

# The Indonesian Executives Perspective of CSR Practices

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## Abstract

The objective of this study is to investigate the CSR (Corporate Social Responsibility) practices after the issuance of the government regulation as the implementation guideline of the CSR as stipulated in the law no.40/2007 through business players' interviews. Using the semi-structured interviews with Indonesian executives/informants of Indonesian companies, this study found that CSR practices have been viewed as philanthropic activities of companies with all the consequences that follow: shareholder as the most important stakeholder, reporting CSR practice as means to have public image and no need to have any standard to prepare CSR practice reporting. Given the findings, there is a need to redefine CSR based on the intention to maintain good relationship with stakeholders and to have the integrated management system to help management well interact with them in market and non-market mechanism.

**Keywords:** *CSR practice, informants, executives, Indonesia.*

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## Introduction

Since the term Triple Bottom Line (TB) had been introduced by Elkington (Elkington, 1997; Slaper and Hall, 2011), the demand that companies consider social and environmental aspects in their business activities has become increasingly common and got positive responses from other parties such as WBCSD (World Business Council for Sustainable Development, WTO (World Trade Organization), and OECD (Organization for Economic Cooperation and Development). Indonesia is not exceptional. To respond to the demand Indonesian Government passed the Law No 40, 2007 (Republic of Indonesia, 2007), pertaining to Limited Liability Companies, approved by Indonesian parliament in 2007. In the article 74 (1) of the law, it is stipulated that any limited liability company in Indonesia must conduct corporate social responsibility (CSR). The obligation of CSR for the companies got reactions from the business com-

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munities under Kadin (Indonesian chamber of Commerce and Industry) by appealing the law to the Constitutional Court with the decision by the court ruling that the CSR is still mandatory for any limited liability company in Indonesia (Business News, 2009; Fauzi, 2009).

The reason why the business players reacted to the law is that the CSR will make companies' cash flow getting worse by having expenditure beyond their business activities. For them CSR is costs for activities nothing to do with business. Such CSR perspective perceived by Indonesian business players is found by Fauzi, Mahoney, and Rahman (2007) and Fauzi (2008 and 2009) with the finding that no relation between CSR and financial performance exists and by Fauzi and Idris (2009) with the relation of CSR and financial performance under the slack resource theory is weaker than that the one under the good management theory. On the other hand, the CSR perspective of the Indonesian business players has been dominated by the CSR paradigm of Friedman (1970).

While CSR studies in the economy setting where no regulation obligating the CSR for companies provided the three possibilities of findings in terms of its relation to financial performance: positive (see for example, Frooman, 1997; Konar & Cohen, 2001; Mahoney & Roberts, 2007; Murphy, 2002; Orlitzky, & Benjamin, 2001; Orlitzky, 2001; Orlitzky et al., 2003; Preston & O'Bannon, 1997; Roman et al, 1999. , Ruf et al., 2001; Simpson & Kohers 2002; Waddock & Graves. 1997; Worrell et al, 1991), negative (see for example, Patten, 2002; Wright & Ferris, 1997), and mixed result (see for example Fauzi, 2004; McWilliams & Siegel, 2000 and 2001; Moore, 2001), the studies of CSR in Indonesian context before the implementation of the law in effect<sup>2</sup> tended to have no relation to financial performance or negative result compared to the ones in their counterpart with positive result in majority (Fauzi, Mahoney, and Rahman, 2007; Fauzi, 2008, and 2009; Fauzi and Idris, 2009). Therefore, it is then very interesting and important to understand how Indonesian business players practice the CSR after the effective implementation of the law No.40, 2007. The importance of this study is that interval between the law passed and the corresponding government regulation issued is very long (more than 5 years), an unusual process for issuing the governmental regulation in Indonesia. In addition, in terms of the content, the government regulation in which the CSR practices for limited liability companies in Indonesia will be based upon seems controversial and not to address properly the things stipulated in the article 74 of the law No. 40, 2007 (Rahman, 2013; LKDI, 2015). Thus, the objective of this paper is to investigate the CSR practices after the issuance of the government regulation as the implementation guideline of the CSR as stipulated in the law no.40/2007 through business players' interviews.

### **Understanding the company's existence**

According to Donaldson and Preston (1995), there are two views on the existence of the company: input & output and stakeholder model. In the view of the input & output

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<sup>2</sup> In Indonesia a law is considered effective for implementation if the government regulation (commonly called PP as abbreviation) related to the law has been issued. This is because the function of the government regulation is as guidance to conduct in the proper way the law approved by the parliament. The government regulation related to law No. 40, 2007, especially for article 74, is PP No.47, 2012, pertaining to Social and Environmental Responsibility of Limited Liability Companies, issued in 2012.

model, a company exists because of the contribution of the various parties as follows: fund contributor, supplier, employee, and customer. The fund contributor, represented by investors (shareholder and creditor), contribute money, with expectation of a return, to the company to buy raw materials for the transformation process purpose. Supplier, in exchange for an agreed priced, plays a role to contribute the raw materials needed in the company's transformation process. Given the raw materials, employee, based on the agreed wage, is tasked to transform the raw materials into finished goods for customer need. Finally, it is the job of customer to pay the agreed price of the finished goods to the company. The view of input & output model is called the primary stakeholder by Post, Lawrence and Weber (2002). The four parties contribute to company through the market mechanism. Simons (2000) also describes their action with company using the three markets approach: financial market for the fund contributor, factor market for supplier and employee, and customer market for customer.

The stakeholder view on the company existence holds that in addition to the four parties as discussed in the input output model, the company affect or is affected by other parties such local communities, the public, business groups, media, social activist groups, foreign governments, and central and local government. The type of stakeholders in this category is often called the secondary stakeholder (Post et al, 2002). They are interacted with the company through non market mechanism. Consequently, the decision made by the company should take into account the two groups of stakeholder. There are three perspectives justifying the stakeholder view: descriptive accuracy, instrument power, and normative validity (Cooper, 2004; Donaldson and Preston, 1995). Under the descriptive accuracy, the parties that need to be considered in the company's decision include shareholder, employees, government, and community. Thus, the stakeholder view is important because it can correctly reflect and predict the operation of the business (Cooper, 2004). According to the instrument power argument, the use of the stakeholder view can improve company's performance in terms of economics and other criteria (cooper, 2004). The performance will be achieved through the balanced interests the company considers in making the business decision. The normative validity perspective justifies the stakeholder view using argument that anybody has moral right to be taken into account by the company. Thus, it is unethical for the company to focus on shareholder only in the decision making process (Cooper, 2004).

### **Approach to CSR**

CSR has so far been approached using two perspectives: philanthropic and stakeholder (Fauzi, 2009). CSR defined using the philanthropic perspective usually separates the CSR activities with the company business. Under this perspective, CSR is burden for the company. It can be argued that the idea of this perspective may be extension of the CSR developed by Friedman (1970), in his controversial essay that the social responsibility of a business was to earn a return for shareholder. When the business that focuses on shareholder only results in the negative impact, the CSR activities may be conducted to cover the complaint from other parties. Another theory that may be related to this CSR perspective is slack resource theory (Waddock and Grave, 1997), holding that CSR activities will be conducted if financial resource of the company is strong. Otherwise, the company is reluctant to do so. This situation applies to Indonesian context (Fauzi and Kamil, 2010).

Stakeholder approach to defining CSR focuses on the company's awareness to maintain good relationship to its stakeholders. Under this perspective, CSR and business are hard to differentiate because CSR is a part of good business practice (Fauzi, 2009). The company business is usually closely related to parties such as investors/shareholders, suppliers, employees, and customers. Maintaining good relationship with them means the company are doing good and finally doing well. At the same way, the company can extend other parties. This CSR perspective can be connected to good management theory developed by Waddock and Graves (1997). According to theory, the company will conduct CSR regardless of its financial position. Implication of this theory is that "doing good" with stakeholders will impact on company's performance. This theory also applies to Indonesian setting, although not as strong as in slack research theory.

### Method

This paper was based on findings from the semi-structured interviews with executives/informants of companies in industry including: (1) Mining, (2) automotive, (3) Airline, (4) Construction, (5) Infrastructure, and (6) Financial. The topics in the interviews include: (1) general aspect of CSR, (2) stakeholder concept, (3) pressure from stakeholders, (4) motivation for CSR practice reporting, and (5) accounting standard for CSR reporting.

### Findings

The findings are presented based on topics of the interviews:

#### General Aspect of CSR

When having talks with the executives as to what CSR was about, the response of most executives was in the following:

*"The CSR is a commitment related to funds reserved for philanthropic activities, the ones nothing to do with the main business activities such as corporate giving for student scholarships, natural disasters, social benefits, and development of micro-scaled business in the location where companies with the CSR commitment are operating, with development fund can be distributed directly by the companies' staff or by third party assigned by companies"*

When the talking was extended to include social accounting or CSR accounting, the following was their responses:

*"We don't understand social accounting or CSR accounting. For them, CSR is nothing to do with accounting matters. They reiterate that CSR is one beyond the companies' main activities"*

#### Stakeholder concept

When a list of stakeholder components was shown to the executives for comments, they agreed with the list. The responses were as follows:

*"Our stakeholders include: shareholder, employee, costomer, supplier, government, society and community, lender, media, and local community"*

However, when the talk on the stakeholder was extended to the issue of the importance of the stakeholders, their responses was as in the following excerpt:

*“For our company the shareholder is the most important stakeholder followed by customer, government, and employee for the next importance”*

The order of the next importance was dependent upon the industry where the executives came from. For the mining industry, the second importance was government, while customer was the second order for the manufacturing industry.

Still in the same topic, the discussion with the executives was extended to include stakeholders consideration in the CSR reporting process. Most of the executive responded that they considered them in the sense that the stakeholders like shareholder and customer were part of their business, but they never said that CSR was a part of their business. It was mere company's philanthropic activities. The talk with the executives went in the deepening question to confirm if the interests of stakeholders were in line with the business the companies were doing. Their responses were in following excerpt:

*“Business and CSR are different thing. In our understanding, shareholder, customer, employee, and government are the ones related to business, while environment and social community and the related-other components are nothing to do with the business. Philanthropic activities by our company are company's concern beyond the business”*

### **Pressure from Stakeholders**

The discussion on this topic with the informant started with industry situation where their companies were operating. Those coming from the mining, construction, and infrastructure industries said that their industries had lot of pressures from Nongovernmental organization (NGO). But their companies did not have problem with that because they successfully managed their public images and CSR (as philanthropy) programs.

### **Motivation for CSR Practices reporting**

The possible reasons for companies to report the CSR activities include pressure for NGO, corporate philosophy, philosophy of top management, government regulation, holding company direction, corporate image, investor request, and trend. According to the executives, they reported the CSR activities as a part of corporate image. And this is true especially for mining industry. For the state-owned company, the reason for the CSR reporting was due to company policy and government regulation. Very few informants said that reporting CSR activities was due to the companies' vision and mission reason. The fact that the companies' annual reports very often report many things beyond stakeholders' concern (except shareholder) become one of the discussion issues extended in this topic. The possible reasons for the issue include: the company objective is to earn a return; the return is not enough for company to do the meaningless activities, cost is greater than benefit in short and long term, the annual report is always briefly written, compliance with certain regulation requires the report in such way, company's concern of the social aspects is not necessary for the company to report them, CSR report is not useful for shareholder, and the lack of company aware-

ness for social and environmental aspects. According to the informants, the reason for company to do so was due to the cost factor.

### **Standard for CSR Practice Reporting**

CSR practiced by Indonesian companies finally will appear in their annual report or standalone report like Sustainability Reporting issued by certain companies. In the discussion with the executives/informants, when question on the need for standard for CSR reporting was raised for their comment, they commented as in the following excerpt:

*"We do not need a standard for reporting CSR practices as CSR is different from economics transaction that needs accounting treatment. CSR is not the domain of accounting"*

If the informants said that they did not need accounting standard for reporting the CSR practice, then the discussion was extended to include: how they report the CSR practices, who determine the CSR information content in the annual report, the need for verification of CSR practice reporting by external party, and to whom the annual report is distributed.

The executives said that they never think about standard when reporting CSR practice in the annual report. The information content of CSR practices in the annual report was the task area of public relation or CSR manager. According to the informants, the external verification of information content of the CSR practices in the annual report was not required as they considered CSR practices were not the same as financial statement requiring the external verification. Finally, the executive said that the annual report with the CSR practice information content was distributed to the capital market authorities and higher education institution. In addition to using the annual report, according to the informants, CSR practices were communicated using the media: newspaper, press release, and company website.

### **Discussions**

CSR practice reporting by Indonesian companies is a part of the companies' efforts to build images: company reputation. The CSR reporting as understood by the executives/ informants is the one nothing to do with the disclosure concept as in the financial statement, given their understanding of CSR, CSR accounting and reporting. They understand CSR as philanthropic-based activities, nothing to do with the main core business. The activities are done by companies by reserving funds for certain activities such as development of Small-Medium Enterprises and social benefits for local society. The understanding is in line with CSR concept of Friedman (1970) saying that social responsibility of company is to earn a return for shareholder. Given the understanding, the CSR reporting is considered as the one different from accounting reporting. And they consider that CSR is not domain of accounting and they do not recognize social and environmental accounting concept accordingly.

There are some motives for CSR practice reporting by Indonesian companies: (1) maintaining public image, (2) compliance with government policy or regulation, (3) direction of corporate holding policy, and (4) in line with corporate philosophy (vision

and mission). Most of Indonesian companies' CSR practice reporting is to maintain the public image. A company with the public image motive normally will report CSR activities by exposing them to the public. Most of companies doing this way are the ones with environment-sensitive category that the Proper committee classified into 4 (four) industry: (1) mining, energy, and gas, (2) manufacturing, (3) agroindustry, and (4) industry region and waste treatment. Companies in the four categories are found very often to massively expose their CSR activities in the leading media to improve the public image. The ultimate goal of doing that way is to avoid the possible pressures from parties such as NGO.

Compliance of government policy or regulation is one of the motives for Indonesian companies, especially for the state-owned companies (SOC), to report CSR activities. For the SOCs, CSR practice reporting is not only compliance with the 2007 law no.40, but it also meets the CSR regulation for the SOCs, that is the 2003 law No. 19. According to the law, the COCs are required to do: (1) CSR activities so called partnership program and environment development, and (2) fund allocation of 2.5% of the SOCs's net profit for CSR activities. It is important to note that CSR understanding is still in the context of the philanthropic-based CSR.

The direction of corporate holding is also a motive for Indonesian companies to report CSR activities. In the holding companies complexities of treats for a business entity can affect the business as whole. The situation is compounded if the gaps of understanding of CSR between corporate level (holding management) and business level exist. Given the situation, the motive for CSR practice reporting comes from the management holding direction.

CSR practice reporting motive may be due to corporate philosophy. The motive is very rare for Indonesian companies. Of the companies pursuing the motive are the ones with Gold, Green, and Blue category in the Proper environmental evaluation system under the Ministry of Environment and Forestry. They include PT. Semen Indosemen Tunggal Perkasa, PT. Bukit Asam, and PT. Surto Toto Indonesia. In the companies CSR is included in their vision and mission.

Some factors have contributed to the inhibiting factors of CSR practices reporting: (1) internal and (2) external. The internal factor relates to the lack of understanding for management for (1) CSR definition, (2) stakeholder concept, and (3) CSR practice reporting. External factor may be due to no support from regulator and accounting profession pertaining to the non-financial reporting.

It is the philanthropic-based CSR, as understood by most of Indonesian business players, contributing to the inhibiting factor. The understanding has the implication on their reluctant to conduct wholeheartedly the CSR. Given the understanding, CSR is considered as cost to impact on financial performance. Thus, the relation of CSR and financial performance will be negative. Therefore, there is a need to redefine the CSR concept (Fauzi, 2009) to lead to maintain the relationship among stakeholder components. In the redefined concept, CSR can be understood as good business practice. By doing so it is expected to satisfy the stakeholders.

Stakeholders include the following components: (1) shareholders, (2) employee, (3) customer, (4) supplier, (5) government, (6) society, (7) lender, (8) media, and (9) local

community. The executive/informants agree with the components. However, when asked to identify the importance of the components, it seems that they are not consistent with them as they consider the shareholder as the most important stakeholder and the ones beyond the market mechanism players are omitted. The understanding is clearly based on shareholding or agency concept underlying the Friedman (1970) thought.

The lack of clear standard for CSR practice reporting results from the misunderstanding of CSR and stakeholder by the business players. The standard for CSR practice reporting is the one in non-financial, especially for social and environment. In the guideline of GRI (Global Reporting Initiative), it is stipulated that CSR reporting will include the three aspects: (1) financial/economic, (2) social, and (3) environment. In terms of the first aspect, financial/economics, the understanding of the executives/informants that CSR reporting is not domain of accounting is clearly questionable. For the non-financial aspect, social and environment, analogy of non-financial aspect in the balanced scorecard concept developed by Kaplan and Norton (1996) applies to the one in the CSR reporting.

The external factor refers to the one from regulator such as Bapepam as capital market authority. The Bapepam has so far not adopted yet a mandatory regulation of CSR practice reporting for companies listed in Indonesian stock exchange. All regulation issued by Bapepam and used by BEI (Indonesian Stock exchange) as guideline to regulate the capital market still focus on shareholder and creditor. It is important to note that the role of other stakeholders whose interaction with the company beyond the market mechanism can make the index of the capital market volatile due to the negative actions by some companies.

Another external factor is accounting profession support. To date no CSR practice reporting standard has been set by Accounting standard board of IAI (Indonesian Accountant Association) to report or disclose CSR activities, the non-financial aspect. In the country like Jordan, the disclosure of CSR activities is mandatory in nature (Al-Khadash, 2007). The support from accounting profession become very strategic as once the standard for CSR reporting has been released, the companies preparing financial statement should include CSR practice reporting. Otherwise, the consequence of audit opinions issued by auditor will emerge accordingly.

## **Conclusion**

CSR as practiced by Indonesian companies has been understood by Indonesian executives as philanthropic activities. Their understanding is line with definition stipulated in the Law No.40/2007 and government regulation (PP) No.49/2012. The consequence of the understanding is that CSR is not a part of the company business. Given the understanding, of the companies' stakeholders, the shareholder is the most important, followed by customer, government, and employee, with the order depending upon the industry type. For the mining industry, government will be the second order, while customer and employee will be ranked in the second position in the manufacturing industry. With the treatment of the stakeholders by the companies, pressures from stakeholders, especially for those considered as inferior, are high in the industries. However, many companies can handle the high pressures using the public image and CSR (as philanthropic) program. It is the motivation for the companies to



report CSR practice. For that reason, any standard including accounting standard for reporting the CSR practices is considered as unimportant.

The theoretical implication of the findings is that given the stakeholder concept, CSR definition needs to be redefined to focus on the importance for the companies to maintain their relationship with the stakeholders. By doing so, they view CSR as a good business practice accordingly. The social responsibility is encouraged from the spirit to maintain a good relationship with corporate stakeholders. Another implication of this study from managerial perspective is the need for management to integrate the redefined CSR into management system as whole. For the purpose of managing stakeholders, the integrated management system will facilitate management to better interact with stakeholders through both market and no market mechanism.

It is suggested that future research needs to be done to extend the coverage for study of the companies that have issued sustainability reports recently. The sustainability reports have been prepared based on the guideline of GRI (Global Reporting Initiative). GRI requires the preparing party to have clear CSR-related vision and mission, strategy and other requirement including performance measures. The next suggestion of using the combined interview and documentation review for future study are expected to improve the findings of this study.

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