

# CSR's Capability as a Conflict's Resolution to Enhance a Firm's Value in Indonesia

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## ABSTRACT

*The purpose of this research is to analyse the part of agency cost reduction, firm's corporate governance quality in its relation with corporate social responsibility (CSR), and firm's value. The sample used in this research are firms that have CSR information disclose in their annual company's report and firms that are joining corporate governance ranking conducted by The Indonesian Institute for Corporate Governance (IICG) publicized as CGPI (Corporate Governance Perception Index) year 2006-2012. The research outcomes demonstrate that CSR produces a direct positive result to firm's value. It also demonstrates that agency cost reduction has a role as an intermediary between CSR and firm's value. Other outcomes demonstrate that firm's corporate governance quality do not moderate correlation between CSR and agency cost reduction.*

*Keywords:* Agency Cost Reduction, Corporate Governance, Corporate Social Responsibility, Firm's Value

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## 1. INTRODUCTION

The argument about importance of conducting corporate social responsibility (CSR) in Indonesia as one of the firm's business arise with the increased understanding of the advantages CSR have for the firm conducting it. The group that supports CSR see that a firm has obligation to protect and increase communities' welfare in broad term i.e. society. The reason for this is that the society has their part in creating the law and regulation which control firm's business behavior and they are the one that supports the firm's existence by purchasing the goods and services rendered (Solihin, 2011). The group that opposes CSR sees that CSR is more to increase firm's reputation in the public eyes that cause ambiguity in accomplishing its main purpose which is economic productivity. Various CSR conduct are also believed as costs that has to be carried out by the firm and as a result disturbed the firm's profitability (Robbins & Coutler, 2003). Many arguments that have occurred about CSR demonstrate that CSR is still being an important subject at the moment and also still has possibility to develop in the future. Nowadays CSR has become unavoidable

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demand to firms in Indonesia. CSR activities are no longer just about moral responsibility but also a firm's strategy in their effort to create reputation and firm's image which can give positive implication that is increase in the firm's value.

A lot of research prior to this research regarding the implication of CSR to the firm's value has been done, for instance research by (Schnietz & Epstein, 2005) who investigate the implication of firms which have good reputation with those which do not have good reputation for CSR to the firm's financial value during economic crisis. The result demonstrates that there are significant implication for those firms that have good reputation for CSR to the firm's financial value, while those firms which do not have good reputation for CSR are also do not have significant implication to the firm's financial value. This discovery is supported with the research conducted by Orlitzky et al. (2003), Hammann et al. (2009), Carmen, M, & Lisa (2011), Weshah et al. (2012) and Flammer & Caroline (2013) that reported there are significant implication between CSR and increased firm's value.

Research like this is also being done by (Brine et al., 2009) that examine CSR implication to financial performance. The result of this research demonstrates that there is no significant statistic connection between implementation of corporate social responsibility with financial performance. This research is also supported with the research conducted by (Mackey et al., 2007), (Wang & Yungchih, 2010), and (Mwangi & Oyenje, 2012) which reported that CSR statistically does not have significance to increase in the firm's performance.

Researches about the implication of CSR to the firm's value demonstrate results' inconsistencies that CSR has positive implications to the firm's value. This inconsistencies are said by (Harjoto & Jo, 2011) is because of two point of view that are based by agency theory in CSR. The first point of view is based on the over-investment hypothesis which claim that to some firms the top management is conducting CSR by over investing to increase their personal value which is to gain social reputation and as result can reduce the firm's value. The second point of view is based on the conflict-resolution hypothesis which claims that the firms use CSR as one of their activities to reduce agency problem between the top management and various other parties including shareholder which in the end can increase the firm's value.

The foundation of this research is to observe the integrated implication of CSR to the firm's value from the agency theory point of view. CSR from the agency theory point of view is a firm's strategy as a conflict-resolution to agency problem. According to agency theory CSR has the ability to reduce information asymmetry, therefore reducing agency cost. CSR is also a firm's strategy to control manager's opportunistic behavior, by implementing CSR thus require fund allocation which can reduce free cash flow to manager, therefore reducing manager's self-interest. CSR is also a firm's strategy to create reputation and firm's image, thus giving positive impression to the public (impression management), therefore can increase the firm's value.

CSR can be an activity that cause over investment that is when management implementing CSR by over investing to increase their personal value just to gain good reputation (Harjoto & Jo, 2011). With good corporate governance, manager activities are monitored by its system therefore can direct CSR to become conflict resolution and reduce agency problem. Corporate governance is also a media, social control, and reputation. CSR activities which conducted by the firm are also one of their effort to show that the firm has establish good corporate governance. CSR reflects of how the firm's concern to the community and environment. CSR is also activities that are used to perform regulation from the corporate governance. (Haniffa & Cooke, 2005) stated that CSR and corporate governance implementation has a purpose to manage organization for a long term benefit since CSR and corporate governance has the same function that is to enhance organization's competitiveness.

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