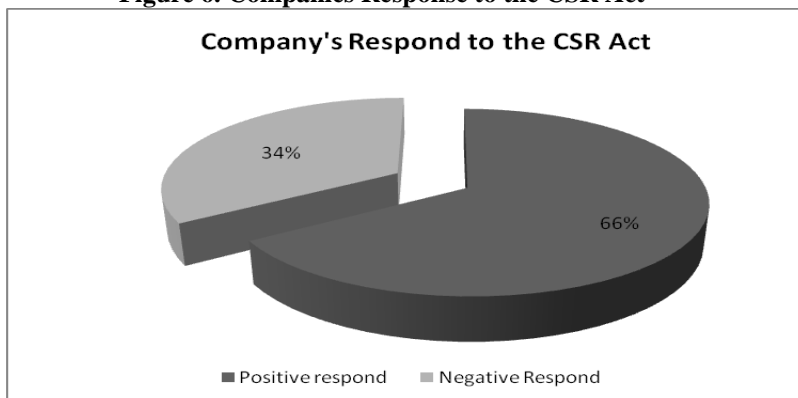
The above three indicators that used to measure companies respond to the CSR show that almost all companies have positive response to the CSR, which indicated by a high percentage of each of indicators that used to differ company response. Nevertheless, most of companies do not disclose how much money they allocate to support CSR (79%). Only 21 % of the companies disclose their CSR, as presented on Figure 5.

Figure 5. Disclosure of CSR Amount



Based on the company compliance on each indicator above, thus companies response to the CSR Act are categorized into two types, that is positive and negative response groups as shown in Figure 6. As much as 66% of the sample companies have a positive response and the rest, 34% have a negative response. Majority of companies have positive response to the CSR Act, however the result cannot be used to justify that the CSR Act success in increasing the compliance of CSR implementation. The possibility reasons why companies comply to the rules are to avoid the punishment, to assure outside parties that companies run their business ethically and not merely for self serving purposes, and to attract good reputation from their stakeholder.

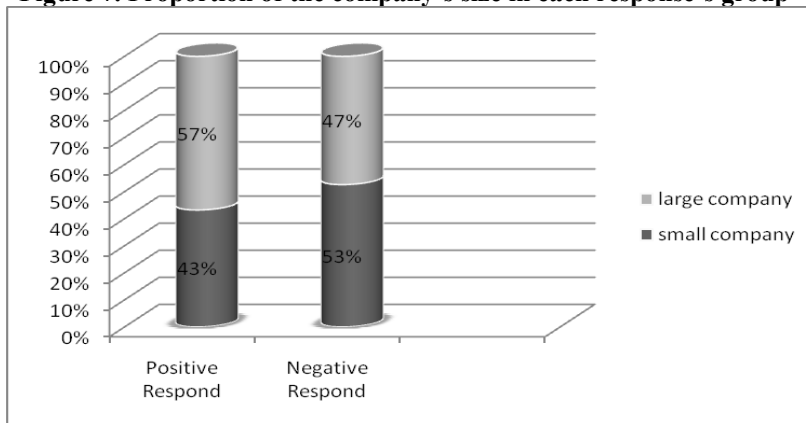
Figure 6. Companies Response to the CSR Act



B. CSR Response , Company's size and Company's age

Big companies usually experience higher pressure from their stakeholder than small companies. Therefore big companies tend to more comply with the regulation, especially when it seems to be one of their stakeholder's interests. Big companies also have interested to assure that they just not engaged activities for only self serving purposes (Meranus, 2010) The greater part of the companies with positive response should be big companies. After classifying company size using their total assets (Basu 1997) into big and small companies, then calculated the composition of firm size in each group that is positive and negative responses. The result is presented in Figure 7.

Figure 7. Proportion of the company's size in each response's group

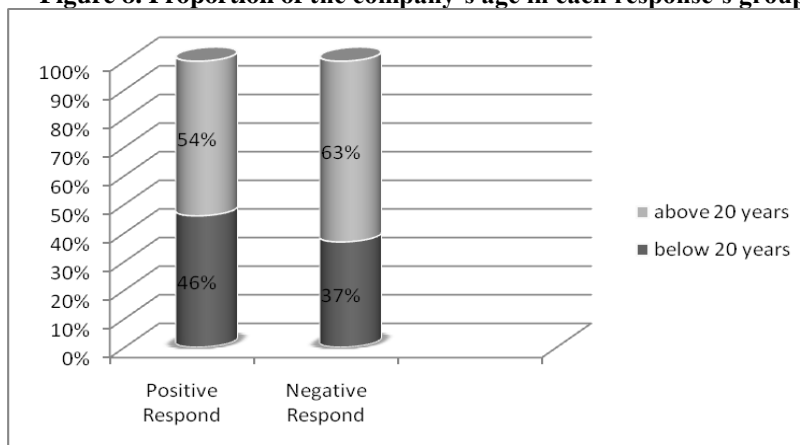


The result confirms that most of the company's size of a positive response group is big companies, as much as 57%, and only 47% of the negative response groups is big companies. This indicates that big companies more comply with the CSR Act than small companies.

Furthermore, company's age of each response also need to be observed to get inside whether certain age group has a similar response to the CSR Act. Years of operation is used to classify company age, the average age of companies in this research is 23 years. Then based on company age, companies are grouped into two group i.e. below 23 years (growth company) and above 23 years (mature/established company).

The proportion of company's age from the positive response group should be dominated by age company group above 23 years and below 23 years for the group of companies that have a negative response. However Figure 8 shows the different results. This result do not indicate that company age differ company response to the CSR Act. Company age of the positive response groups is indeed dominated by age groups above 23 years (54%), however that is not supported by the result of the negative response group. To be consistent with the results of positive response group, company age of the negative response group should be dominated by age below 23 years (37%), instead of above 23 years. In fact, as presented in Figure 8, the opposite conditions exist, 64% of the group having a negative response is dominated by age group above 23 years. This is shown that company age do not differ a company response.

Figure 8. Proportion of the company's age in each response's group



V. CONCLUSION AND LIMITATION

This research is aimed to describe how Indonesia's public companies respond to the CSR Act. The results conclude that majority of companies sample respond positively to the CSR Act, as much as 66% and the rest, as much as 34% respond negatively. The positive companies response groups are at least qualify three of four indicators of the company response i.e. CSR scope, the BOD's statement that CSR is a part of company's strategit, CSR disclosure and CSR amount disclosure.

Further, company size has contribution to the company's response, big companies, generally have a positive view to the CSR than small companies. It proved by 57% company's size of positive response group is big companies, on the other hand majority of company's size from the negative response group is small companies (53%). While, company's age has no similar pattern in both of groups' response, it is indicated that company's age cannot be used to predict company's response.

However the conclusion that most of companies respond positively cannot used to justify the success of CSR Act in driving companies to comply CSR implementation. It is needed to conduct further study to prove it.

Some limitations of this research may constraint the proper description of the company's response, first, the research samples do not cover all companies that have already implemented CSR, because data is not available. The evaluation of company's response to the CSR Act is only based on data on annual report, and not confirmed it with another sources such as inquiry, confirmation with stakeholder etc. Further study need to be conducted in area of this research limitation to get a comprehensive picture of the company's response to the CSR Act.

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