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THE EFFECT OF GOOD CORPORATE GOVERNANCE MECHANISM AND CORPORATE SOCIAL RESPONSIBILITY DISCLOSURE ON THE COST OF EQUITY CAPITAL

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ABSTRACT

This study aims to see the integration of accounting concepts in Good Corporate Governance Mechanism, Corporate Social Responsibility Disclosure and Cost of Equity Capital. This research is explanatory research intended to explain the causal relationship between variables through hypothesis testing. This analysis is used to determine the magnitude of the influence of independent variables to the dependent variable. This research is an empirical and grounded study based on existing theories which then developed into a research model where the model in this study is designed to examine the influence of Good Corporate Governance Mechanism and Corporate Social Responsibility Disclosure on the Cost of Equity Capital. This study aims to find and obtain research empirical evidence to obtain answers to research problems on how much influence Good Corporate Governance Mechanism and Corporate Social Responsibility Disclosure on the Cost of Equity Capital. The benefits of this research are to contribute scientifically to the science of financial accounting and management accounting and to solve problems for managers in the execution of tasks related to Cost of Equity Capital.

The result of this study states that the Good Corporate Governance Mechanism in this case is proxyed by Independent Commissioner, Frequency of Audit Committee Meeting and Audit Quality as follows: The Independent Commissioner and The Frequency of Audit Committee Meeting have no effect on the Cost of Equity Capital, while The Audit Quality affects Cost of Equity Capital. The Corporate Social Responsibility Disclosure also has no effect on the Cost of Equity Capital.

KEYWORDS:

The Good Corporate Governance Mechanism, The Corporate Social Responsibility Disclosure and The Cost of Equity Capital

INTRODUCTION

Cost of equity capital is a financial concept that can show an attachment between a firm's long-term investment decision and the expected rate of return. With the calculation of cost of equity capital, the return on investment decisions will be made by a company becomes more secure because the company has estimated the return to be received from the investment. Cost of equity capital relates to the risk of investing in the company's shares. One of the risks to be considered is the risk of information related to the uncertainty of the prospects of the company in the future.

Good corporate governance is a mechanism for the performance of managers, who have a close relationship with corporate structure, such as board of commissioners. Board of commissioners plays an important role in the implementation of good corporate governance, because the board of commissioners is the core that is directly related to its role to perform supervisory functions in the company's performance. However, to oversee the performance of the board of commissioners, an independent commissioner is established which directly the existence of this independent commissioner becomes important for the company, because in practice is often found transactions that contain conflict of interest.

Guidelines on independent commissioners drawn up by the KNKCG (Task force of the National Committee on Corporate Governance Policy), affirm that the independent commissioner is a member of the board of commissioners who is not affiliated with the directors, the members of the board of commissioners and the controlling shareholder and is free from any business or other relationship which may affect the ability to act independently or act on behalf of the company.

Each composition of the board of commissioners in the company has different characteristics, as well as the membership of the audit committee and the quality of its external auditor. Companies that have independent commissioners generally have better supervision of management, thereby affecting the possibility of fraud in presenting the financial statements made by managers, meaning that the more competent the board of commissioners the less likely the fraud in financial reporting (Chtorou, et al., 2001) .

The audit committee plays an important role in the implementation of Good Corporate Governance as it is part of the board of commissioners responsible for overseeing the company's operations. The independence and characteristics of the audit committee also influence the board's decision to take a policy related to financial matters or issues related to the effectiveness of internal control within the company. The audit committee provides professional and independent opinions to the board of commissioners on any report or other matters submitted by the two boards of directors to the board of commissioners, and to identify matters which require the attention of the board of commissioners. (Efendi, 2009).

Research on factors affecting cost of equity capital has been done a lot, but there are inconsistencies on the results of research, research conducted by Widarti and Gunawan (2016) stated that good corporate governance which is proxy with independent commissioner has an effect on cost of equity capital. While research conducted by Nugroho (2014) states that good corporate governance is proxy with independent commissioner does not affect the cost of equity capital.

Research conducted by Nugroho (2014) concluded that good corporate governance which proxies with frequency of audit committee meeting influence to cost of equity capital. In contrast to research conducted by Kurniawati & Marfuah (2014) which concludes good corporate governance proxied with audit committee meeting frequency does not affect cost of equity capital.

Corporate social responsibility is the responsibility of the company's activities internally and externally.

LITERATURE , THEORITICAL FRAMEWORK AND HYPOTHESES LITERATURE

Cost of Equity Capital

Modigliani and Miller (1958) were the first to define cost of equity capital in the financial literature. Modigliani and Miller argue that the cost of equity capital is the cost incurred to finance source of financing. Cost of equity capital from the side of the company is basically the cost borne by the company in the business of obtaining capital from outside, managing capital, until the result of using the capital. While from the investor side, the cost of equity capital is the rate used to calculate the cash flow to be received in the future (Ashidiqi, 2013).

According to Karamony & Wokas (2011), cost of equity capital is the real cost that must be incurred by the company to obtain funds either from debt, preferred stock, ordinary shares, or retained earnings to fund an investment or company operation. Because of its nature as a cost, then the cost of equity capital is also defined as the minimum level of results that must be achieved by the company for the company not to lose.

According Utami (2005), states that the cost of equity capital can be measured by several models of corporate valuation are as follows:

Constant Growth Valuation Model

This model uses the rationale that share value is equal to the present value of all dividends to be received in the future (assumed at constant growth rate) indefinitely.

This constant growth assessment model can be formulated as follows:

$$P_0 = \frac{D_1}{Ks - g}$$

P0 = The value of ordinary share

D1 = Dividends in the first year

Ks = Rate of yield / minimum return of ordinary share

g = Dividend growth rate

Capital Asset Pricing Model (CAPM)

Under the CAPM model, the cost of ordinary share capital is the expected rate of return by investors as compensation for undevaluable risk as measured by beta (Utami, 2005). In a study conducted by Rebecca, (2012) calculation of cost of equity capital by using CAPM formulated as follows :

$$\mathbf{COE = R_f + \beta\,(R_m - R_f)}$$

COE = Cost of equity or expected return of a securities

Rf = The rate of return on risk-free assets

β = Sensitivity of a securities to changes in market value

Rm = Rate of return from the market portfolio (market return)

Model Ohlson

The Ohlson model is used to estimate the value of the firm by basing on the book value of equity plus the cash value of the abnormal profit. In Nugroho's study, (2014). The calculation of cost of equity capital by using Ohlson model is formulated as follows:

$$\mathbf{r = (\ B_t + X_{t+1} - P_t\ )\ /\ (\ P_t\ )}$$

r = Cost of equity capital

Bt = Book value per share in t period

Xt + 1 = Earnings per share in t + 1 period

Pt = Share price in t period

Good Corporate Governance Mechanism

The term Good Corporate Governance was first introduced by the Cadbury Committee in 1992 using the term in their report which became known as Cadbury Report. This report is seen as a decisive turning point for Good Corporate Governance practices worldwide. The Cadbury, Tjager and Deny committees define Good Corporate Governance as a system that directs and controls the company with the objective of achieving a balance between the power of authority required by the company to ensure its sustainability and accountability to stakeholders. This relates to the regulatory authority of the owner, director, manager, shareholder and so on (Hanna, 2015)

Based on the Decree of the Minister of State-Owned Enterprises No. KEP-117 / M-MBU / 2002, Good Corporate Governance is a process of the structure used by SOE organs to improve business success and corporate accountability in order to realize shareholder value in the long term by taking into account interests other stakeholders, based on legislation and ethics.

According to Arief (2009), GCG understanding is a company's internal control system that has the main objective of managing significant risks to meet its business objectives through securing company assets and increasing shareholder value of investment in long term.

The existence of two principal participants and agents led to the emergence of problems concerning the mechanisms that must be established to align the different interests between the two, hence the emergence of good corporate governance mechanism. Corporate governance mechanisms will be able to reduce company resource deprivation and promote enterprise efficiency. This is one fact about the importance of corporate governance.

Good corporate governance usually refers to a set of mechanisms that influence decisions that managers will make when there is a separation between ownership and control some of these controls lie in the function of the board of directors, institutional shareholders, and the control of market mechanisms.

The mechanism of Good Corporate Governance which is suspected to have relationship with cost of equity capital are:

Independent Commissioner

The National Committee on Governance Policy (2006) states that an independent commissioner is a member of the board of commissioners who is not affiliated with management, other members of the board of commissioners and majority shareholders, and is free from business relations and / or other relationships that may affect his ability to act independently or solely for the sake of the company.

The percentage of independent commissioners in this study is consistent with Widarti and Gunawan (2016) calculated using the following formula:

$$IC = \frac{\text{Number of Independent Commissioners}}{\text{Board of Commissioners}} \times 100\%$$

Frequency of Audit Committee Meetings

The existence of the audit committee as part of good corporate governance is regulated in Decision Letter of Capital Market Supervisory Board (BAPEPAM) through Kep-29 / PM / 2004. In performing its functions, duties, and responsibilities, the audit committee is welcome to conduct periodic meetings based on the agreement of the audit committee itself. According to the FCGI article (2002) , the audit committee should hold an audit committee meeting three to four times a year.

In this study, the frequency of audit committee meetings was measured in a way:

Frequency of Audit Committee Meetings = Number of audit committee meetings in one period (Nugroho, 2014)

Quality Audit

Audit quality is an audit performed by a competent and independent auditor. Based on the Standards of Public Accountants Professional (SPAP) audits conducted auditors are said to be qualified, if they meet the requirements or standards of auditing. The auditing standard includes professional quality, independent auditor, judgment used in audit execution and preparation of audit report.

To improve the quality of the audit, a company will use the Public Accounting Firm service with a reputation of good and big names. One is the Big Four, a universally applicable the Public Accounting Firm.

According to Lennex, (2000) in Putranto, (2013) reputation theory predicts a positive correlation between audit quality and the Public Accounting Firm size where if large the Public Accounting Firm size will result in a higher quality audit. This can happen because a large the Public Accounting Firm will recruit qualified human resources with high standards in order to produce good audit results to maintain the reputation it already has.

Corporate Social Responsibility Disclosure

Rawi and Munawar (2010) define Corporate Social Responsibility as a mechanism for an organization to voluntarily integrate environmental and social concerns into its operations and interactions with stakeholders, exceeding the legal responsibility of the organization. The disclosure of its relation in the financial statements implies that the report finance shall provide sufficient information and explanation of the activities of a business unit. Thus, the information must be complete, clear, and able to describe accurately, about the economic events that affect the operating results of business units (Ghozali and Chariri, 2007). Disclosures in Hendriksen and Breda (2002) are defined as the provision or delivery of financial information about a company in the financial statements, usually in the form of annual reports.

THEORITICAL FRAMEWORK

Independent commissioners within the structure of the board of commissioners are in charge and collectively responsible for supervising and advising directors and ensuring that corporate governance in the enterprise is applicable (Widarti and Gunawan, 2016). The growing proportion of independent commissioners can improve the quality of supervision as more and more independent commissioners demand transparency in corporate reporting and disclosure (Gunawan and Hendrawati, 2016). The financial statements of a company that has an independent commissioner will have higher integrity so that it can affect the cost of the company's capital because it can be considered for investors and creditors to determine the requested return (Widarti and Gunawan, 2016). Nugroho (2014) stated that independent commissioners positively influence the cost of equity capital. Independent commissioner variable is measured by calculating the percentage of the number of independent commissioners by dividing the number of commissioners within a company. This result is contrary to research conducted by Widarti and Gunawan (2016) which proves that independent commissioners have no effect on cost of equity capital.

In carrying out its duties, the audit committee is welcome to conduct meetings periodically based on the agreement of the audit committee itself. The meeting was held to bring together different votes or opinions among audit committees. In addition, such meetings may reduce information asymmetry among audit committees. Nugroho (2014) states that the frequency of audit committee meetings affect the cost of equity, which means that the frequency of audit committee meetings will affect the cost of equity capital.

In accordance with the theory of the agency, principal as the owner of the company will tend to appoint the agent of Public Accounting Firm with a good reputation in order to obtain a good audit quality and can reduce the cost of equity capital. The company's financial statements audited by the Public Accounting Firm big four will be more trusted by stakeholders than the financial statements audited by the Public Accounting Firm non big four. This is believed to reduce the cost of equity capital. Research conducted by Nugroho (2014) states that audit quality has a negative effect on cost of equity capital.

Corporate Social Responsibility is an idea that makes the company is no longer faced with responsibility that rests on the value of the company that is reflected in its financial condition only. Awareness of the importance of Corporate Social Responsibility is based on the idea that the company not only has economic and legal obligations to shareholders but also obligations to stakeholders. Corporate Social Responsibility demonstrates that corporate responsibility must rest on the social, economic, and environmental aspects

(Hereuka, 2015). Therefore, companies can use Corporate Social Responsibility information as one of the company's competitive advantages. This will affect the cost of equity capital ..

The linkage between Good Corporate Governance Mechanism, Corporate Social Responsibility Disclosure, and Cost of Equity Capital can be seen in the following figure:

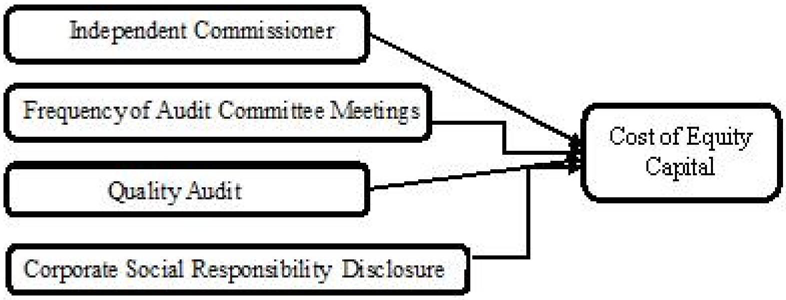

Figure 1
Theoritical Framework

HYPOTHESES

Based on the framework that has been put forward before, it can be arranged research hypothesis as follows:

H1: The Independent commissioners has a positive effect on the cost of equity capital.

H2: The frequency of audit committee meetings has a positive effect on the cost of equity capital.

H3: The Audit quality has a positive effect on the cost of equity capital.

H4: The Corporate Social Responsibility Disclosure has a positive effect on the cost of equity capital.

RESEARCH METHODS

This research is exploratory with a type of investigation of causal studies in which the researcher wants to find the cause of one or more problems (Uma Sekaran, 2007). In this research will be tested the influence of good corporate governance mechanism and corporate social responsibility disclosure on the cost of equity capital.

The population of this study are all banking companies listed on the Indonesia Stock Exchange with a population of 32 banks. Observation periods conducted in this study is for a period of 3 years, including yearly company data year 2013-2015 taken from the official site IDX . The sampling technique used is purposive sampling. Companies that meet the sample criteria are 11 companies.

DISCUSSION

The result of hypothesis testing shows that good corporate governance mechanism which is proxy with independent commissioner has no significant effect on the cost of equity capital. These results indicate that the appointment of an independent commissioner is only limited to the fulfillment of established regulations but has not been addressed for the implementation of good corporate governance within the company. Weak practice of good corporate governance can enable the asymmetry of information between managers and stakeholders that affect the cost of equity capital is not decreased.

The Good corporate governance mechanism which is proxied by frequency of audit committee meeting has no significant effect on the cost of equity capital. These results indicate that the frequency of regular audit committee meetings and often has not been able to reduce the issue of financial reporting. Therefore, the existence of the audit committee has not been able to improve the performance of the company to be better, this resulted in decreased investor confidence to invest in the company so that the frequency of meeting the audit committee has not been able to reduce the cost of equity of the company.

The Good corporate governance mechanism which is proxied with audit quality has significant effect on the cost of equity capital. These results indicate that audit quality measured using Big four the Public Accounting Firm size will be more trusted by stakeholders than firms audited by non big four the Public Accounting Firm . This is because the quality of audit is one component that determines the quality and accuracy of information a company's financial statements. Transparent, accurate, and reliable financial statements are believed to be able to reduce information asymmetry which results in a decrease in cost of equity capital.

The Corporate Social Responsibility Disclosure has no significant effect on the cost of equity capital. This is because the Corporate Social Responsibility Disclosure is only used as a means of fulfilling the obligation of legislation and also informers about corporate responsibility to outside parties in order to know whether the company has run and contribute well or not to the social environment. However, The Corporate Social Responsibility Disclosure does not have a direct impact on cost of equity capital.

CONCLUSIONS AND RECOMMENDATIONS

CONCLUSIONS

1. The Good corporate governance mechanism proxied by independent commissioners has no significant influence on the cost of equity capital.
2. The Good corporate governance mechanism that is proxied with frequency audit committee meetings have no effect on the cost of equity capital.
3. The Good corporate governance mechanisms proxied audit quality has an influence on the cost of equity capital.
4. The Corporate Social Responsibility Disclosure has no effect on the cost of equity capital.

RECOMMENDATIONS

In this study still have limitations - later limits on subsequent research the researchers put forward the following suggestions: For the company to improve the implementation of good corporate governance that already exist so that more useful for the progress of company. In addition, the management is also expected to disclose the Corporate Social Responsibility to be more comprehensive so that it can be used as a reference by potential investors to invest capital. Further research is expected to develop other variables to add references from research that has never been done, but also multiply the research sample to be more representative .

FIGURES & TABLES

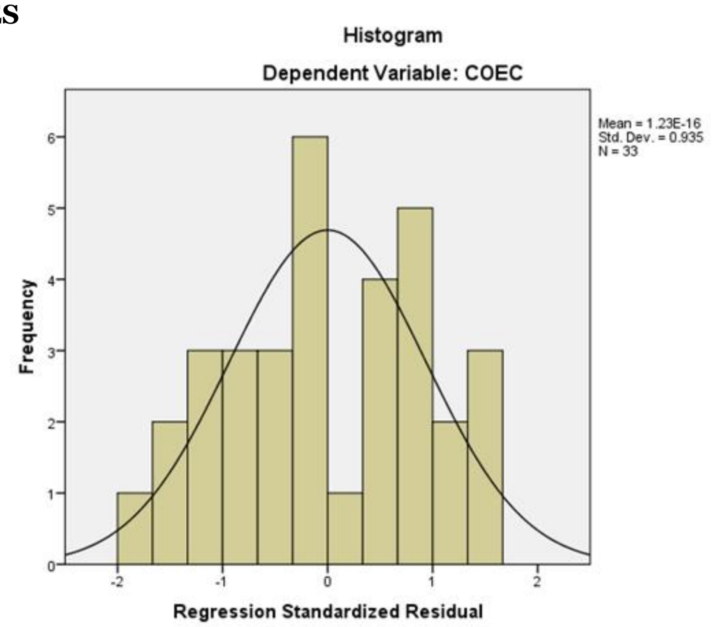

Figure 1 : Normality Test Chart

Source: Results of SPSS Data Processing

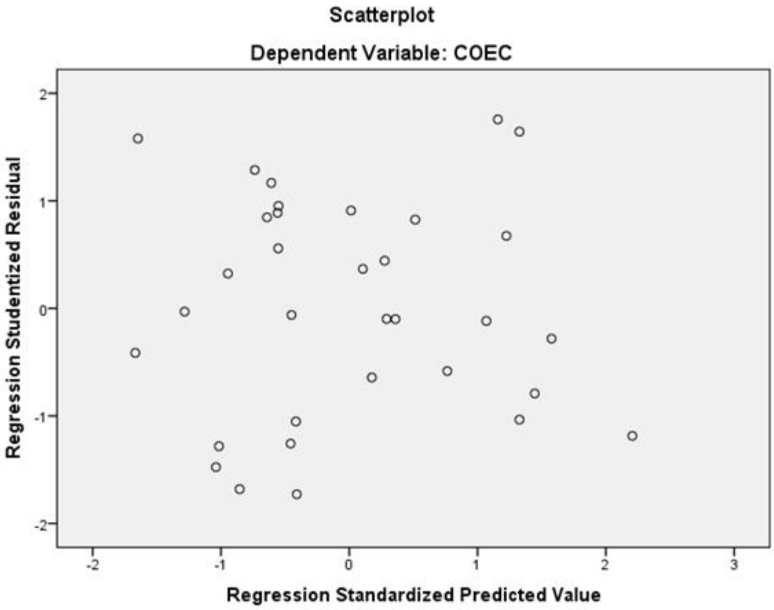

Figure 2 : Scatterrplot Chart

Table 1
F Statistical Test Results
ANOVA[b]

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	.740	4	.185	3.449	.024[a]
Residual	3.573	28	.128		
Total	4.313	32			

a. Dependent Variable: COEC
b. Predictors: (Constant), CSR, KI, FKA, KA

Table 2
T Statistical Test Results
Coefficients[a]

	Unstandardized Coefficients		Standardized Coefficients		
Model	B	Std. Error	Beta	t	Sig.
1 (Constant)	.542	.433		1.252	.221
IC	-.480	.694	-.121	-.692	.494
FACM	-.011	.008		-1.291	.207
AQ	-.261	.174	-.251	-1.502	.044
			-.295		
CSR	.425	.470	.173	.905	.373

a. Dependent Variable: COEC

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