International Journal of Innovation, Creativity and Change. www.ijicc.net
Volume 10, Issue 12, 2020

Bank Financial Soundness and the Disclosure of Banking Sustainability Reporting in Indonesia

Sandra Sukma Embuningtiyas[a], O R Puspasari[b], Anak Agung Gede Satia Utama[c*], R I Ardianti[d], [a,b,c,d]Department of Accountancy, Faculty of Economics and Business, Universitas Airlangga, Email: [c*]gde.agung@feb.unair.ac.id

Sustainability reporting is a model of reporting company information to stakeholders that integrates several reports, namely financial, social, and environmental, which are integrated in one reporting package. The purpose of sustainability reports is to provide information to stakeholders that the company does not merely prioritise aspects of profit, but also pays attention to social factors and environmental sustainability. This study aims to investigate whether disclosure of sustainability reporting on banking companies that are measured using content analysis is influenced by bank soundness, which includes risk profile non performing loans (NPL) and loan to deposit ratios (LDR), good corporate governance (GCG), earnings that use ROA as indicators, and capital that is measured by CAR ratio. The sample used is 7 conventional banks in Indonesia that was determined using the purposive sampling method, while the period of analysis was from 2014-2018. Multiple regression analysis was used to analyse the data. The results show that NPL, LDR and CAR don't affect the disclosure of sustainability reporting. While the GCG and earning (ROA) do influence the disclosure of sustainability reports in conventional banking companies in Indonesia.

Key words: *Sustainability Reporting, Non Performing Loan, Loan to Deposit Ratio, Good Corporate Governance, Return On Assets and Capital Adequacy Ratio.*

Introduction

Demand for the disclosure of sustainability reporting for companies is increasing along with public awareness increases of social and environmental issues (Tagesson, Blank, Broberg, & Collin, 2009), strengthened by the enactment of rules that require every organisation, both public organisations and the private sector to disclose sustainability reporting (SR). The CEO's of some world companies are increasingly aware that disclosure of more comprehensive reports (not just financial statements) will support company strategy. In addition, it can show their commitment to sustainable development (CSR Quest in Dilling, 2009). Investors also consider companies with good environmental responsibility to have a small risk, so that the company's market value will increase (Eriandani, Narsa, dan Irwanto, 2019).

The goal of sustainable development is to meet the needs of the present generation by not reducing the ability of future generations to meet their needs (Achmad, 2018). In achieving sustainable development, the support of various parties is needed, and a global framework is prepared that is consistent, using general language in order to make it easy to implemented by various companies; the concept is known as a sustainability report (Suryono and Prastiwi, 2011).

There are several reasons that strengthen a company to apply the concept of sustainable management (Darwin, 2006) on (Sri AuliaandSyam, 2013), including as a kind of social act for the community and the environment, building trust and strengthening relationships and communication with stakeholders, maintaining corporate reputation and reducing corporate risk, (Socially Responsible Investment / SRI), increasing competitiveness in efforts to obtain capital and loans, and improving the quality of human resources and suppliers.

PWC surveys about sustainability practice taken by 79% of CEOs around 33 countries, revealed that "sustainability is vital to the company profitability" (Chariri, 2009). Other surveys conducted on 350 countries in Europe revealed "a company will be more competitive when it is integrating responsible business practices. This condition has led to increased sustainability management practices (Sri Aulia and Syam 2013). Companies need accurate, detailed, and relevant information regarding visible costs and unseen costs, in addition to the necessary limitations on the use of existing resources so that environmental sustainability will be maintained (Agustia, Sawarjuwono, and Dianawati, 2019).

The problem which then arises is how to measure the success of implementation of sustainability management. Sustainability reporting is used as a medium to reveal the results of sustainability management practices that have been carried out by the company (Persson and Vingren, 2017). The guidelines for carrying out further SR compilations were initiated by the Global Reporting Initiative (2006) which has issued guidelines that can be used to measure sustainability management practices by showing several important elements related to economic, environmental and human aspects.

In Indonesia, the implementation of social and environmental responsibilities has also been regulated in the Law of the Republic of Indonesia, however, there are no rules that carry an obligation to conduct and disclose sustainability reporting. The impact is, there are so many companies in Indonesia who have not disclosed sustainability reporting on their annual reports. The banking industry is one of them, as a service industry that is directly related to the community and various stakeholders involved, only a few banks have conducted disclosures on sustainability reporting.

Various factors can influence the company in compiling and disclosing sustainable reporting. Adams C, (2002) said that there are several factors that influence sustainable reporting, which are: company characteristics, general contextual factors, and other internal factors such as CEO identity and CSR committee. Sari's research results (2013) stated that financial performance does not fully affect the company in disclosing sustainability reporting.

This study will analyse the influence of bank soundness measured by the RGEC method. The formulation of the problem in this study includes: the influence of the risk profile proxied by the ratio of NPL and LDR to the bank soundness, how the influence of corporate governance as measured by the GCG ranking index affects the soundness of the bank, how the earnings proxied with ROA influence the bank soundness, and how capital is proxied by the CAR ratio to influence the bank soundness.

The difference between this research and previous research is that in this study the object of research is conventional banks in Indonesia that have gone public. In addition to using banking company objects, this study also uses bank financial health variables as measured by the RGEC method, where bank financial health as measured by the RGEC method is still rarely used in previous studies.

This research is important for several reasons. First, sustainability reports are corporate information reporting models that integrate financial reporting with social reporting, environmental reporting and corporate governance reporting in one integrated reporting package. Companies that disclose sustainability reports can not only show the financial performance that has been achieved, but the company can also show the form of corporate social responsibility towards society and the environment. Second, this research can provide information about factors that can influence disclosure of sustainability reports in banking companies in Indonesia.

Literature Review

The Stakeholder Theory

According to the Stakeholder Theory, a company should operate its organisations on their best practices to make their stakeholders satisfied. Freeman (1984), defines stakeholders as individuals or groups which are affected by the company actions or an individual or group who have ability to support a company in achieving its objectives. The stronger the stakeholders, the more the companies are trying to adapt (Soewarno & Mahrani, 2018).

Gray, Kouhy, and Adams (in Ghozali and Chariri, 2007), stated that the survival of a company depends on stakeholder support, so the company activities should practice to seek their support. The more powerful stakeholders are, the greater the company's efforts to get their support. Social disclosure is considered as part of the dialogue between the company and its stakeholders.

Legitimacy Theory

Legitimacy is very important for companies, since the existence of companies in the environment or social community implies they must interact with the community in the company environment. This is also related to business survival; companies operate in a dynamic environment, so they must try to run a business in accordance with social norms, societies and stakeholders. According to (Michelon & Parbonetti, 2012), this theory explains that companies try to convince people that they operate by following and respecting the norms in the surrounding community. In other words, the organisation wishes to obtain the right to exist because they have carried out activities in accordance with social community expectations.

Sustainability Reporting

According to Elkington (1997) in Lako, 2014), so that companies can grow and develop sustainably, the company is not only profit-oriented but companies must also care and be responsible for the universe (planet) and society (people) based on the triple bottom theory - line of business (3-P). The three concepts, namely profit, planet and people must be disclosed through sustainability reporting. Sustainability reporting is a corporate accountability report to stakeholders that integrates financial reporting with social, environment and corporate governance reporting in one reporting package.

Disclosing sustainability information was a strategy by a company to respond to pressures from society, as well as a medium by a company to report their activities to the stakeholders. As a guide to every organisation that will conduct sustainability reporting, The Global

Reporting Initiative (GRI), as a non-profit organisation produces standards for sustainability reporting with a multi-stakeholder approach (Global Reporting Initiative, 2016). The standard made by GRI is an international standard that can be applied on both a voluntary and mandatory basis by each company. GRI appears to complement the weaknesses of traditional reporting, which are considered to lack sufficient views relating to the implementation of sustainability development, which includes several indicators from each category, covering the economy, environment and social.

Bank Financial Soundness

The rating of bank soundness is based on Bank Indonesia Circular No. 13/24 / DPNP dated October 25, 2011. Banks are required to conduct periodic self-assessments of their level of health and take corrective steps accordingly by using an assessment of factors including risk profile, good corporate governance, earnings (profitability), and capital, which is abbreviated as RGEC.

Risk Profile and Sustainability Reporting

This study uses Non Performing Loans (NPL) and Loan to Deposit Ratio (LDR) as indicators of risk profile. A high of NPL ratio indicates a low level of bank soundness, since the company is not able to manage the distribution of its financing well, so the problematic financing level increases. Companies that have a high level of problematic financing will focus on reforming the company's operational controls, especially related to the distribution of funding. Therefore, it can have an impact on the lack of implementation of sustainability reporting in the company.

The loan to deposit ratio (LDR) describes the ability of the bank in terms of measuring the ability of bank liquidity. This increase in the ratio signals that the bank's management has the ability to market funds that are getting better. In line with the theory of stakeholders, that banks must be able to provide the best performance in this matter by exercising good control on the distribution of credit funds using received funding funds, the better management of liquidity shows that the bank is trying to get the best ratings from its stakeholders. Therefore they have a high tendency to carry out sustainability reporting to improve the company's reputation.

Hypothesis 1: Risk profiles as measured by NPL have a negative influence on the Disclosure of Banking sustainability reporting.

Hypothesis 2: Risk profiles as measured by LDR have a positive influence on the Disclosure of Banking sustainability reporting.

Good Corporate Governance (GCG) and Sustainability Reporting

Good Corporate Governance (GCG) is one of the variables in the RGEC that describes the quality of bank management for the implementation of the principles of transparency, accountability, responsibility, independence and fairness. The bank conducts a self assessment to assess how well the bank's GCG factors are reflected in its composite value. Not only from the financial ratios, corporate governance also needs to be ensured of being in good condition because of the need to anticipate the risks that might be faced by banks that have a negative impact on the bank. In line with the theory of legitimacy, increasing financial performance indicates that the bank is healthy and shows that banks are well managed and do not heed the norms both environmentally and socially, therefore the desire to implement sustainability reporting will increase. This result is in line with Luthfia, (2012), which states that GCG has a positive influence on sustainability reporting, but contrary to (Ratnasari, 2012), the results of GCG have no influence on SR.

Hypothesis 3: Good corporate governance has a positive influence on the Disclosure of Banking sustainability reporting.

Earning and Sustainability Reporting

ROA is used to assess the condition and capability of the bank's profitability in supporting its operational activities. The increase in this ratio signals that the bank is better at running its business and is in line with the theory of stakeholders to be more satisfying to stakeholders; companies that have high profitability ratios have the desire to better enhance the company's reputation to stakeholders, so they tend to be more interested in sustainability reporting. This is in line with Dilling (2009), who states that companies with high levels of profitability tend to disclose sustainability reporting.

Hypothesis 4: Earning has a positive influence on the Disclosure of Banking sustainability reporting.

Capital And Sustainability Reporting

Capital Adequacy Ratio (CAR) is used as a capital proxy in the RGEC model that measures capital adequacy to support risk-bearing assets. Increasing the CAR ratio indicates the the ability of a bank to bear the risk of each productive asset that contains risks. A CAR ratio that is too high illustrates the conservative bank in managing capital, for conservatives banks, in line with legitimacy theory, tend to try to show that bank management is done well by heeding norms and desires in higher disclosure of sustainability reporting .

Hypothesis 5: Capital has a positive influence on the Disclosure of Banking sustainability reporting.

Research Methodology

The methods used in this research are the descriptive and verification methods. The population used is conventional banks in Indonesia, while the number of samples of 7 banks is obtained from the sample selection process based on the purposive sampling method from the period 2014-2018. Content analysis is carried out to analyse the disclosures of sustainability reports. Then panel data regression analysis is performed to test the hypothesis. The equation model used to test the effect of bank soundness ratios on the disclosure of conventional banking sustainable reports is:

SRit = α + β NPLit + βLDRit + βCGCit +βROAit + CARit

Results and Discussion

The estimation results from panel data regression analysis are shown in Table 1:

Table 1: The Result of Regression Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1.334	0.553	2.413	0.022
NPL	0.002	0.008	0.139	0.890
LDR	-0.009	0.005	-1.862	0.073
GCG	0.128	0.057	2.236	0.033
ROA	0.043	0.018	2.466	0.020
CAR	0.002	0.014	0.146	0.885

Risk Profile and Sustainability Reporting

Based on the results of the data analysis obtained, NPL significance value = 0.890 > 0.05, which means that the effect of NPL on banking sustainability reporting (SR) disclosure is not significant. This result is not in line with the initial hypothesis, which states that the risk profile measured by NPL has a negative effect on banking SR disclosure. This shows that banks' soundness measured by risk factors (NPL) does not affect management's consideration in an effort to disclose sustainability reports.

The result for the risk profile as measured by the LDR shows a significance value = 0.073> 0.05, which means that the risk profile associated with managing the credit and deposit ratio has no effect on banking SR disclosure. This result is not in line with the initial hypothesis, which states that the LDR ratio can have a positive effect on SR disclosure. The LDR ratio must always be maintained; the range of LDR is about 90-110 percent, a good ratio shows a good management of loans using adequate funding resources. It can be concluded that management of risk profile measured by LDR ratio does not make management motivated to disclose SR, the concentration of management is to maintain the LDR value so that the company's financial performance will always be maintained. The results of this study are not in line with Belkaoui, et al. (1989), which revealed that the strength of a company as indicated by a high liquidity ratio would be related to a high level of disclosure. However, the results of this study are in line with Sari's findings (2013), which state that there is no influence between liquidity and disclosure of sustainable reports.

Good Corporate Governance (GCG) and Sustainability Reporting

Based on the results of the data analysis, the significance value of GCG was 0.033 <0.05, which means that GCG has a significant positive effect on banking SR disclosure. This shows that better corporate governance can motivate the bank's management to disclose sustainability reports. Companies which have good governance tend to be more fair in providing information. This information is generally carried out by disclosing information that is not only compulsory information, namely financial statements, but about how the company has considered social and environmental factors in carrying out its business processes. The results of this study are in line with Luthfia (2012) which states that GCG has a positive effect on sustainability reporting.

Earning and Sustainability Reporting

Based on the results of the data analysis obtained, earning significance value measured by the ROA indicator = 0.020 <0.05, which means that ROA has a significant positive effect on banking SR disclosure. This shows that higher ROA value, representing higher profitability, should motivate bank management for disclosing other information beside financial performance.

The stakeholder theory supports the result, which explains that the company does not only operate to fulfill its own interests, but also has a responsibility to be able to benefit stakeholders. The company will continue to strive to provide authority to stakeholders by generating high profitability. With the high value of profitability, it will show that management has worked towards its best performance in managing the company's financial performance. In order to get sympathy from stakeholders to the company, after showing good financial performance they will be encouraged to carry out activities related to social and environmental responsibility and disclose them in the sustainability report. The results of this study are in line with Dilling (2009), which states that companies with high levels of profitability tend to disclose sustainability reporting.

Capital and Sustainability Reporting

Based on the results of the data analysis, the significance value of CAR was obtained as an indicator of the capital variable = 0.885> 0.05, which means that the effect of CAR on banking SR disclosure was not significant. These results indicate that the size of the capital ratio in conventional banks does not have a significant effect on bank management to disclose sustainability reporting. In banking companies the composition of capital is strictly regulated by regulators, namely Bank Indonesia. Banking companies must maintain a minimum CAR ratio of 8% of risk-weighted assets. Greater levels of CAR shows the ability of banks to be better at maintaining sufficient capital. However, the concentration of management in maintaining capital ratio does not correlate with the motivation to carry out social and environmental responsibility activities as well as sustainability report disclosure.

Conclusion

Based on the results of testing the hypothesis and analysing the results of the research, the results of this study indicate that the variable risk profile measured by the NPL variable has a positive and not significant influence on disclosure of sustainability report (SR). This shows that disclose of sustainability report isn't affected by the risk profile. In addition, based on the results of the data analysis, it also shows that NPL has a positive direction towards sustainability report disclosure, as opposed to the initial hypothesis, which stated that risk profiles negatively affect sustainability reporting disclosure. While for the risk profile variable measured by the LDR variable it has a negative and insignificant influence. Similar to the risk profile variable, variable capital (CAR) also has no effect on sustainability report disclosures on banking companies in Indonesia. The results of the data analysis show that the CAR variable shows a positive direction towards sustainability report disclosure. Furthermore, for good corporate governance and profit (ROA) variable, the results are different. The results of the data analysis shows that the GCG variable and earnings (ROA) have a positive and significant influence on disclosure of sustainability reports. Thus it can be concluded that bank financial soundness does not fully affect the disclosure of banking sustainability reports. Based on our findings, this research can be useful for standard makers, the public, and investors. This research can provide information for standard makers that, until now, there are still many banking companies that have not disclosed sustainability reporting. Thus, standard makers can encourage banking companies to disclose sustainability reporting. This is because business development is based on three main pillars, namely economic, social and environmental. So it is important for all companies not only to publish financial statements.

REFERENCES

Adhima, M F dan Hariadi B. (2012). The Effect of Sustainability Report Disclosures on Company Profitability: A Case Study of Manufacturing Companies Listed in the Indonesia Stock Exchange. *FEB Scientific Journal UniversitasBrawijaya*. 1(1).

Aggarwal, P. (2013). Impact of Sustainability Performance of Company on its Financial Performance: A Study of Listed Indian Companies. *Global Journal of Management and Business Research Finance*. 13(11).

Dian Agustia, Tjiptohadi Sawarjuwono, Wiwiek Dianawati. (2019). The Mediating Effect of Environmental Management Accounting on Green Innovation - Firm Value Relationship. *International Journal of Energy Economics and Policy*, 9(2), 299-306.

Aryati, T dan Manao, H. (2000). Financial Ratio as Predictor of Problem Banks in Indonesia. *SimposiumNasionalAkuntansi III*.

Eriandani R., Narsa I.M., Irwanto A. (2019). Environmental Risk Disclosure and Cost of Equity. *Polish Journal of Management Studies*, 19(2), DOI: 10.17512/pjms.2019.19.2.10.

Kapereit, Thomas dan Kerstin Lopatta. (2016). The Value Relevance Of SAM's Corporate Sustainability Ranking And GRI Sustainability Reporting in The European Stock Markets. *A European Review*. 25, 1-24.

Lako, Andreas. (2014). "Green Economy".Greening Economy, Business, and Accounting.*PT GeloraAngkasaPratama, Erlangga.*

Mahrani, M. and Soewarno, N. (2018). The effect of good corporate governance mechanism and

corporate social responsibility on financial performance with earnings management as mediating variable. *Asian Journal of Accounting Research*, 3(1), 41-60.

Nakabiito, S and Udechukwu D. (2007). Factors Influencing the Degree of Disclosure Sustainability Reporting, A Study of Swedish Companies Using the GRI Reporting Guidelines. *Master Thesis*, Accounting/International Business Programme, Linkoping Universitet.

Ong, Tze San. (2012). Influence of Enviromental Disclosures on the Financial Performance of Public Listed Malaysian Manufacturing Companies. *Asia Pasific Management Accounting Journal*. 10, 107-136.

Persson, K and Vingren T. (2017). Factors Affecting the Sustainability Disclosures in Swedish State-Owned Enteprises as Hybrid Organizations. *Master Thesis.*

Retnosari. (2016). Comparative Study of the Effect of Sustainability Reporting on Financial Performance in Indonesia and Malaysia. Thesis. UniversitasJenderalSoedirman.

Wibowo, Iman dan Sekar. (2012). Impact of Sustainability Reporting Disclosures on the Company's Financial and Market Performance.*SNA 17 Mataram, Lombok.*