Does Human Rights Disclosure Enhance Firm Value?

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Received 12 April 2022
Revised 20 June 2022
Accepted 6 July 2022

Abstract

The objective of this research is to explain the effect of human rights disclosure, independent commissioners, and family ownership on firm value. We also analyzed descriptively human rights disclosures for three periods, which is from 2017-2019, in Indonesia. UNGP-BHR and the Indonesian State Law No. 39 of 1999 about Human Rights are used as the disclosure index checklist. This study uses 345 non-financial companies that are fully listed for three periods on the Indonesia Stock Exchange (IDX). The data used were collected from Bloomberg and Annual Report, which had been taken from the official website of IDX and the official website of the sample companies. The data analysis technique used to test our hypothesis is panel regression. The main result of this study showed that human rights disclosure and independent commissioners have a positive impact on firm value, while family ownership negatively affects firm value. We also found that each item of human rights disclosure increased during the observation period, in which the least disclosed item was related to engagement with external human rights experts to undertake human rights issues. The implication of this research is that increasing human rights disclosure provides a positive image for the investors and creditors.

Keywords: Firm value, Human rights disclosures, Independent Commissioners, Family ownership

Introduction

As the largest economy in Southeast Asia (World Bank, 2020), Indonesia still faces challenges in implementing human rights. Human rights issues can be an obstacle to Indonesia's improvement in the future (Cahaya, 2019). Restrictions on operational activities have caused several companies to cut wages of their employees, such as Fast Food Indonesia Tbk and Matahari Department Store Tbk (CNN Indonesia, 2020). This situation is exacerbated by the fact that the number of workers under 18 years from 2017 to 2019 has reached 1.6 million workers (Badan Pusat Statistik) which is in accordance with Law No. 13 of 2003 concerning Manpower, that workers under 18 years old fall under child labor.

Disclosure related to human rights for Indonesian companies has not become compulsory (Putra, 2020). Therefore, human rights disclosure in the annual report is still very low which is only 36.74 percent (Cahaya, 2019) compared to other Asian countries such as Japan, India, and South Korea (Laskar , 2018). *Human Rights Watch* in the 2020 *World Report* also revealed that the rights of indigenous people are serious threats in upholding human rights in Indonesia.

To achieve high value, companies should not only focus on maximizing profits. One thing that can be done is to pay attention to the company's environment and society because it has a significant influence on the company (Li, 2017). Human resources disclosure can have a positive impact on firm value because it provides a clear picture to investors of how management is performing (Han, 2020).

Corporate governance mechanisms is an important factor affecting firm value (Asante, 2018). The existence of independent commissioners can mitigate agency costs (Hatane, 2019) and encourage the practices of good corporate governance (Purbawangsa, 2019). It is because they have no attachment to the company which can affect firm value (Asante, 2018).

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IJOBP

International Journal of Organizational Behavior and Policy
Vol. 1, No. 1, July 2022
pp. 27-36
Department Accounting, UKP
eISSN 2961-9548
DOI 10.9744/ijobp.1.1.27-36

Family ownership is also a focus in developing countries. Likewise in Indonesia, the proportion of family firms still plays an important role in Indonesian firms. The dominant family company shows a higher company risk (Rajverma, 2019). This can lead to conflicts between majority and minority shareholders where family companies tend to ignore minority interests, thereby affecting firm value (Liew, 2020).

Other factors that can affect firm value are firm size, profitability and firm age. Large, long-established companies are considered to interact with more stakeholders (Hanifa, 2016) so they will provide more information that satisfies stakeholders (Cahaya, 2019), thus affecting firm value positively. The company's goal is to make a profit, so profitability becomes a major concern for management and investors (Purbawangsa, 2019).

This research contributes in several ways. First, this research focuses on how human rights disclosure practices in Indonesia can affect firm value, previous study only explained the factors that influenced human rights disclosure. Second, this study analyzes how corporate governance, especially independent commissioner and family ownership, can affect firm value in Indonesia, whereas previous studies only focused on governance in Western developed countries.

With a sample of non-financial companies in 2017-2019, this study found that the human rights disclosure and the existence of independent commissioners had a positive effect on firm value, while family ownership showed a negative effect on firm value.

Literature Review and Hypothesis Development

Agency Theory

Rajverma (2019) explained that the activities of company executives will be monitored by the shareholders and bring up the agency conflict type 1. Information asymmetric problems often occur in agency conflict type 1 because management can choose the information disclosed by the company, eventually the information owned by management and shareholders is not balanced (Agyei-Mensah, 2017). The existence of monitoring of performance can reduce agency costs so it is expected to improve company value (Al-Farooque et al. 2019).

Majority shareholders' decisions will be monitored by minority shareholders where this can lead to agency conflict type 2 and often occurs in concentrated ownership companies (Darmadi, 2016). According to Kumala and Siregar (2020), high family ownership will increase agency conflict type 2 because it has control over management while minority shareholders do not. Darmadi (2016) argued that the domination of family ownership can be used to take over wealth from other shareholders and increase agency problems, thereby reducing the value of the company (Rajverma, 2019). Thus agency theory is the right basis for explaining the relationship between management and shareholders in the variables we use.

Stakeholder Theory

This theory explains that the company's survival relies on stakeholder support, so the activities carried out by the company are expected to increase stakeholder support and trust (Cooper, 2017). Stakeholder managerial theory argues that companies make disclosures only for certain stakeholders. This theory was also adopted in Cahaya (2019) which found that human rights disclosures in Indonesia are only to satisfy influential stakeholders in ensuring the continuity and sustainability of companies such as investors and creditors. Consistent with Jiang (2019) who stated that in developing countries, there is a classification of stakeholder power from the most influential to the least influential on the company. Barman, E, (2018) found that disclosing non-financial information will support company sustainability goals and explain the company's performance in the company's social and business environment. Therefore, for long-term goals, companies will meet financial and non-financial needs, and build relationships and trust with stakeholders (Oncioiu, 2020). To support the importance of disclosing human rights and their relationship in improving company performance, in this study we adopt the stakeholder theory because this theory has been widely used in previous research (Cahaya, 2019; Jiang, 2019; Oncioiu, 2020).

Hypothesis Development

Human Rights Disclosure

Annual reports are used by management to control and evaluate company performance, while for external parties it is used to make decisions (Han et al., 2020). This leads management to disclose things that provide added value to the company such as sustainability disclosure (Harymawan et al, 2020), and human resources disclosure (Zulaikah, 2019). Consistent with managerial stakeholder theory, Alawi (2019) said human rights disclosure can fulfill the demands of influential stakeholders. Alvarez (2015) showed that Spanish companies pay more attention with social information about employees like health and safety, management and relations with trade unions and workers' rights to create company value. Han et al (2020) further showed that companies with higher human rights disclosure tend to have better future performance. Therefore, we draw the following hypothesis:
H1: Human Rights Disclosure has a positive effect on Firm Value

Independent Commissioners

The board of commissioners is categorized as an influential stakeholder in Indonesia's corporate governance (Cahaya, 2019). Consistent with agency theory type 1, the relationship between shareholders and management may cause conflict, therefore the presence of independent commissioners can solve this problem (Hatane, 2019; Salem 2019). Independent commissioners help the management to perform tasks more effectively (Hatane, 2019) and ensures that the interests of all stakeholders are considered. Kao (2019) found that companies' performance became stronger when the proportion of commissioners increased. Uribe-Bohorquez et al. (2018) concluded that most independent boards tend to create value for firms; and improve company performance (Thenmozhi, 2020). Based on these results, this study predicts the following hypothesis:
H2: Independent commissioner has a positive effect on Firm Value

Family Ownership

Family as controlling shareholders will tend to use investment and financing strategies that are not too risky, thereby eliminating the potential for receiving company funds. Ramírez and Romero (2018) found that decision-making in family companies is influenced by emotional support and is willing to accept a lower level of required return even though it has to sacrifice the company's financial benefits. Information asymmetry that arises in family companies can destroy company value (Rajverma, 2019). Also, the majority shareholder will prioritize their own interests if the personal benefits of the family are greater than the mutual benefits that will be distributed to each shareholder (Sitthipongpanich, 2017) which will lead to *agency conflict type 2*. Other factors, such as family ownership by the second generation, indicate a lower company value creation ability (Memili, 2015). Therefore, we conclude the following hypothesis:
H3: Family ownership has a negative effect on Firm Value

Research Methods

Sample selection

This study uses a purposive sampling technique by taking companies listed on the Indonesia Stock Exchange from 2017 to 2019. Our sample does not use financial companies because they have more stringent rules and regulations. The following is an attachment of the companies sample used in this study.

Table 1. Sample Selection

Criteria	Number observation
Total companies	637
Financial and investing companies	(114)
Listed companies	(96)
Delisted companies	(4)
Suspend companies	(11)
Companies with incomplete annual reports	(40)
Companies with dollar currency	(27)
Total companies observed	345
Total period in years	3
Total sample used (345x3)	1035

Data Collection

This study uses a quantitative method, which combines numerical numbers that state a certain amount, quantity, or scale. To analyze human rights disclosures, we use the content analysis method. We collect data from Bloomberg and annual reports that are obtained through the official website of Indonesia Stock Exchange www.idx.co.id and the official websites of sample companies.

Variable Measurement

This study aims to reveal the correlation between human rights disclosure, independent commissioners, and family ownership with firm value using the following assessments:

Table 2. Variable definitions

Variables	Definition	Source
Dependent Variables 1. Firm Value	Tobin's Q = (market value of equity + book value of debt) / total assets (Thenmozhi, 2020)	Bloomberg
Independent Variables 1. Human Rights Disclosure* 2. Independent Commissioners 3. Family Ownership	Dummy variable; 1 if the company discloses human rights items; 0 if otherwise (Wahab, 2020)	Annual Report
	Proportion of independent commissioners to the total number of commissioners (Hatane, 2019)	Annual Report
	The proportion of shares owned by families that own at least 20 percent of common shares (Darmadi, 2016)	Annual Report
Control Variables 1. Firm Size 2. Firm Age 3. Profitability	Natural logarithm of total assets at the end of the year (Kao, 2019)	Bloomberg
	Age of the company since it was founded in the sample year (Kao, 2019)	Annual Report
	Net income divided by total assets (Kamaliah, 2020)	Bloomberg

Model of Study

$$FV : \beta 0 + \beta 1HRDisc + \beta 2IC + \beta 3FOwn + \beta 4FSize + \beta 5Prof + \beta 6Age + \varepsilon$$

Description:

$\beta 0$ = Constant
HRDisc = Human Rights Disclosure
IC = Independent Commissioner
FOwn = Family Ownership
FSize = Firm Size
Prof = Profitability
Age = Firm Age
ε = Error Term

Research result and analysis

Sample Description

Based on table III, the average human rights disclosure of Indonesian companies is 30.7% or 6 of the 20 items. Several companies do not make disclosures of human rights indicated with a minimum value of 0. Meanwhile, Unilever Indonesia and Sinar Mas Agro Resources and Technology disclosed all 20 items related to human rights.

Table III also shows that the average independent commissioner is 41%. Even so, Intikeramik Alamasri Industri in 2017 did not have independent commissioners. Meanwhile, Hexindo Adiperkasa and Bentoel Internasional Investama are companies in which all commissioners are independent commissioners. Furthermore, family ownership with an average of 40.9% indicates that most companies in Indonesia are publicly owned.

Table 3. Descriptive Statistics

Variable	Mean	Median	S.D.	Minimum	Maximum
Tobinsq	1.571	1.034	2.141	0.16	35.4
HRDisc	0.307	0.30	0.174	0.00	1.00
IC	0.410	0.40	0.115	0.00	1.00
Fown	0.409	0.464	0.321	0.00	0.983
FSize	28.76	28.77	1.65	23.6	33.5
Prof	0.058	0.053	0.116	-1.41	0.695
Age	34.99	34.0	16.3	3.00	103

Table IV shows that the most significant increase on human rights disclosure items were companies that facilitated external complaint mechanisms related to human rights (A9) with a total increase of 10.72% during the observation period. Meanwhile, independent commissioners experienced an increase of 0.46%; family ownership in 2018 increased by 1.36% but decreased in 2019 by 0.15%.

In addition, table IV shows that each year more than 90% of Indonesian companies disclosed P3 thus makes P3 is the most disclosed item, While A5 is the rarely disclosed item, which is only less than 4%.

Panel data regression

This study uses panel data regression to collect data from companies with a period of time over one period. The regression model chosen in this study is Weighted Least Square. A good regression model is tested by three types of testing. The F-test is performed to determine the suitable model between combined and fixed panels while Breusch-Pagan will define the suitable model between composite and random panels. Meanwhile, the Hausman test verifies whether the fixed effect model or random effect model is the appropriate model (Wooldridge, 2016).

The complete results of this study are shown in tables V and VI. This study used a classic assumption test that includes heteroscedasticity and multicollinearity test. Heteroscedasticity is a condition where the error variant is not constant or does not match all observations (Wooldridge, 2016). Heteroscedasticity is a research problem, therefore testing is necessary to test for variability, whether it is the same, and is in the range of the second variable. When the value is < 0.05, it means that the model contains heteroscedasticity. After passing the heteroscedasticity test, variable reliability must be tested by looking at the value of the full collinearity variance-inflation factor (VIF).

When the heteroscedasticity test was performed, it was found that this study was not suitable for using a fixed model because of the heteroscedasticity problem. If heteroscedasticity occurs, then using a GLS estimator to correct for heteroscedasticity is called the Weighted Least Square estimator (Wooldridge, 2016). If the test results show a p-value > 0.05

then H0 is accepted, vice versa. To solve the heteroscedasticity problem, the Fixed Effect Model must be replaced with the Weighted Least Square model. Thus, the best choice model is Weighted Least Square. Complete results can be seen in table VIII and IX.

Table 4. Summary of Variables percentage

			2017	2018	2019
HRDisc	Principle	P1	17%	20%	26%
		P2	10%	11%	14%
		P3	91%	93%	95%
	Action	A1	11%	15%	17%
		A2	7%	10%	13%
		A3	3%	5%	6%
		A4	17%	21%	23%
		A5	1%	3%	4%
		A6	2%	4%	6%
		A7	26%	27%	31%
		A8	79%	83%	87%
		A9	43%	48%	54%
	Thematic	T1	8%	11%	14%
		T2	7%	9%	13%
		T3	27%	31%	36%
		T4	69%	71%	76%
		T5	43%	46%	52%
		T6	85%	88%	90%
		T7	4%	4%	6%
		T8	8%	10%	13%
IC			40,8%	40,9%	41,4%
FOwn			40,0%	41,4%	41,3%

Table 5. Summary of OLS Models

Dependent variable	Coefficient	t-ratio	Tobin's Q (p-value)	Collinearity (VIF > 10,0)
Const	6.32999	4.895	<0,0001 ***	1.387
HRDisc	1.18038	2.751	0,0060 ***	1.009
IC	1.12875	2.046	0,0410 **	1.074
Fown	−0,52741	-2.586	0,0098 ***	1.401
Fsize	−0,20756	-4.571	<0,0001 ***	1.070
Prof	5.04172	8.949	<0,0001 ***	1.063
Age	0.00888	2.223	0,0264 ***	
Adjusted R Squared			0.098352	
p-value (F)			5,73 e-22	
Heteroskedasticity			2,06692 e-012	
Normality			0	

Notes: *p<0.10 (weakly significant); **p<0.05 (significant); ***p<0.01 (highly significant)

Table 6. Summary of panel effect tests

Dependent variable	Tobin's Q (p-value)
The Fixed effect estimator	1,49355 e-125
Result	Fixed
Random effect estimator	1,36383 e-105
Breush-Pagan test statistic	Random
Result	5,37958 e-012
Hausman test statistic	Fixed
Result	

Hypothesis and research results

Table 7. Comparison of fixed effect and random effect

Variables	Fixed effect		Random effect	
	Coef.	p-value	Coef.	p-value
cons	28.0951	<0,0001 ***	5.7553	0,0020 ***
HRDisc	-1.0783	0,0876 *	-0.2565	0.5817
IC	0.1763	0.7861	0.4508	0.4119
FOwn	-0.1713	0.7630	-0.6101	0,0318 **
FSize	-0.8237	0,0002 ***	-0.1577	0,0154 **
Prof	0.2783	0.6544	2.1362	<0,0001***
Age	-0.0721	0.1212	0.0106	0,0871*
Adj. R2	-0.219225		0.070118	
p-value (F)	7,0 e-139		7,09679 E-005	

Table 8. The final regression models of weighted least square

Variables	TOBIN'S Q			
	Coefficient	error	z	p-value
cons	5.12282	0.20285	25.25	<0,0001 ***
HRDisc	0.83842	0.09036	9.279	<0,0001 ***
IC	0.65411	0.11061	5.914	<0,0001 ***
FOwn	-0.42575	0.04006	-10.63	<0,0001 ***
FSize	-0.15872	0.00703	-22.58	<0,0001 ***
Prof	4.99213	0.16716	29.87	<0,0001 ***
Age	0.00662	0.00068	9.730	<0,0001 ***

Notes: *p<0.10 (weakly significant); **p<0.05 (significant); ***p<0.01 (highly significant)

Table 8 shows that there is a significant positive effect on firm value of 0.8384, which indicates that human rights disclosure in the annual report increases firm value, therefore we accept H1. Consistent with Han et al., (2020) who argued that companies with higher disclosure tend to have better future performance and company openness with stakeholders can increase trust, thereby playing an important role in the company.

Table 8 shows that there is a significant effect on firm value of 0.6541 which indicates that the presence of an independent commissioner on the executive board has a positive effect on firm value, therefore we accept H2. Consistent with Kamaliah (2020) and Thenmozhi (2020), independent commissioners have an important role in exercising internal control to minimize the occurrence of conflicts within the company.

Table 8 shows that there is a significant negative effect on firm value of 0.4257, which indicates that family ownership as a controlling shareholder can cause a decline in firm value therefore we accept H3. Consistent with Rajverma (2019), family ownership has a negative effect on firm value, because it tends to use less risky strategies to protect their own interests and make decisions by ignoring the opinions of minority shareholders.

The control variables used in this study statistically affect firm value. In which profitability and firm age have a positive effect on the firm value, but firm size has a negative effect on the firm value.

Discussion

Increased disclosure at each period shows the increasing awareness of Indonesian companies of the importance of human rights. This significant increase was also due to Financial Service Authority regulation Number 51/POJK.03/2017, which requires companies to report sustainability reporting starting in 2019. This report can be prepared separately or as an inseparable part of the annual report. Investors usually see an annual report because it summarizes the company's overall performance for a year. Therefore, the company hopes that by disclosing non-financial activities, it can create effective communication with stakeholders. It is clear that the increase in human rights disclosure by companies is aimed at influential stakeholders and saves the company's financial crisis.

Overall the lowest disclosure is item A5 which is similar to Cahaya's (2017). It is undeniable that most companies do not collaborate with human rights experts because they feel they have the ability to solve human rights-related problems on their own, thus saving costs for experts. In fact, to identify the importance of human rights and potential problems that will arise, special expertise is needed, such as the involvement of independent human rights experts in determining risks to companies (Wahab, 2020). Meanwhile, the disclosure of item P3 proved to be the highest. This shows that the Indonesian companies express their willingness to comply with government’s regulations clearly .

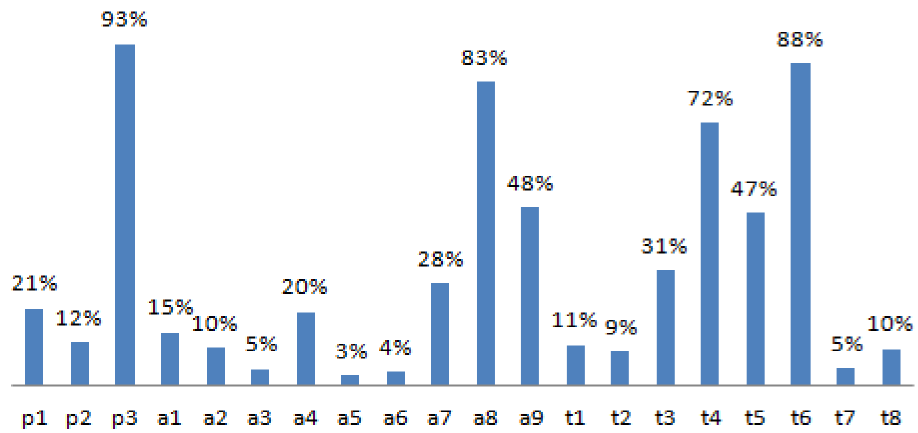

Chart 1. Human Rights Disclosure 2017-2019

The independent commissioners helps shareholders monitor the executive to be tighter because they do not have a special relationship with other stakeholders; and reach the best decisions so that the company's performance is more efficient. However, we still find companies that do not comply with Financial Services Authority regulations, which may have an impact on independent commissioners effectiveness in performing its function. Furthermore, family as controlling shareholders tend to maintain the existence of family members in the company even though they don't have adequate abilities. This makes employee work ineffective and inefficient which will have an impact on the decline in company performance.

Conclusion

Disclosure regarding principles and actions performed by Indonesian public companies as a form of implementation of disclosure guidelines such as the United Nations Guiding Principles on Business and Human Rights (UNGP-BHR), although in practice companies are not required to do so. The information disclosed affecting firm value positively and has the potential to improve its image because it can show that the company is not only focused on getting profit but also pays attention to the human resources they have and contributes to the environment affected by their operational activities. Also we found that companies form independent commissioners which can reduce conflicts of interest between shareholders and management; reduce agency costs, thus increase firm value. Moreover, the higher the family ownership affecting lower the company's value because family-owned companies are more private, controlled, and dominate both in management and decision-making.

This research is limited in several ways. This is a quantitative research, so qualitative research was required to deepen the understanding of factors affecting firm value. We only use annual reports to analyze human rights disclosures because the obligation to make sustainability reports by Indonesian companies just started in 2019. Also we did not analyze the finance and investing sectors so further research is expected to fulfill these limitations to find new evidence.

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