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CHAPTER 2

REVIEW OF RELATED LITERATURE

This chapter will explain what theories were used to build this research, previous research that has a relationship with the topic of this thesis, research framework, and hypotheses formulation. The content of this chapter is very important because it is a reference to the thinking of this research.

The theoretical foundation will contain relevant concepts or theories to support the discussion and analysis of the research. Previous research will contain the results of previous research related to this research obtained from journals, theses, thesis, and dissertations. The research framework is a mindset that shows the relationship of the variables studied, in the form of schemes and brief descriptions. For the hypothesis formulation, they contain temporary presumptions that is later proven as the research proceeds, those hypotheses refer to the research framework.

A. Theoretical Framework

1. Signaling Theory

According to signaling theory, the owner is informed of managerial success or failure using signals. Information asymmetry is connected to signaling theory. The asymmetric information issue is solved by signaling, in which the knowledgeable party informs the uninformed party of an unobservable quality of the product. The advantage of the signaling theory is that it separates businesses with "positive news" from those without by informing the market of their

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circumstances. The market won't accept a company's signal of strong future performance if its prior financial performance has been below par (Wolk and Tearney, 1997).

One of the foundational theories for comprehending financial management is the signaling theory. Typically, the signal is viewed as a signal sent to third parties such as investors by the business, usually by the management department. These signals can appear in a variety of ways, including those that can be seen immediately and those that call for further investigation. The signals are all intended to imply something, regardless of their form or content, in the hopes that the market or other parties will change how much the business is valued. Or, to put it another way, the indication of choice must be strong enough to change the perception of the organization among outsiders.

Signal theory and a company's financial performance have a link that is the expanded transparency will send a favorable message to the interested parties in the business such as stakeholders as well as the company's shareholders. A firm can generate more trust from stakeholders if they convey a wider scope of information to the stakeholders. Stakeholders show their confidence in a company by purchasing its goods, which helps the company increase its profits and Return on Equity (ROE).

In economics and finance literature, signal theory is used to explicitly demonstrate evidence that insiders frequently have more information about a company's status and future prospects than outsiders. For instance, shareholders, creditors, the government, or even investors. In other words, the corporation has the upper hand over outside parties who have an interest in the company in terms of information mastery. Information asymmetry, as used in financial theory, describes

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the circumstance in which one entity has access to a wealth of information while the other does not.

The primary focus of signaling theory, in contrast, is on the intentional actions insiders take to deliberately convey their positive, undetectable traits. While not all visible behaviors adopted by insiders can be interpreted as signals, they may overpower outsiders with them. However, effective communications share two key characteristics. The first is signal observability, or how easily someone else can see the signal. If insiders' actions are not readily apparent to outsiders, it is difficult to use them to interact with receivers.

The company's disclosure of its corporate social responsibility in the annual report expands on the connection between signaling theory and firm worth. By doing this, the company is promoting itself to investors. The more disclosure the business makes, the more information investors will learn. As more information becomes available, investor faith in the business will increase. If investors have a high level of confidence, they will undoubtedly react favorably to the business with rising stock prices. As a result, the amount of information the business discloses will affect how quickly stock prices change, which in turn will affect how much is traded. Rising stock price changes will surely have an impact on the corporation's increased stock return (Connelly, 2010).

Akerlof (1970) gives a simple but illuminating illustration of the importance of signals to distinguish a company's positive traits from those of rival businesses. Businesses of higher quality need to be creative and daring enough to use certain cues that indicate they are better than other businesses of lower quality. Applying an indication is one strategy managers can use. This can be costly, but it can still be

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done by their company. This is too costly for low-quality businesses to do, so they won't be able to do it or copy it.

Signaling theory suggests how companies signal to users of their financial statements. Appropriate disclosure of corporate social responsibility, in line with stakeholder expectations, can help management communicate to the public a positive view that the company has good prospects for the future and that sustainable development is assured. This theory is based on the idea that a firm's managerial actions can provide positive signals by maximizing benefits to stakeholders, in the form of information about what management has done to further the interests of investors and the public. The importance of information presented as announcements signaling investors to make investment decisions.

2. Agency Theory

The agency theory of company governance was put forth by Alchian and Demsetz (1972) and Jensen (1976) respectively. They proposed that firms might be seen as a center for a collection of contractual connections between individuals, as opposed to the way businesses are viewed in traditional economics, which views them as entities with a single product and a single aim of maximizing profit. Businesses can be viewed as contracts that are constantly negotiated by various parties who each want to optimize their own profit, according to Learmount (2002).

According to Shleifer and Vishny (1997), agency theory uses the perspectives of multiple contracts between different parties to describe how a corporation behaves. Instead of the company's owners, investors who contribute money to its activities are seen as taking risks. In the real world, managers of businesses are given financing by investors who have faith in their ability to use the

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funds wisely and profitably for the companies. The contracts that the managers execute specify the obligations they must fulfill as well as the profit distribution schedule. The contracts that managers sign are difficult to put into practice because it is extremely difficult to specify and anticipate possible future contingencies. Managers are therefore granted the power to make choices that are not governed by their employment agreements. Everyone tends to make decisions that are in their own best interests, and supervisors are not an exception. They will make decisions that are in their best interests and pay little attention to stockholder interests. This leads to the agent problem (Fama and Jensen, 1983) and the principal’s issue (Ross, 1973).

The principals and agents in the agency theory are shareholders and administrators, respectively. According to the theory, business managers cannot use their discretion to maximize their own profits if adequate incentives or monitoring are inadequate to deter them from doing so. This allows us to further explain this: first, in order to overcome the principals' and agents' conflicting preferences for business activity and attitudes toward risk exposure, it is essential to align their interests. Due to information asymmetry, which states that the principal and agent possess unequal amounts of knowledge, it is difficult and costly for the principal to monitor the agent's behavior. Typically, the agent has access to more knowledge than the principal. Jensen and Meckling (1976) outline three agency costs for principals to keep a watch on agent behavior: monitoring management, binding the agent to the principal, and residual losses.

With the asymmetry of this information, it can cause problems, Jensen and Meckling (1976) explained that there are two problems that arise, namely:

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a. Adverse selection is a situation where parties inside the company such as company managers and people around them can know more about the company's situation than investors who are parties outside the company. With this, it is possible that the company management (manager) provides company information that is not accordance with the reality in the company such as the financial statements presented are not in accordance with actual conditions, so that it will make investors as parties outside the company make decisions that can harm themselves.
b. Moral hazard is an activity that is only carried out and known by the company's management so that the investor or creditor does not know the things that happen in the company. This is what can make the company's management to carry out actions that benefit themselves such as falsifying financial reports, and this causes a breach of contract because it has violated ethics or applicable norms, because these actions are actions that should not be allowed.

According to Fligstein and Freeland (1995), agency theory establishes the best contract to make use of and control the principal-agent relationship. The creation of this compact is a key component of agency theory as well. The contract should cover and make clear a number of issues, including agent obligations, pay, and the principal's rights to monitor the agent's performance. The behavior-oriented contract and the outcome-oriented contract are the two main contracts that have been adopted. Salary is the main incentive in behavior-oriented contracts, whereas commission, stock options, and the transfer of property rights are some of the various rewards provided to the agent under outcome-oriented contracts. The key to resolving the agency issue is choosing which of these contracts to use for the agent's pay.

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Agency theory was essential for understanding business governance in the 20th century. It significantly increased our understanding of the processes involved in how companies function. Perrow (1986) asserts that agency theory has made rewards and self-interest once again important in organizational theory. According to Eisenhardt (1989), the primary contribution of agency theory is that it provides guidance on how to manage knowledge and risk in the operation of a company. Agency theory is subject to a number of limitations, though. People's "individualism" and "self-interest" are presupposed, according to this theory. However, this assumption does not take into account the complexity of human behavior, according to Doucouliagos (1994). This presumption fails to account for the intricacy of human endeavor. According to Ghoshal and Moran (1996), the premise of this theory has a significant and negative impact on how individuals behave. In other words, the premise of this ideology encourages people to act independently and in their own best interests.

Additionally, according to agency theory, there are only two players in a corporation: managers and shareholders. The impact of a company's operations on different stakeholder groups must obviously be considered. While a company that is accountable to its shareholders can draw and retain equity investment, it is also important to correctly consider the interests of other stakeholder groups. Eisenhardt (1989) asserts that because agency theory considers a great deal of a firm's complexity, it only accurately captures a part of reality.

The obligation that a business must fulfill to stakeholders who are not shareholders expands agency theory as well. An increasing worldwide concern over the planet's carrying capacity, environmental degradation, and disruption of social order has been embraced by the United Nations, giving rise to CSR regulations,

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environmental management accounting, and sustainability reports. The development of the concept of an integrated report has demonstrated to improve the position of the Sustainability Report to maintain business continuity in Europe, as shares available to the public will be more appreciative to stakeholders and potential investors than to investors.

3. Legitimacy Theory

The idea of legitimacy is important when examining how companies interact with their surroundings. Parsons (1960) defined legitimacy as the evaluation of an action in terms of common or shared ideals within the context of the action's participation in the social society. A peer or superior system must be persuaded that an organization has the authority to continue, import, modify, and export energy material or information, according to Maurer (1971).

The idea of organizational legitimacy, which has been described as a condition or status that arises when an entity's value system is congruent with the value system of the large social system of which the entity is a part, is the foundation of legitimacy theory. The legitimacy of the entity is threatened when there is a difference between the two value systems, whether it is real or potential (Dowling and Pfeffer, 1975). According to Donaldson and Preston (1995), legitimacy is defined as the alignment of institutional behavior with societal values, whereas legitimization refers to the measures that institutions take to either publicly demonstrate their alignment with social values or to alter them.

By proving that businesses' actions are consistent with society values, legitimacy is attained. According to Bansal and Roth (2000), examples of legitimation include following the law, creating a position of environmental

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manager or an environmental committee to oversee a firm's ecological impact, creating networks or committees with local community representation, conduction environmental audits, setting up an emergency response system, and aligning the company with environmental advocates. The focus of legitimacy theory is on the idea of a social contract, which suggest that a company's ability to survive depends on how closely it adheres to societal rules and norms (Brown and Deegan, 1998).

Every social institution and business operates in society via a social contract, expressed or implied, whereby its survival and growth are based on: the delivery of some socially desirable ends to society as a whole and, the distribution of economic, social, or political benefits to groups from which it derives its power, described by Shocker and Sethi (in Patten 1991). According to Gray (1994:52), there would be a social contract between corporations and particular people of society. Corporations receive their legal standing, characteristics, and the authority to acquire, use, and employ personnel from society as a whole.

According to Suchman (1995), legitimacy is a generalized perception or presumption that an entity's actions are desirable, proper, or suitable within some socially constructed system of norms, values, beliefs, and definitions. This definition explains how the legitimacy theory can be used to explain how organizations act when they implement and develop voluntary disclosure of social and environmental information in order to uphold their social contract, which enables the recognition of their goals and the survival in a choppy and turbulent environment.

Legitimacy is dynamic in principle, as dynamic as society's expectations of the company. O'Donovan (2002) gives an illustration of the theory of legitimacy in

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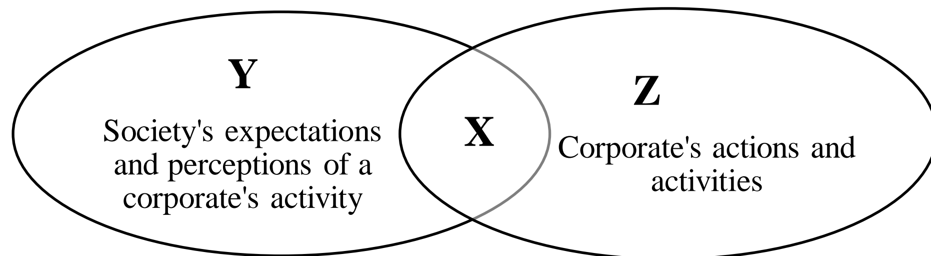
the form of the position of the company's connectedness with society in the following figure:

Figure 2.1 Legitimacy Gap Area



Source: O'Donovan (2002)

The figure above explains that legitimacy is a form of relationship between the company and society. Region Y is society's expectation of the presence or existence of the company. Region Z is a company's expectation of its investment or operations. Region X is congruence between corporate activities and society's expectations. Meanwhile, regions Y and Z are incongruences between the company's operations and the expectations of society (legitimacy gap). The higher region X means the higher the legitimacy of society towards the company, while the smaller region X indicates otherwise. The way taken to improve region X is with legitimacy strategies, one of which is to increase social responsibility.

Taking into account the character of society that is always dynamic and has the potential to shift legitimacy in the company, management must always evaluate and adjust so that there is a harmony of relations between the company and the community. Patten (1992) argues that in order for companies to effectively manage legitimacy, they must:

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a. Identifying and engage the public,
b. Communicating dialogue on issues of social and environmental values, and building its perception of the company, and
c. Implement legitimacy and disclosure strategies, particularly those that deal with social responsibility issues.

According to Kytle and Ruggie (2005), CSR reporting methods have developed into a crucial management tool for the management of multinational corporations' expanding complexity. They go on to say that CSR reporting aids in integrating CSR activities into businesses' strategic risk management in order to maximize the impact of CSR operations. According to Waddock et al.c. (2002) choosing a place of employment is frequently influenced by an employee's impressions of how a firm accepts and manages its responsibilities. Therefore, sharing sustainability-related data can help to position a company as a "employer of choice", which can promote employee loyalty, lower staff turnover, and improve a company's ability to recruit and keep top talent.

To fulfill a company's social responsibility to society is the mechanism of corporate social responsibility. This is in line with the legitimacy theory, which contends the businesses must act in accordance with the laws and standards of the society in which they operate.

4. Stakeholder Theory

Stakeholder theory is a view of capitalism that stresses the interconnected relationships between a company and its customers, suppliers, workers, investors, communities and others who have a stake in the organization. The theory contends that a firm should generate value for all stakeholders, not just shareholders. The

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stakeholder method is defined by seven primary traits by Freeman and Mcvea (2001). The promotion of values-based management, holistic thinking (i.e., taking into account political, ethical, social, and environmental issues in addition to the purely economic), and mutual success are included on the list. In a nutshell, it's stockholder theory, the engine that sparked modern capitalism's quest for maximum profit, with additional guests welcomed to the party (and on an equal footing).

The stakeholder theory, which is based on Freeman and Mcvea (2001) seminal work, claims that as more businesses have realized the importance of integrating corporate social responsibility (CSR) elements into their planning efforts. Although there are few empirical findings that demonstrate that engaging in CSR-related behavior improves financial performance, it has been maintained from the beginning that CSR can significantly improve a firm's overall performance and the goals of the firm's stakeholders, including society (Burke and Logsdon, 1996). Furthermore, these writers contend that superior CSR performance can result in the development of tactical, commercial advantages. Therefore, organizations must consider stakeholder objectives when planning. More specifically, they should identify (1) the crucial stakeholders who can help the organization achieve its mission and strategic goals and (2) the particular strategies that can help these stakeholders achieve their goals.

The identification of these crucial stakeholders becomes the biggest issue that emerges. Since the term "stakeholder" has many definitions and no single definition has been agreed upon, "stakeholder theory" has many different theoretical underpinnings. The work of Freeman and Mcvea (2001) provides the concept's broadest meaning, where a

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> "Stakeholder is by definition any individual or group of individuals that can influence or are influenced by the achievement of the organisation's objectives."

For a variety of reasons, including ambiguity regarding (1) the relative significance or equality of the various stakeholders (or the "value" and "stake" of each stakeholder), and (2) the measurement of performance with regard to the objectives of various stakeholders, attempts to further define "generic" categories of stakeholders are very difficult to achieve in practice. Furthermore, the goals of the various parties involved are frequently extremely varied and even at odds with one another. There may be disagreements between factions even within a stakeholder group regarding the goals to be achieved. As a result, there are issues with the legitimacy of the specific stakeholder group and it is challenging to assess the performance of the organization in which the group has a "stake" (Hill and Jones, 1992).

5. Social Contract Theory

The historical roots of social contract theory can be found in Hobbes (1946), Locke and Latham (1991), and Rousseau and Cranston (1968). Donaldson (1982) approaches the relationship between business and society from a philosophical perspective. He contends that there is an unspoken social contract between business and society, and that this agreement entails some indirect responsibilities on the part of business.

Social contract theory is acknowledged expressly as a type of post-conventional moral reasoning (Rest, 1999). Donaldson (1982) suggest an integrative social contract theory as a mechanism for managers to make decisions in an ethical fashion, thus extending the social contract theory. The social

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perspective contends that businesses have obligations to society, of which they are an essential component. This viewpoint's central tenet is that commercial organizations work with the agreement of the public to satisfactorily address societal requirements (Van Marrewijk, 2003). The societal strategy seems to be a deliberate reaction to evolving conditions and new corporate difficulties that had not before happened, like CSR.

The ideas of social components, social equity, and net social contribution are proposed to be defined by (Ramanathan, 1976). Social groups to which the corporation is supposedly obligated by a social contract are different from social components. He defines social equity as the ability of each of these groups to quantify changes in their rights in relation to the corporation as a result of social transactions. Finally, it is conceivable to define a firm's net social contribution as the sum of its non-market contributions to society's welfare less non-market withdrawals from society's resources made by the firm (Toukabi, in Kemunto and Maende 2021).

According to Dunfee (2006) in Kemunto and Maende (2021), social contract theory will work in an emerging economy where people can allocate scarce resources to their highest-valued uses, where government is constrained to serving only its most effective purposes, where free-moving prices are permitted to indicate the relative value of alternative uses for scarce resources without being distorted by taxes, where the value of money is predictable, and where private property rights and contracts between individuals are respected (Rest et al.c. 1999).

According to the social contract theory, CSR disclosure is a result of an unspoken social contract that exists between businesses and society. This agreement suggests that businesses have some indirect responsibilities to society.

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The social perspective contends that businesses have obligations to society, of which they are an essential component. Business organizations therefore function with the approval of the public in order to meet societal needs satisfactorily and actively. The societal approach appears to be a reaction strategy to both evolving conditions and new business challenges that had not previously occurred, such as CSR initiatives and disclosures. It should come as no surprise that the social contract theory is best suited for organizations operating in developed economies and countries where people can transact with neighbors, people in their state, or people from other countries, where private property rights and contracts between individual decision-makers are upheld impartially, and where the government does not interfere with the free exchange of goods, ideas, and services.

6. Corporate Social Responsibility

There are two different definitions of corporate social obligation. First, it's a general term for any corporate theory that places equal emphasis on the obligation to produce revenue and the obligation to interact morally with the community. Second, corporate social responsibility is a specific interpretation of the duty to maximize profits while advancing larger societal welfare concerns.

Kotler and Lee (2004) defined corporate social responsibility as an organization's dedication to enhancing community well-being through independent business practices and financial contributions. The definition of CSR is a principle that explains that a company must take full responsibility for the consequences of the company's business activities on the community and the environment around the company. Kilcullen and Kooistra (1999) say CSR is the level of moral

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responsibility associated with a company according to the laws of the country where the company is located.

There are two different categories of CSR concepts: broad and specific. In a broad sense, CSR and the pursuit of sustainable economic activity are closely intertwined. The sustainability of economic activity involves corporate accountability to society, the country, and the global community in addition to social responsibility. According to Yeremia and Gunawan (2008), CSR is a form of collaboration between businesses (not just limited liability companies) and every entity (stakeholder) that has a direct or indirect relationship with the company in order to maintain the company's survival and sustainability. This concept is the same as social and environmental responsibility, which is the company's commitment to take part in sustainable economic growth to enhance the quality of life and the environment for the benefit of the company, the local community, and society as a whole.

The concept of corporate social responsibility (CSR) is typically understood in terms of three key concepts. First, CSR is a voluntary role that a business can choose to play in assisting in the resolution of social and environmental issues. In addition to being a for-profit organization, the business also donates a portion of its earnings to charitable causes like philanthropy that aim to improve social conditions and repair environmental harm brought on by exploitation and exploration. Third, CSR as a way for businesses to show concern for and work to resolve the escalating humanitarian and environmental disaster (Marnelly, 2013).

According to Anne (in Marnelly 2013), CSR is important in a corporation to:

a. Balancing the strength of the corporation with the aspect of responsibility

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b. Reduce the presence of government regulation (which is excessive)

c. Increase long-term profits

d. Increase the value and reputation of the corporation

e. Improving social problems caused by the company

Then Kotler & Nance (in Marnelly 2013) added by emphasizing the business aspect that CSR can:

a. Increase sales and market share

b. Strengthen trademark position

c. Improve the ability to attract, motivate and nurture employees

d. Lower operating costs

e. Attract investors and financial analysts

CSR positively advances the public interest by encouraging the growth and development of society. At its core, CSR is a corporate behavior that seeks to improve people's welfare by paying attention to three basic principles: People, Planet, Profit. It can be concluded that CSR not only includes the responsibility to stakeholders and public, but also the implementation of good business ethics by the company.

According to the Holmes Report (2016), The ISO 26000 standard was developed by the International Organization for Standardization to guide businesses toward greater societal responsibility. The seven guiding principles of the ISO 26000 are seen as the foundations of morally responsible behavior. They are as follows:

a. Accountability

b. Transparency

c. Ethical behavior

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d. Respect for stakeholder interests
e. Respect for the rule of law
f. Respect for international norms of behavior
g. Respect for human rights

7. Corporate Social Responsibility Disclosure

Often referred to as social disclosure, corporate social reporting, social accounting, or corporate social responsibility (CSR), the disclosure of corporate social obligation (Suchman, 1995). Communication of the social and environmental effects of economic activity on organizations of special interest groups and on society at large is known as CSR (Hackston and Milne, 1996).

The meaning of corporate social responsibility is given by Kartini (2013). Disclosure is a strategy used by businesses to educate stakeholders and demonstrate accountability. It broadens the company's obligations beyond its customary function of giving shareholders and other capital owners with financial reporting. This growth presupposes that the business is responsible for more than just serving its owners' interests.

According to Gray et al.c. (1988), corporate social responsibility disclosure has the following purpose:

a. To improve the image of the company.
b. To improve the accountability of an organization, with the assumption that there is a social contract between the organization and the community.
c. To provide information to investors.

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8. Good Governance

Rudito and Famiola (2019) define governance as the exercise of political, economic, and administrative authority in the management of a state, including complex mechanisms and related processes, institutions that can voice the interests of both individuals and groups of people in obtaining their rights and carrying out their responsibilities, as well as resolving all disputes that arise between them. Synergy between the government, private sector, and civil society in the management of natural, social, environmental, and economic resources indicates effective governance.

The minimum prerequisites for achieving good governance in Rudito and Famiola (2019) are transparency, accountability, participation, legal empowerment, effectiveness and efficiency, and fairness. Rudito and Famiola (2019) also states that community involvement at every level in the decision-making process is also one of the factors that determine the existence of good governance.

Good governance has more to do with the ethical basics of the regulatory system and must be evaluated through references that refer to the specificity of the underlying norms and objectives. This is as seen in the functions of the community parts that have different points of view based on stakeholders and customers. Good governance is not just about morals, values, and principles.

9. Managerial Ownership

The greater the proportion of management's ownership in the company, the more active management tends to be for the benefit of shareholders, who are none other than themselves (Ross et al.c. 2000:11). Agency problems can be solved in one way, namely managerial ownership. This is because managerial ownership is

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used as a tool to supervise the performance of managers that are internal (Melinda and Sutejo, 2008). In the meantime, managerial ownership, according to Soesetio (2008), is the ratio of managerial ownership to the total number of issued shares. Both parties (managers and shareholders) have a mutual interest in maximizing each other's goals.

In a situation known as managerial ownership, the manager simultaneously serves as the company's owner and also holds shares of the business. This situation is shown in the financial statements by the substantial management ownership of the business. Because it is crucial to share this information for both internal and external users of financial statements, it is included in the notes to the financial statements. When managerial proprietorship is considered in light of the agency theory, it takes on an intriguing quality.

Managerial ownership is very useful for the company because the management participates in the shareholding aspect of the company. As a result, the manager will then do better to increase the value of the company as they too would enjoy the benefits of this. The greater the share ownership by the managerial party of the company, the more proactive the managerial work to realize the interests of shareholders and will eventually increase trust, which will then increase the value of the company.

10. Independent Board of Commissioners

An independent commissioner is a committee member who has no business or other connections that could compromise their ability to act independently and who is not connected to the board, other committee members, or the controlling

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shareholders. Focusing on the duty to defend shareholders, particularly independent shareholders, from capital market fraud and crime, independent standing.

The opportunity to commit such fraud can occur due to low corporate social responsibility. Subarto and Alijoyo (2004) said that public companies located in Indonesia have a lot to learn from companies located abroad, especially companies that have a good reputation in implementing Good Corporate Governance (GCG).

An independent commissioner is a member of the Board of Commissioners who has no financial or managerial ties to the Board of Commissioners, the Board of Directors, controlling shareholders, or any companies that could compromise their ability to act independently in accordance with GCG (Good Corporate Governance) principles, as well as no family ties to any of these parties. The Independent Commissioner is in charge of carrying out supervision and standing up for the interests of small shareholders.

The existence of an Independent Commissioner in the company with the right educational background regarding the awareness of disclosing voluntary objects such as corporate social responsibility activities always ensures that the monitoring mechanism runs effectively and in accordance with laws and regulations. The criteria for determining the company's independent commissioner in accordance with POJK Number 33/ POJK.04.2014 are:

a. Not a person who works or has the authority and responsibility to plan, lead, control, or supervise the company's activities within the last six months, except for reappointment as Independent Commissioner of the company in the next period,
b. Does not have direct or indirect ownership in the company's shares,

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c. Has no affiliation with the company, members of the Board of Commissioners, members of the Board of Directors or the company's major shareholders,
d. Does not have a business relationship, either directly or indirectly, related to the company's business activities.

11. Social Costs

According to Masud (in Januarti 2005), social problems that must be reported in financial statements to the public can be interpreted as social costs. Social costs are costs that are related to social accounting including environmental costs, product costs, employee costs, and community costs. Therefore, it can be said that the cost of employee benefits can increase job satisfaction, affect employee productivity, and affect the organization's ability to generate income.

A form that shows the company's corporate social responsibility and concern for the community is the costs borne by the company when carrying out social activities. There are various activities that fall into the category of social activities that show the community that the company is engaged in social activities.

According to Kotler and Lee (2004:49) there are six alternative corporate social responsibility programs that companies can choose from by considering the company's objectives, the type of program, the potential benefits to be obtained, and the stages of activity:

a. Cause Promotions, companies that use this type of CSR program provide a certain amount of funds as a form of CSR contribution or other resources to increase public awareness of a social problem or support fundraising, community participation, or in order to recruit volunteers to support the social problem.

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b. Cause Related Marketing, a company that implements CSR with this type of program is committed to donating a certain percentage of its income to a social activity based on the size of product sales.

c. Corporate Societal Marketing, the company develops and implements campaigns to change people's behavior with the aim of improving public health and safety, preserving the environment, and improving community welfare. The CSM campaign focuses more on encouraging behavior change related to several issues, namely health issues, protection against accidents, the environment and community involvement.

d. Corporate Philanthropy, companies with the program provide direct contributions for free (charity) in the form of cash grants, donations, and the like.

   As stated by Kotler (2005), "Corporate Philanthropy refers to the firm giving back to society some of wealth it has created thanks to society's input".

e. Community Volunteering, the company supports and encourages employees, franchises, or fellow retailers to set aside their time voluntarily to help local community organizations and communities targeted by the program.

f. Socially Responsible Business Practice, is a business practice in which a company makes investments that support the resolution of a social problem to improve the welfare of the community and protect the environment.

12. Environmental Performance

The relationship between a company and the environment in terms of the environmental impact of the resources it uses, the environmental impact of its operational activities, the environmental impact of its products and services, the

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restoration of product processes, and the company's compliance with work environment regulations is known as environmental performance. According to Bahri and Cahyani (2016), the company's environmental performance is the company's performance in creating a good environment. A high level of environmental damage from the activities of an enterprise means that the company's environmental performance is low, and vice versa. The greater the impact of environmental damage, the worse the company's commitment to the environment.

The Indonesian Government considers environmental performance important through the procurement of the Company Performance Rating Assessment Program (PROPER) implemented by the Ministry of Environment and Forestry. PROPER is a form of government policy, to improve the performance of the company's environmental management in accordance with what has been stipulated in the laws and regulations. Furthermore, PROPER is also a manifestation of transparency and democratization in environmental management in Indonesia. The company's environmental performance in this study can be measured by PROPER rating as follows:

Table 2.1 PROPER Ranking Criteria

Rank	Criteria
Gold	The company has consistently demonstrated excellence in production and service processes, as well as conducting ethical and community-responsible business
Green	The company has carried out environmental management better than what has been required in the regulations (beyond compliance), implemented an environmental management system and they have utilized resources efficiently and carried out social responsibility well
Blue	The company has made the required environmental management efforts in accordance with the provisions or laws and regulations
Red	The company has carried out the required environmental management efforts but not in accordance with the provisions or laws and regulations

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Black	The company has deliberately committed acts or omissions resulting in pollution or environmental damage and has not implemented administrative sanctions

Source: Article on ‘*Program Penilaian Peringkat Kinerja Perusahaan dalam Pengelolaan Lingkungan Hidup* (PROPER), 2018’

B. Previous Studies

Corporate social and environmental disclosure remains a trend in the business world to date. Numerous research has been done on this topic in recent years. At first most of the research was only conducted in developed countries, but over time this research also spread to developing countries. Here is a previous study that revolved around the topic of corporate social responsibility disclosure:

Table 2.2 Previous Studies

No.	Researcher	Year	Title	Research Results
1	Budiyono and Maryam	2017	Disclosure of Corporate Social Responsibility (CSR) Through Company Characteristics at Company Listed on LQ45 Indonesia Stock Exchange (IDX)	According to the study's findings, corporate social responsibility disclosure is not significantly impacted by public ownership, liquidity, or firm growth. Meanwhile, corporate social obligation disclosure is significantly impacted by leverage and profitability.
2	Ayman I. F. Issa	2017	The Factors Influencing Corporate Social Responsibility Disclosure in the Kingdom of Saudi Arabia	The findings demonstrate a positive and significant relationship between profitability and size and CSR disclosure in publicly traded Saudi companies. Board independence, which has a negative effect, is the only aspect of corporate governance that has an impact on CSR disclosure.
3	Nor Hadi	2017	*Peran Biaya Sosial Terhadap Peningkatan Kinerja Social Responsibility Pada Perusahaan Industri*	Environmental cost is significantly linked to social performance, according to statistical analysis. While social success is significantly correlated with social cost (environment, energy,

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			Manufaktur Listed Di Bursa Efek Indonesia	employee, and consumer) statistics test results.
4	Anissa and Machdar	2017	*Pengaruh Kepemilikan Institusional, Kepemilikan Manajerial dan Profitabilitas terhadap Pengungkapan Tanggung Jawab Sosial Perusahaan*	The findings showed that managerial ownership and profitability have a beneficial impact on corporate social responsibility disclosure while institutional ownership has a negative impact.
5	Nurleni	2018	The Effect of Managerial and Institutional Ownership on Corporate Social Responsibility Disclosure	The results showed that there is a direct effect of a negative and significant correlation between Managerial Ownership on Corporate Social Responsibility Disclosure and there is a direct effect of the positive and significant correlation between Institutional Ownership on Corporate Social Responsibility Disclosure.
6	Leny Oktavianawati, Indah Fajarini, and Sri Wahyuningrum	2019	Factors Affecting Corporate Social Responsibility (CSR) Disclosure	The conclusion of this research indicates that leverage, profitability, board of commissioners size, and firm size have significant effect on CSRD. Meanwhile, firm status findings do not significantly affect CSRD.
7	Sofik Handoyo	2020	The Determinants of Corporate Social Responsibility Disclosure: Empirical Evidence from Indonesia Listed Firms	The findings showed that corporate social responsibility disclosure is highly influenced by firm size, earnings per share, and stock price. The study's empirical results aid in comprehending how corporate social responsibility disclosure is carried out in developing nations, particularly in Southeast Asia. Additionally, the results offer useful data for performing cross-country comparison studies.
8	Amrie Firmansyah	2020	Corporate Social Responsibility	The results showed that profitability and firm size

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	and Amardianto Arham		Disclosure In Indonesia: A Bibliographic Study	shows a positive effect on CSR disclosure. In contrast, the majority of test results on effect of leverage show no effect.
9	Umi Kalsum	2021	Factors Affecting the Disclosure of Corporate Social Responsibility	The results indicated that the variable board of commissioners, company size, and profitability have the same significant influence on corporate social responsibility disclosures, while leverage shows no significant effect on corporate social responsibility disclosure.
10	Najeb Masoud	2021	Factors Influencing Corporate Social Responsibility Disclosure (CSRD) by Libyan State-Owned Enterprises (SOEs)	The results showed that firm sizes, firm age, and type of sector are statistically significant and positively related to the dependent variable CSR disclosure. Meanwhile, institutional ownership does not significantly affect the dependent variable CSR disclosure.

Source: Various references, 2022

Unlike previous studies, this study aims to examine the influence of managerial ownership, independent board of commissioners, social costs, and environmental performance on corporate social responsibility disclosures. In this study, environmental performance variable acts as an intervening variable that is predicted to strengthen the relationship between the dependent variable and independent variables used in this study.

C. Research Framework

1. The Effect of Managerial Ownership on Environmental Performance

The stakeholder theory states that the existence of managerial ownership is an effort by the company to establish good relations with stakeholders because the manager is also the owner of the company. Managers who own shares in companies

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or become shareholders of companies are motivated to improve performance, and this is also expected by shareholders. A manager's shareholding helps combine the interests of the manager and the shareholders. Managers are therefore directly affected by the decisions made and suffer losses because of poor decisions (Jansen and Mackling, 1976).

Environmental performance is a company's effort in creating a good environment. Environmental performance is the result obtained by the company from efforts to preserve the environment and fulfil responsibility to the environment (Arieftiara and Venusita, 2017). The Indonesian Government considers this environmental performance important through the procurement of the Company Performance Rating Assessment Program (PROPER) implemented by the Ministry of Environment and Forestry. The company's environmental performance is an effort by managers to increase their responsibility to the environment in order to build a corporate image. One of the ways that management can do in increasing firm value is by increasing concern for environmental performance.

Previous research by Esita and Yanto (2016) shows that managerial ownership has a positive impact on environmental performance. Thus, the more shares owned by the managers in a company, the better environmental performance results are observed from the companies as managers that are also stakeholders in a company tend to make decisions based on increasing firm value to benefit themselves as well by showing concern for environmental performance.

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2. The Effect of Independent Board of Commissioners on Environmental Performance

Agency theory governs the relationship between principals and agents. The principal in question is the party who gives the authority, while the agent is the party who receives the authority and exercises the authority. In connection with this theory, according to Ulya (2020) the highest control lies with the independent board of commissioners responsible for monitoring the actions of top management. A large size of the board of commissioners will improve the company's monitoring capabilities and contribute to improving the company's performance.

The existence of an independent board of commissioners can make the monitoring carried out by the board of commissioners more effective because the independent commissioners will be neutral in carrying out their duties. Independent commissioners are the best position to carry out monitoring functions in order to create a company with good corporate governance stated by (Fama and Jensen, 1983). Companies that have a larger independent board of commissioners will of course be more effective in supervising management's actions in carrying out their operational activities. Companies that have independent boards are more sensitive to social performance and have better social performance ratings than dependent ones. This is supported by the research done, where there is a positive influence between the independent board of commissioners and the company's environmental performance done by Dunn and Sainty (2009).

The results of research conducted by Villiers et al.c. (2009) states that independent boards tend to critically assess management decisions on environmental activities and prevent actions that may lead to environmental violations to create better environmental performance. Results conducted by Dunn

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and Sainty (2009) and Suharyati (2015) also shows that independent commissioners are positively related to environmental performance. Thus, the greater the proportion of independent commissioners, the greater the company's monitoring ability and reduce irregularities committed by agents and the greater the pressure on management to carry out environmental performance.

3. The Effect of Social Costs on Environmental Performance

The theory of legitimacy assumes that the acceptance of the company in the middle of the community, if the company wants to follow the social values that already exist in the community. The company's strategy to be able to gain legitimacy from the community, namely by allocating social costs for corporate social activities. The social costs incurred by the company are seen as an investment for the future of the company because social costs are used to finance activities related to social responsibility. Social costs are the cost of partiality towards stakeholders that have the potential to improve the company's social performance, which can be seen from the smaller claims of stakeholders against the company. The company's partiality efforts towards stakeholders will increase the company's legitimacy.

Research conducted by Januarti (2005) shows that companies that incur higher social costs will have a positive impact on a company's relationship with the surrounding community and improve the company's environmental performance. This result is aligned with research conducted by Pomering and Johnson (2009) which shows that social costs have a positive effect on the environmental performance of a company. Environmental performance in their research was measured based on the Corporate Image Index (CII) score as a weighted average of

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the four measurement dimensions, namely quality, performance, social responsibility, and attractiveness. Companies with Corporate Image Excellent (CIE) predicate have a high CII score above the industry average. The greater the allocation of social costs, the higher the company's CII score.

4. The Effect of Managerial Ownership on Corporate Social Responsibility Disclosure

The manager is the person the owner appoints and gives decision-making power over the operation of the company. The manager is expected to act in the owner's best interests (Sudana, 2011).

The disclosure of the company's social and environmental activities is an effort by the management to meet the information needs needed by stakeholders, because stakeholders not only need financial information but also non-financial information. Companies that have managerial ownership better understand what management should do to satisfy shareholders and other stakeholder groups. Agency theory assumes that problems between principal and agent will increase when the manager holds little equity in the company. This will make managers act opportunistically (Jensen and Meckling, 1976). Agency issues between managers and shareholders may be reduced if the manager has an understanding with the shareholders and the actions taken are in accordance with the wishes of the shareholders. Based on this theory, the relationship between management and shareholders is prone to cause problems so that with managerial ownership in the company, it is expected to be able to minimize problems arising from the delegation of principal authority to agents.

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Managerial ownership has a beneficial impact on corporate environmental transparency, according to Suprapti (2019). Research conducted by Amal (2011) shows the results that managerial ownership affects the social and environmental disclosure of the company. This is because the existence of managerial ownership in the company will make the company have sufficient awareness to carry out its social responsibility activities and then carry out broader disclosure of such activities by reporting them in the company's annual report. The research conducted by Amal is also backed up by previous studies by Listyaningsih et al.c. (2018) which discovered that more environmental knowledge is revealed when managerial ownership is greater. Because they feel they own the business, managers who have a larger stake in it will be more concerned with the interests and welfare of shareholders and will take all reasonable steps to disclose the company's environment.

5. The Effect of Independent Board of Commissioners on Corporate Social Responsibility Disclosure

The number of directors who oversee the management of a company or management team and provide guidance and direction can improve the efficiency of company performance to promote corporate social responsibility disclosure. As the number of independent commissioners increases, the corporate social responsibility disclosure made by companies are more widespread. The larger the number of independent commissioners, the more beneficial it becomes for the company as it has more supervisory roles.

The implementation of the idea of good corporate governance (GCG), whose guiding principles include, among other things, that businesses need to pay

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attention to their stakeholders' interests, in accordance with the law, and establish active cooperation with stakeholders for the long-term survival of the company, logically leads to disclosures. In addition, it is also stated that governance mechanisms and structures in companies can be used as supporting infrastructure for Corporate Social Responsibility Disclosures in Indonesia and independent board of commissioners is one of the indicators used to assess a company's governance mechanism through their monitoring activities. When information asymmetry occurs, it is very likely that adverse selection and moral hazard will occur as well, with the consequence that the company does not carry out corporate social responsibility disclosures (Utama, 2007).

The results of research conducted by Putri and Wahyuningrum (2021) and Kalsum (2021) show that independent commissioners are positively related to corporate social responsibility disclosure. Thus, the greater the proportion of independent commissioners, the greater the company's monitoring ability and disclose more information related to corporate social responsibility activities.

6. The Effect of Social Costs on Corporate Social Responsibility Disclosure

The allocation of social costs by the company is a form of the company's concern for its environment for the impact that the company has on its operational activities. The theory of legitimacy underlies the relationship of social costs to the social and environmental disclosures of companies. Where the company's efforts in fulfilling the social contract with its society require social costs that it uses to carry out social activities and is then disclosed in the company's annual report.

Research conducted by Indah (2014) that social costs have a positive effect on corporate social responsibility disclosure, so it can be concluded that the greater

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the allocation of social costs, the wider the disclosure of corporate social responsibility because the company thinks that the company has made considerable sacrifices by spending money to finance social activities and care for the environment in order to build a corporate image.

7. The Effect of Environmental Performance on Corporate Social Responsibility Disclosure

Based on the theory of legitimacy that the company needs to disclose its operational activities including social and environmental activities so that external parties of the company can know that the company has made an effort to be able to fulfill the social contract with the environment and the surrounding community. Companies that implement good environmental performance can be sure to make environmental disclosures because they will certainly be more extensive in disclosure.

Research conducted by Setyaningsih (2014) shows that there is an influence between environmental performance and disclosures made by companies.

8. The Effect of Managerial Ownership on Corporate Social Disclosure through Environmental Performance

The disclosure of social and environmental information carried out by the company is certainly inseparable from the environmental performance that has been carried out. Environmental performance is a company’s effort to create a better environment. In this study, the existence of managerial ownership is predicted to affect the company’s environmental performance to be disclosed in the company’s annual report. The theory of legitimacy can be used to base the relationship between

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these variables because by carrying out environmental performance the company has shown efforts to follow social values in society to build good relationships with its stakeholders.

Managerial ownership is considered to be able to affect the performance of the company's environment because the company's management is also a shareholder in the company, so that the management can understand what kind of things the stakeholders want or expect, one of which is the shareholders. According to Susanti and Riharjo (2013), problems between managers and shareholders may be reduced if the manager has an understanding with shareholders and the actions he takes are in accordance with the wishes of shareholders. In addition to expecting good company performance, stakeholders also expect the company to have good environmental performance as well. There are several studies that reveal a positive and significant influence between environmental performance and social disclosure including Rakhiemah & Agustia (2009).

9. The Effect of Independent Board of Commissioners on Corporate Social Disclosure through Environmental Performance

The existence of monitoring carried out by the board of commissioners is considered to be able to influence the company to carry out its environmental performance and disclose it in the form of reports. Independent commissioners are considered to be able to make monitoring carried out by the board of commissioners more effective, because independent commissioners are parties who can be neutral. Independent commissioners are the best position to carry out monitoring functions in order to create a company with good corporate governance. The implementation of good corporate governance in the company will encourage management to

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manage the company correctly, including implementing its social responsibility. This is accordance with one of the GCG principles, namely Transparency.

The results of research conducted by Villiers (2009) also states that independent boards tend to critically assess management decisions on environmental activities and prevent actions that may lead to environmental violations to create better environmental performance. Since environmental performance and corporate social responsibility disclosure goes hand in hand, the presence of independent commissioners can improve a company's transparency in disclosing corporate social responsibility activities. This is supported by research conducted by Putri and Wahyuningrum (2021) and Kalsum (2021) which showed that the composition of the independent board of commissioners has proven to significantly affect the disclosure of corporate social responsibility. There are several studies that reveal a positive and significant influence between environmental performance and social disclosure including (Suratno et al.c. 2007).

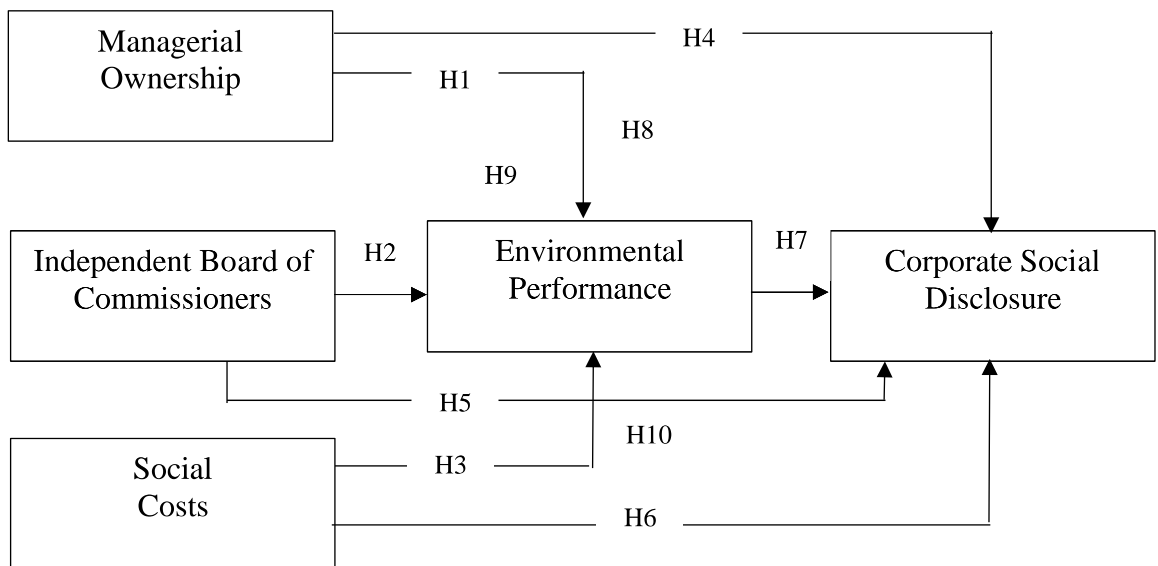
10. The Effect of Social Costs on Corporate Social Disclosure through Environmental Performance

The environmental performance carried out by the company is inseparable from the allocation of costs for the implementation of these activities. Social costs are costs used by companies to support the company's social and environmental activities. The company's activities are then disclosed in the company's annual report so that it can be known by external parties of the company and as management's responsibility to its stakeholders.

There are several studies that reveal a positive and significant influence between environmental performance and social disclosure including Wardhani and

Sugiharto (2013). Indah (2014) shows that the social costs incurred by companies affect the improvement of environmental performance and the availability of widespread social disclosure.

Figure 2.2 Research Framework



D. Hypothesis Formulation

H_1: Managerial Ownership has a positive effect on the company's Environmental Performance

H_2: Independent Board of Commissioners has a positive effect on the company's Environmental Performance

H_3: Social Costs has a positive effect on the company's Environmental Performance

H_4: Managerial Ownership has a positive effect on Corporate Social Responsibility Disclosure

H_5: Independent Board of Commissioners has a positive effect on Corporate Social Responsibility Disclosure

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H_6: Social Cost has a positive effect on Corporate Social Responsibility Disclosure

H_7: Environmental Performance has a positive effect on Corporate Social Responsibility Disclosure

H_8: Managerial Ownership has a positive effect on Corporate Social Responsibility Disclosure through Environmental Performance

H_9: Independent Board of Commissioners has a positive effect on Corporate Social Responsibility Disclosure through Environmental Performance

H_{10}: Social Cost has a positive effect on Corporate Social Responsibility Disclosure through Environmental Performance