

## The Influence of the Existence of an Oversight Committee and the Extent of Voluntary Disclosure on Stock Prices in Indonesia

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### Abstract

This study consists of two test models. The first model investigates the impact of the existence of an oversight committee on the extent of voluntary disclosure. The second model investigates the impact of the extent of voluntary disclosure on stock price. The data was collected from the annual reports of non-financial companies listed on the Indonesian Stock Exchange (BEI) in the period of 2012, 2013 and 2014. Analysis tools used in the first test model is a multiple regression and in the second is simple regression model. The results of analysis show that only the existence of the risk management committee has a significant positive effect on the extent of voluntary disclosure. Then, the extent of voluntary disclosure has a significant positive effect on stock prices.

**Key words:** Corporate governance, Stock price, Disclosure.

## *Pengaruh Keberadaan Komite Pengawasan dan Tingkat Pengungkapan Sukarela pada Harga Saham di Indonesia*

### Abstrak

*Penelitian ini terdiri dari dua model tes. Model pertama menyelidiki dampak dari keberadaan komite pengawasan pada tingkat pengungkapan sukarela. Model kedua menyelidiki dampak tingkat pengungkapan sukarela pada harga saham. Data dikumpulkan dari laporan tahunan perusahaan non-keuangan yang terdaftar di Bursa Efek Indonesia (BEI) pada periode 2012, 2013 dan 2014. Alat analisis yang digunakan dalam model tes pertama adalah regresi berganda dan yang kedua adalah model regresi sederhana. Hasil analisis menunjukkan bahwa hanya keberadaan komite manajemen risiko memiliki efek positif yang signifikan pada tingkat pengungkapan sukarela. Kemudian, tingkat pengungkapan sukarela memiliki efek positif yang signifikan terhadap harga saham.*

**Kata kunci:** Tata kelola perusahaan, Harga saham, Pengungkapan.



## **INTRODUCTION**

Companies in Indonesia today are demanded to increase competence and effectiveness in meeting their respective visions and missions. The application of Good Corporate Governance (GCG) is expected to contribute a sustainable added value for companies through a healthy, long-term growth pattern. One of the ways in which GCG principles is effectively applied is through the formation of committees by Board of Commissioners. Among these committees are operational committee and management oversight committee. Both committees serve as effective mechanisms in the focus of companies for risk oversight, risk management, and proper internal control (Subramaniam, et al., 2009).

In Indonesia, management oversight committee has been increasingly developing. The government subsequently solidifies the formation of management oversight committee for banking sector. However, different from that of tightly regulated banking and financial sectors, the formation of management oversight committee for other industrial sectors in Indonesia is still largely voluntary.

An effective management system can help companies in meeting the goals of their businesses, increasing the quality of their financial reports and maintaining their reputations. The act of disclosure, specifically voluntary disclosure, is one of the ways in which companies can increase the quality of their financial reports and maintain their reputations. The further the extent of the voluntary disclosure made by a company, the more value the company will have.

Voluntary disclosure reduces information asymmetry, so as to increase trust of investors toward the management of a company (Kangarlouei, et.al., 2013). Voluntary disclosure also minimize the possibility of profit statement manipulation, which makes stock prices of a company reflecting the financial condition of the respective company more reliably, and thus form a relationship between voluntary disclosure and stock prices.

Voluntary disclosure of information of a company may be affected by the specific characteristics of the company such as the existence of a management

oversight committee. The existence of this committee affects the extent of voluntary disclosure of information within the annual report of a company, and it affects the stock prices of the company. The difference of this extent of voluntary disclosure of information is an interesting phenomenon to be studied.

This research aims to test the impact of the existence of nomination and remuneration committee as well as risk management committee toward the extent of voluntary disclosure. Moreover, this research also aims to test the effect of the extent of voluntary disclosure toward stock prices of companies in public, non-financial companies in Indonesia.

## **LITERATURE REVIEW**

### **Agency Theory**

In the theory of agency, conflict of interest arises between the principals and the agents since each side is motivated by its own agenda (Jensen & Meckling, 1976) The theory of agency can be used to discuss the existence of oversight committee in terms of monitoring aspect. Committees formed by the Board of Commissioners are the extensions of the board as the principal of a company which serve overseeing function toward company management as the agent. With the existence of the committee, it is expected by the Board of Commissioners that the management (agent) will act in accordance to the directives of the board as the principal.

Committees formed by the board of commissioners is an effective corporate governance mechanism to address the agency problem. Generally, the committee is also likely to provide a better quality of internal control by guiding managers to behave opportunistically lower.

### **Stakeholder Theory**

This theory states that all stakeholders has the right to information on organizational activities pertaining to their interests even when they choose not to use such information as well as when they cannot directly assume their constructive roles in the existence of the organization (Deegan, 2004). The theory of stakeholder, then, is a strong basis for the voluntary disclosure of information.

### Legitimacy Theory

Theory of legitimacy largely refers to the premise that there is a 'social contract' between a company and the community in which the company operates. Based on the theory of legitimacy, an organization must consistently show that its operation and behavior are consistent to the social values held by the community (Guthrie and Parker, 1989). This mutual relationship can be achieved by disclosure of information in the report of a company, specifically voluntary disclosure.

### Signaling Theory

Signaling theory states that company will divulge more information than it is required as a signal from the company to the stakeholders, particularly to the investors (Godfrey, 2006). As a logical consequence of signaling theory, managers are encouraged to signaling hope for the future, with a view if investor trusts the signal, the company's stock price will rise and shareholders will get benefit.

An effective management system can help companies achieve their business objectives, improve financial reporting and maintain their reputation. One of the ways to improve the quality of financial reporting and maintain the reputation is by doing disclosure.

Voluntary disclosure can increase the value of the company, because the company would seem more honest and care about the world in which they live (Francis et al., 2005). Voluntary disclosure of information will reduce the asymmetry of information, so it will build investors' trust in the company management, in addition, there is relationship between voluntary disclosure to the stock price (Kangarlouei, et al., 2013). According Matoussi & Raida (2006), the quality of voluntary disclosures in the annual report, nowadays, is at the heart of modern financial problems. Companies are faced with a serious crisis of trust and these companies are not able to think about the efficiency of financial communications. Thus, transparency and greater transparency will make corporate stakeholders have better information. This will lead to a better allocation of capital in the stock market anyway. Hana (2012) states that the voluntary disclosure (CSR) has an influence on stock returns.

Generally, previous studies more frequently only examine the effect of audit committee on voluntary

disclosure. Ho and Wong (2001) provides empirical evidence that there is a positive influence between voluntary disclosure on the existence of audit committee. Audit committee, nomination and remuneration committee, and risk management committee are the type of supervisory committee formed by the board of commissioners. Nomination and remuneration committee and risk management committee have the same task with the audit committee. Empirical evidence to test the influence of nomination and remuneration committee and risk management committee on the voluntary disclosure and stock price changes is still limited so that the phenomenon is interesting to study. This research is made with reference to the research conducted by Subramaniam, et.al. (2009) and Hana (2012) along with adjustment and development

The theoretical framework built for this research is as follows,

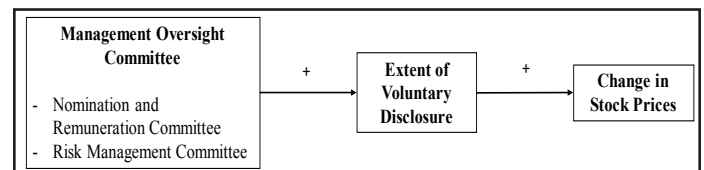


Fig. 1. Theoretical Framework

The existence of effective management oversight committee can help the company achieve its business objectives, improve financial reporting and maintain their reputation. The committee is not only considered important in financial companies but also in non-financial companies. It is considered as an important part of implementation system of good corporate governance, although it has not been mandated. With the existence of management oversight committee, the risks faced by non-financial companies can be minimized. The presence of management oversight committee will create a more qualified financial reporting because there is motivation to reduce information asymmetry. Then the company will be able to provide a broader voluntary disclosure.

Investors need signals when they want to invest in a company. Voluntary disclosure is one of the signals used by investors to gain an overview of the company condition. The extent of voluntary disclosure is a form of transparency made by the company. Transparency



is considered to be reducing information asymmetry and profit manipulation, thereby reducing the level of uncertainty about the prospects of the company. Stock price is considered more reliable in reflecting the company's financial condition. A reliable stock price information will encourage the creation of investors' trust in the company. The creation of investors' trust will affect investment behavior of investors to the company.

### **Hypotheses**

H1: The existence of nomination and remuneration committee in companies of non-financial sectors positively impacts the extent of voluntary disclosure.

H2: The existence of risk management committee in companies of non-financial sectors positively impacts the extent of voluntary disclosure.

H3: The extent of voluntary disclosure in companies of non-financial sectors positively impacts the stock prices of the said companies.

### **Operational Definitions**

#### **The Existence of Nomination and Remuneration Committee (NRC)**

The nomination and remuneration committee is measured by a dummy variable, within companies which possess or express the existence of risk management committee in their annual report by giving the value of one (1), whereas otherwise the value of zero (0) is given (Subramaniam, et al., 2009).

#### **The Existence of Risk Management Committee (RMC)**

The risk management committee is measured by a dummy variable, within companies which possess or express the existence of risk management committee in their annual report by giving the value of one (1), whereas otherwise the value of zero (0) is given (Subramaniam, et al., 2009).

#### **The Extent of Voluntary Disclosure (DSCORE)**

Voluntary disclosure is measured by index of voluntary disclosure which numbered in 49 items. The following are general descriptions of the checklist in each voluntary disclosure measurement item:

**Table 1. Checklist of item groups in voluntary disclosure**

Indicators	Number of Items
General information of the company	7
Information on Board of Commissioners and Board of Directors	7
Evaluation on future operations	5
Research and development	5
Information on Employees	10
Reports on Company Social Responsibility	6
Improvement of products and services	3
Information of the application of CG	6
Total number of items	49

### **Changes in Stock Prices (CSP)**

Changes in stock prices is the increase or decrease in stock prices as a consequence of new information which affects the price of the sock.

### **RESEARCH METHODS**

This research is intended to be an explanatory research. The population studied in this research includes companies listed under Bursa Efek Indonesia / Indonesian Stock Exchange (BEI) during the 2012, 2013, and 2014 periods.

#### **Samples**

Samples are collected using purposive sampling method. Companies set up as objects in this research are those which meet the following criteria: first public companies listed in BEI consecutively during the periods of 2012, 2013, and 2014 and second companies which are not listed as banks or other institutions with business in the financial sector.

From these criteria, 405 companies are categorized under non-financial sectors. Out of all those companies, 81 are set as annual research samples. The number of annual research samples is determined using the Slovin formula.

#### **Tools of Analysis**

Tools of analysis used in this research is Multiple Linear Regression and Simple Linear Regression / Ordinary Least Square (OLS).

$$(DSCORE) = \alpha + \theta_1(NRC) + \theta_2(RMC) + e \quad (1)$$

$$(CSP) = \alpha + \theta(DSCORE) + e \quad (2)$$

- RMC : Risk Management Committee  
 NRC : Nominations and Remuneration Committee  
 DSCORE : Voluntary Disclosure  
 CSP : Changes in Stock Prices

## RESULT AND DISCUSSION

### Results

The research samples are divided into four groups, namely companies which express the existence of nomination and remuneration committee, companies which do not express the existence of nomination and remuneration committee, companies which express the existence of risk management committee, companies which do not express the existence of risk management committee. Of the total 243 companies in non-financial sector, 145 companies or 59.7% express the existence of nomination and remuneration committee, whereas 146 companies or 60.1% do express the existence of risk management committee. As many as 44 companies in 2012 express the existence of nomination and remuneration committee, 49 committees in 2013, and 52 companies in 2014. In addition, 43 companies express the existence of risk management committee in 2012, 49 companies in 2013, and 54 companies in 2014.

The results of analyses are obtained using two testing models, namely multiple linear regression to test H1 and H2, whereas simple linear regression is used to test H3. The results of analyses can be seen below:

**Table 2. Summary of Hypotheses Testing Results**

No.	Hypothesis	Significance	Results
1.	The existence of nomination and remuneration committee in companies of non-financial sectors positively impacts the extent of voluntary disclosure.	0.134	Not passed
2.	The existence of risk management committee in companies of non-financial sectors positively impacts the extent of voluntary disclosure.	0.000	Passed
3.	The extent of voluntary disclosure in companies of non-financial sectors positively impacts the stock prices of the said companies.	0.000	Passed

## Discussions

### First Testing Model

#### The Existence of Nomination and Remuneration Committee

Based on the analysis made in this research it is identified that the existence of nomination and remuneration committee does not have a significant influence toward voluntary disclosure. This is shown by the value of NRC variable probability of 0.134. The significance value obtained is more than 0.05. Therefore, it can be concluded that the existence of nomination and remuneration committee does not affect the extent of the voluntary disclosure in a financial report.

#### The Existence of Risk Management Committee

Based on the analysis made in this research, it is identified that the existence of risk management committee has a significant influence toward voluntary disclosure. This is shown by the value of RMC variable probability of 0.000. The significance value obtained is less than 0.05. Therefore, it can be concluded that the existence of risk management committee positively affects the extent of the voluntary disclosure in a financial report. Studies on the impact of the existence of risk management committee toward the extent of the voluntary disclosure have not been widely made or publicized. Ho and Wong (2001) provides empirical evidence of the positive influence made by the existence of auditing committee toward the extent of the voluntary disclosure. Both auditing committee and risk management committee falls into overseeing-type committees whose formation authority lies on Board of Commissioners. Both committees are charged with similar duties namely to provide independent monitoring over various activities of the board in order to improve accountability of the Board of Commissioners and protect the shareholders.

The required existence of risk management committee by companies in financial sectors has positively impacted the application of good corporate governance. However, the existence of this committee as an operational requisite of companies in non-financial sectors deserves attention. Risk management committee plays a vital role in the realization of good corporate government practices. The existence of the



committee will greatly minimize the risks faced by companies in non-financial sectors. This, in turn, will lead to better quality in financial report so that the companies may improve the extent of their voluntary disclosure of information. The previous statements are reinforced with the findings in this research, namely the existence of risk management committee within companies in non-financial sectors positively impacts the extent of voluntary disclosure.

Larger extent of voluntary disclosure can increase the value of a company, since the company will be perceived to be more accountable and more responsible to the environment in which they operate (Francis, et.al., 2005). Voluntary disclosure can reduce capital cost and improve credibility as well as minimize asymmetry of information (Francis, et al., 2005), which makes larger extent of voluntary disclosure positively impacts the achievement of good corporate governance practices.

### **Second Testing Model**

#### **The Extent of Voluntary Disclosure**

Further in this research, the analysis made has identified that the extent of voluntary disclosure made by companies in non-financial sectors has a significant influence toward the change in stock prices. This is shown by the value of DSCORE variable probability of 0.000. The significance value obtained is less than 0.05. Therefore, it can be concluded the the extent of voluntary disclosure made by companies in non-financial sectors positively affects the changes in stock prices.

A company discloses social information with the objective of building the value and raising the public awareness of the company. Voluntary disclosure can reduce information asymmetry between a company and its shareholders. It also serve as signal of transparency which is used by the investor to obtain the current condition of a company. To the investors, voluntary disclosure serves as a positive signal for the value of the company. The trust built between a company and its investors can influence the stock price set in the market. The higher the trust of investors to a company, the higher the stock price of the company will be.

### **CONCLUSION**

This research has identified that the existence of risk management committee significantly give positive impact toward the extent of voluntary disclosure of companies in non-financial sectors. The existence of the committee within companies in non-financial sectors is still perceived as a vital component in the practices of good corporate governance principles, although the existence has not been mandated. The existence of risk management committee will significantly lower the risks faced by companies in non-financial sectors. This in turn impacts the quality of financial reporting of the companies in that it improve the quality of the reports, so that the companies can improve the extent of their voluntary disclosure as well. Larger extent of voluntary disclosure will positively impacts the credibility as well as the value of the companies to the stakeholders, which is reflected through the stock prices of the companies. Better stakeholders' assessment toward companies is expected to serve as an effective mechanism in achieving the objectives of the companies.

This research can be used as a discourse in the study of the importance of the existence of oversight committees within companies in non-financial sectors, so that after determining the importance of the existence of such committees which is yet to be mandated within companies in non-financial sectors, regulators and implementators of good company governance may come to better consideration. This is important in the realization of good company governance all across the industrial sectors.

There are several limitations found during this research. One of the limitations is the fact that management oversight committee is still considered a new concept in Indonesia, which in the progression of this research causes the limited number of companies which express the existence of management oversight committee. The information on risk management committee is obtained only from the annual reports of corporate governance and auditing committees. Further studies on this subject should add more data collection methods such as questionnaires as well as in-depth interviews to better discover the existence of risk management committee.

**APENDIX**

**Table 3. Descriptive Statistics**

	N	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
DSCORE	243	18	47	33.07	7.023	-.083	.156	-1.237	.311
CSP	243	3	24	12.32	5.094	-.013	.156	-1.047	.311
<b>Valid N (listwise)</b>	<b>243</b>								

**First Testing Model**

**Table 4. Model Summary<sup>b</sup>**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.670 <sup>a</sup>	.449	.444	5.237	1.703

*a. Predictors: (Constant), NRC, RMC*

*b. Dependent Variable: DSCORE*

**Table 5. Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	26.945	.593		45.419	.000		
	RMC	9.068	.752	.634	12.062	.000	.833	1.201
	NRC	1.127	.751	.079	1.502	.134	.833	1.201

*a. Dependent Variable: DSCORE*

**Second Testing Model**

**Table 6. Model Summary<sup>b</sup>**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.933a	.870	.869	1.841

*a. Predictors: (Constant), DSCORE*

*b. Dependent Variable: CSP*

**Table 7. Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	10.054	.570		-17.652	.000
	DSCORE	.677	.017	.933	40.150	.000

*a. Dependent Variable: CSP*



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