

THE RELATIONSHIP BETWEEN CORPORATE GOVERNANCE STRUCTURE AND THE LEVEL OF VOLUNTARY DISCLOSURE

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Abstract

This study investigates the relationship between Corporate Governance Structure (i.e. board of directors composition and the audit committee) and the level of voluntary disclosures in the annual reports of Indonesian manufacturing public-listed companies. Voluntary disclosure items were determined by observing information presented in annual reports and by referring to a large number of voluntary items found by previous researchers in other countries. These voluntary items were then compared to the Indonesian Accounting Standard and the Capital Market Executive Agency's (BAPEPAM) regulations. From discussions with accounting and finance professionals, a final list consisting of 58 voluntary items were derived. The level of voluntary disclosure is measured cross sectionally for 1999 annual reports using a weighted disclosure index formula. The empirical evidence suggests that the board of director's composition and firm size (as an additional variable) are statistically related to the level of voluntary disclosure. In contrast, the presence of audit committee does not appear to be an important factor in explaining voluntary disclosure level of companies. Arguably, this study makes a positive contribution to the existing research in voluntary disclosures from the perspective of a developing country and that it has provided an interesting dimension to the literature of international accounting.

Key Words : Corporate Governance, Voluntary Disclosure, Structure

INTRODUCTION

This study sets out to investigate the impact of the composition of the board of directors, the presence of the audit committee, and firm size on the level of voluntary disclosure practices in the annual reports of Indonesian manufacturing companies listed on the Jakarta Stock Exchange. Owners almost exclusively dominate the composition of board of directors in Indonesian companies since the majority of stockholders are persons who have family relationships or family owners. They act as managers and also became members of board of directors, so that the composition of board of directors almost exclusively consists of *inside* rather than *outside* members.

An audit committee is a sub-committee of the Board of Directors. The primary role of the audit committee is to provide an independent evaluation of a company's financial reporting functions. Typically this involves assessing both financial reporting to shareholders and others (Fischer, 1994). In recent years, the audit committee has become a major means for companies to monitor the reliability of the financial reporting process. In most countries there is no legal requirement for companies to have an audit committee. In Canada, following the recommendations of the Canadian Institute of Chartered Accountants in 1968, a number of provincial governments have enacted legislations which made it mandatory for public-listed companies to have audit committees. In the United States, since 1978, the New York Stock Exchange requires all listed companies to have an audit committee composed solely of non-executive directors as a pre-condition for listing. While in Singapore, in 1989, the Companies Act of Singapore was amended to require all companies listed on the stock exchange of Singapore to have an audit committee. In Malaysia, in January 1992, the registrar of companies recommended that it is mandatory for companies listed on the Kuala Lumpur Stock Exchange to have an audit committee.

In the UK, the Cadbury report recommended that companies should have audit committees but stopped short of recommending them compulsory. In Australia, the Bosch committee has taken a similar position to the UK. Companies in UK and Australia do not make audit committees mandatory. In summary, it is mandatory for public-listed companies to have audit committees in Canada, the United States, Malaysia, and Singapore whilst it is still not mandatory for other countries.

In Indonesia, the presence of an audit committee is not regulated by both Indonesian Accounting Standard and Capital Market Executive Agency regulation. This is the reason why some companies have and others do not have an audit committee. The rapid growth of Indonesian capital market and the need for better management due to business complexity during the last five years have caused some companies to start employing outside persons (professionals) to be members of board of directors and also to start having an audit committee to ensure better control in the

companies' operations. Therefore, this has become an important issue to be studied. While the results of some previous studies support the prediction that the board of director's composition (Watts, 1977; and Beasley, 1996) and the presence of audit committee (Campbell, 1982; Brown and Sarah, 1990; Henry et al., 1994 and Ali Abdul Hamid, 1999) were related to the board's effectiveness at reducing agency costs and financial statement fraud, none has examined or explored the relationship between the board of director composition and the presence of audit committee and the level of voluntary disclosure practices in companies' annual reports.

Based on this reason, this study examines variations in the board of director's composition to test empirically the prediction that the inclusion of outside members on the board and the presence of audit committee in company's structure help to increase the extent of voluntary disclosure among Indonesian manufacturing companies listed on the Jakarta Stock Exchange. Beside these two variables, this study also includes firm size as another variable. As firms become larger, they face new demands of information from their shareholders and other related parties. Pressure from both shareholders and other users of annual reports is likely to be more intense (Cooke, 1989). This is because large firms may operate in a number of geographical areas. It requires efficient management information systems to meet the need of information for management control. Thus, the variety of information demanded can be expected to increase, resulting in an increased level of voluntary disclosure (Choi and Muller, 1992).

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Based on the agency theory framework, shareholders or investors represents the principal, managers of the company represents the agent. Shareholders or investors are essentially users while the managers of the companies are preparers of annual reports. It is argued that preparers have economic incentives to voluntarily disclose such information in the annual report. Several economic incentives include: lower transaction costs in the trading of the firm's securities, greater interest in the company by financial

analysts and investors, increased share liquidity, and lower cost of capital (Choi et al., 1999). It is also argued that voluntary disclosure leads preparers to face proprietary costs. Proprietary costs refer to the costs imposed on the firm if information disclosed can be used by external parties such as investors, shareholders or employees in a way that is harmful to the firm (Craswell and Taylor, 1992 and McKinnon and Dalimunthe, 1993). Foster (1986) divided costs associated with disclosure into: (a) collection and processing costs, (b) political costs (i.e. government or regulatory bodies will increase such regulations, labor unions are said to gain an advantage in wage bargaining), and (c) competitive disadvantage costs (competitors will use information disclosure to their own advantages. For example, sensitive information such as research and development of new products, and advertising budgets are the sort of information that can be learned by the competitors). If management or preparers disclosed information in the annual reports, it can be assumed that their incentives exceed the costs.

a. The Board of Director's Composition

The board of directors, according to Fama and Jensen (1982), is the highest internal control mechanism responsible for monitoring the actions of top management. They argued that outside directors have incentives to carry out their monitoring tasks and not to collude with top managers to expropriate stockholders wealth. Thus, the inclusion of outside directors increases the board's ability to monitor top management effectively in agency settings arising from the separation of corporate ownership and decision control. *Outside directors are defined to be all non-employee directors.*

Existing empirical research provides evidence about the importance of outside directors on the board for purposes of monitoring management in acute agency settings. Lee et al. (1992) found that in management buyouts, shareholder's wealth increases when boards are dominated by outside directors. Brickley and James (1987) stated that expenditures and salaries are negatively related to the percentage of outside members that sits on the board. The latter study was conducted by Beasley (1996). He examined the relationship between the board of director composition and financial statement fraud. He found that (1) the board of directors' composition is an important factor for reducing financial

statement fraud, (2) the proportion of outside members on the board of director is lower for firms experiencing financial statement fraud compared to no-fraud firms, and (3) the inclusion of outside members on the board of director increases the board's effectiveness at monitoring management for the prevention of financial statement fraud.

There are both internal and external governance mechanisms designed to minimize divergences that arise from the separation of ownership and decision control (Fama and Jensen, 1983). The board of directors is one of internal corporate governance mechanism that has an important function to minimize costs that arise from this separation. The board of director receives its authority for internal control and other decisions from stockholders of corporations. This delegation occurs since stockholders generally divide their risks by owning securities in many firms (Fama, 1980). Although the board delegates most management and control functions to top management, the boards placed ultimate control over top management (Fama and Jensen, 1983). Such control includes the board's right to monitor important decisions, and to choose, dismiss and reward important decision agents (Beasley, 1996).

The composition of individuals that serve on the board of director is an important factor in creating a board to monitor management actions effectively (Fama, 1980 and Fama and Jensen, 1983). Having both *inside* (i.e. management) and *outside* (i.e. non-management) members on the board of directors support the board's effectiveness in monitoring management. Furthermore, Fama and Jensen (1989) argued that it is natural for the most influential members of the board to be the internal managers, because they have valuable specific information about the organization's activities that is obtained from internal mutual monitoring of other managers.

Such information assists the board in being an effective device for decision control. As a result, Fama (1980) and Fama and Jensen (1983) expected the board to include several of the organization's top managers. Williamson (1984) notes that, because managers have huge informational advantages due to their full-time status and insider knowledge, the board of directors can easily become an instrument of management, thereby sacrificing the interests of stockholders.

Domination by top management on the board of director can lead to collusion and transfer of stockholder wealth (Fama, 1980). As a result, corporate boards generally include outside members who act as arbiters in disagreements among internal managers and rectify decisions that involve serious agency problems.

In the context of information disclosure, management have incentives to provide financial information to the investment community (Watts, 1977), so management can be viewed as an agent to whom investors have entrusted control over a portion of their resources (Beaver, 1989, p. 15). The number of items and the quality of information disclosed in financial statement prepared by management are affected by management decision. Management has incentives to supply much favorable information and also to suppress unfavorable information. Favorable information generally will be fully disclosed, but unfavorable information seemed not to. As a result, stockholders (e.g. investors and other users of financial statements) would not know specifically the nature of the suppressed information. To overcome this problem, stockholders delegate their authority to monitor management actions to the board of directors.

Agency theory has been used extensively in the board of directors' studies. It takes the stance that there are only two types of directors: outside and inside directors (Kosnik, 1987, Mallette and Fowler, 1992). The board of directors (on behalf of the principal) is the highest internal control mechanism responsible for monitoring the actions of top management, including monitoring the information that will be stated in the annual reports. To avoid collusion among members in the board of directors, the composition of individual which serve on the board of directors generally include outside members who act as arbiters in disagreements among internal managers in deciding items that will be disclosed. By referring to this reason, the inclusion of outside directors increases the board's ability to influence management in deciding the number of voluntary disclosure items presented in firms' financial statement. From the foregoing discussion, the following hypothesis is advanced.

H₁ : The higher the proportion of outside members on the board of directors, the more voluntary information is disclosed in firms' annual reports.

b. The Audit Committee

Both Indonesian Accounting Standard and Capital Market Executive Agency regulations do not obligate the presence of audit committee. Therefore, in Indonesia, audit committee is not mandatory. As stated above that the need for better management due to business complexity during the last several years influenced some companies to have an audit committee to help them have better control over the companies' operations (particularly in the review of financial statements).

Many researchers have conducted several studies about the presence of audit committee. For example, Campbell et al. (1982) examined the relationship between audit committee and the switching of independent accounting firms. Pincus et al. (1989) examined the function of audit committee in monitoring the process of preparing financial statement for users; and Henry et al. (1994) examined the audit committee's role in monitoring management's selection of significant accounting policies.

In relation to the audit failure, Brown and Sarah (1990) in US examined the relationship between the presence and absence of audit committee and the risk of audit failure. The result indicated there is a significant inverse relationship between audit failures and the presence of audit committees. In relation to the effectiveness of audit committee, Collier (1993) and All Abdul Hamid et al. (1999) examined variables that have an influence on the audit committee's effectiveness. Collier (1993) found that there are six factors that could affect the effectiveness of audit committees in carrying out their responsibilities. These are sound judgment, independence from management, full understanding of the purposes and responsibilities of the audit committee, enthusiastic chairman, variety of backgrounds of the audit committee members and ability to devote the necessary time required to carry out the function effectively. All Abdul Hamid et al. (1999), in Malaysia, analyzed the internal auditor's perception of the effectiveness of audit committees. Findings suggest that the most effective role of audit committee is (1) to review of the annual financial statements and interim reports, and (2) to review analysis of the adequacy of the internal accounting and financial controls of the company. The study also found that the internal auditor views the audit committee's role as a mediator between management and external auditor.

A number of studies have used agency theory to examine the characteristics of firms that voluntarily form audit committee (Pincus et al., 1989; Bradbury, 1990; Henry et al., 1994; Menon and Williams, 1994; Beasley, 1996; and Parker, 1997). Pincus et al. (1989) found that there were differences in size, extent of management, ownership of stock, and proportion of outside directors on the board between firms that voluntarily forms audit committees and firms that do not. Similarly, Menon and Williams (1994) used management ownership, leverage, and size to evaluate audit committee formation and firm reliance on audit committees.

A study by Mc Mullen (1992) examines whether the presence of an audit committee affects the reliability of the financial reporting. Logistic regression was used to compare the audit committee attributes of companies with and without various types of unreliable financial reporting. Research results support the association between the presence of an audit committee and more reliable financial reporting. Specifically, logit regression results indicate that a higher percentage of outside audit committee members with accounting and legal expertise are associated with higher quality financial reporting. There is evidence to show that a higher percentage of outside audit committee members and more frequent meetings are associated with more reliable financial reporting.

Another study was conducted by Henry et al. (1994). The objective of the study was to examine the audit committee's role in monitoring management's selection of significant accounting policies (i.e. choices between LIFO or FIFO, and Accelerated or Straight-line depreciation). Management generally prefers FIFO and straight-line depreciation, while owner-controlled firms prefer LIFO and Accelerated or Straight-line depreciation. The results of the study show that audit committees were not effective in encouraging management of firm to adopt policies beneficial to owners. The same results were found by Campbell, W. and McNeil. (1982) which empirically examined the relationship between audit committees and the changing of independent accounting firms. They suggest that no significant relationship between the presence of audit committee and a company's decision to change auditors. Another study was by Beasley (1996), which examine the effect of audit committee on financial statement fraud. His result

shows that the presence of an audit committee is not necessarily related to lesser financial statement fraud.

By referring to prior research, it can be concluded that it is important to examine the effect of audit committee on the level of voluntary disclosure. Pincus et al. (1989) noted that audit committees are viewed as monitoring mechanisms that are voluntarily employed in high agency cost situations to improve the quality of information flow between principal and agent. The existence of an audit committee can be perceived as indicating higher quality monitoring and should have a significant effect on providing more information to users of financial statement. Similar to Pincus et al.'s study, Fisher (1994) argued that audit committee can bring significant benefits such as it improves the quality of financial reporting by reviewing the financial statements, and increases public confidence in the credibility and objectivity of financial statements. Based on the above discussion, a second hypothesis is proposed:

H₂ : *The level of voluntary disclosure is higher for firms that have the audit Committee than those which have no audit committee*

c. Firm Size.

A number of reasons have been put forward supporting the idea that larger firms will tend to give greater financial disclosure (Buzby, 1975; Shingvi and Desai, 1971). One reason, according to Firth (1979), is that collecting and disseminating information is a costly exercise and perhaps it is the larger firms whom can best afford such expenses. Large firms are quite likely to collect the information needed for corporate report disclosure for their annual management systems and hence little extra cost may be incurred. A second reason is that larger-sized firms tend to be listed on the Stock Exchange and they may go to the stock market for finance more often than smaller firm.

Many disclosure studies (e.g. Chow and Wong-Boren, 1987; Cooke, 1989 and 1991; Hosseln et al. 1994, Surlpto, 1998) suggest that there is a positive relationship between firm size and the extent of voluntary disclosure. Another study by Watts and Zimmerman (1986) and Cahan (1992) put forward political visibility as another potential reason for expecting a positive relationship between firm size and voluntary disclosure.

They argue that managers of politically vulnerable firms are likely to voluntarily choose accounting and disclosure policies that reduce reported earnings, and thereby limit the cost of political intervention (such as higher taxation). Moreover, Firth (1979) suggests that firms that are more visible in the 'public eye' are likely to voluntarily disclosing information to enhance their corporate reputation and public image.

In the agency theory literature, Jensen and Meckling (1976) contended that agency costs increase with the amount of outside capital. Agency theory predicts that larger firms will disclose more information in their accounts to alleviate the potential for wealth transfers from suppliers of outside capital to managers. Size can be measured in a number of ways and there is no overriding theoretical reason to select one rather than another. This study used number of employees to measure the size of company since in Indonesia, number of employees is one of the indicators of size (according to the Indonesian Industrial Department). Based on the above discussions, the third hypothesis is:

H₃ : *The larger the size of the firm, the more voluntary information is disclosed in the firm's annual reports.*

RESEARCH METHOD

a. Sample

The 153 publicly manufacturing companies covered by this study were selected from 246 companies listed on the Jakarta Stock Exchange on 31 December 1999. This sample represents approximately 62 percent of the population of Indonesian public-listed companies for which published annual reports were readily available at the time that the study was carried out.

b. Data Collection

Two types of data (primary and secondary data) were used. The primary data was collected by using mail questionnaire and/or interview to obtain information on two variables: the board of directors' composition, and the presence of audit committee. Secondary data was collected by analyzing the annual reports of all Indonesian manufacturing public-listed companies for the year 1999 to obtain information on two variables: the firm size, and the level of voluntary disclosure. The

voluntary disclosure items were identified by using several steps such as (a) obtaining a preliminary list of voluntary disclosure items by referring to existing literature and findings of prior studies, (b) identifying the voluntary items by comparing them with disclosure requirements of the Indonesian Accounting Standards (1995) and the BAPEPAM's regulations (1996), and (c) conducting a discussion with several professionals such as public accountants, bank officers, financial analysts, and academicians. Their feedback was used to refine the final list of voluntary disclosure items. In order to avoid bias and to provide a comprehensive list of voluntary disclosure items, the items to be selected must meet the following criteria (Hossain et al., 1994): the item is covered in the previous research studies, and the item is not mandated or regulated by the Indonesian Accounting Standard (1995) and the BAPEPAM's regulation (1996). From the analysis, a final list of 58 voluntary disclosure items is obtained.

c. Operational Definition and Measurement of the Variables

The level of voluntary disclosure that is determined using the voluntary disclosure index. The voluntary disclosure index is a ratio of the actual score (V) awarded to a company to the scores that company is expected to obtain (M). M is the maximum score a company can obtain. The voluntary disclosure index will be determined by using a similar manner as previous studies (e.g. Buzby, 1975; Wallace, 1988; Cooke, 1991; and Hossain et al., 1994). While the previous study used an unweighted approach to determine the disclosure index, this study used a weighted approach (Chow and Wong-Boren, 1987). The weighted score of each voluntary item was computed in a manner similar to that in Arifin et al.'s study (2001). They derived item weighted score by using mean score of importance awarded by users and preparers of annual reports of Indonesian public-listed companies. Steps in determining the disclosure index for each company are as follows:

1. Scoring the disclosure items.

$$V = \sum_{i=1}^n di \cdot wSi$$

where:

- $d = 1$ if the item di is disclosed.
- $= 0$ if the item di is not disclosed.
- $n =$ the number of item which actual disclosed by the company.
- $WSi =$ Weighted Score of each item
- $V =$ the voluntary disclosure score (actual).

2. Scoring the maximum score of a company can earn (M).

$$M = \sum_{i=1}^n di \cdot WSi$$

where:

- $d = 1$ if the item di is disclosed.
- $di =$ expected item of disclosure.
- $n =$ the number of item which the company is expected to disclose.
- $WSi =$ Weighted Score of each item
- $M =$ the maximum score of a company can earn

3. The voluntary disclosure index of a company $= V / M$.

The independent variables in this study are the board of directors' composition, the audit committee, and the firm size. The board of directors' composition is measured by the ratio between the outside members and total board's members (Beasley, 1996). Outside members are defined as members who are not involved

in the day-to-day operations (non-managers and non-employees). The audit committee is divided into two categories: presence and absence of it (Campbell and McNeil, 1992; Brown and Sarah, 1990; and McMullen, 1992). This variable is represented by a dummy variable of '1' if the company has an audit committee, and '0' if otherwise. Size is measured by the total number of employees in the companies.

RESULT AND DISCUSSION

a. Descriptive Statistics

Table 1 and table 2 report descriptive statistics for dependent and independent variables covered in this study.

Table 1 shows that the voluntary disclosure level varies from 10 % to 70 %, and the mean score is 29.84 %. The mean score of board of directors' composition is 44.06 %. It means that on average, approximately 44 percent of board members of public-listed manufacturing companies are outside persons. The average mean of size is 3,864 employees.

For audit committee variable, table 2 shows that 39.86 % (61 of 153 public-listed manufacturing companies) have the audit committee. This means that more companies *60.14%) have no audit committee. This is because an audit committee is not yet made mandatory for companies to be listed in the Jakarta Stock Exchange.

Table 1. Descriptive Statistics for Dependent and Independent Variables.

Variables	N	Mean	Std. Dev.	Min.	Max.
Level of VD	153	.2984	.1203	.10	.70
Board of Dir. Composition	153	.4406	.3833	.00	1.00
Firm Size	153	3,864.19	8,287.31	41	68,000

Table 2. Descriptive Statistics for Audit Committee Variable.

	No. of Firms	%
Have an Audit Committee	61	39.86
Have no Audit Committee	92	60.14
Total	153	100.00

b. Hypotheses Testing and Results

To test the hypotheses, an *Ordinary Least Square (OLS)* regression is used to examine whether the board of directors composition, the presence of the audit committee, and firm size have a significant influence on the level of voluntary disclosure practices in the annual reports of Indonesian manufacturing Public-listed companies.

The multiple regression equation is as follow:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e$$

Where:

- Y = The level of voluntary disclosure.
- b₀ = Intercept
- b₁₋₃ = Coefficient of regression.
- X₁ = The Board of directors composition
- X₂ = The Audit committee
- X₃ = Firm Size
- e = Error

A summary of the regression results is presented in Table 3. The multiple regression model is highly significant (p < 0.001). The adjusted coefficient of determination (R square) indicates that 13.30 percent of the variation in the dependent variable is explained by variations in the independent variables.

The coefficients representing the board of directors' composition and firm size are highly significant (p = 0.000 and p = 0.002 respectively),

while the coefficient for the audit committee is not statistically significant.

To test the normality assumption of the regression model, a histogram of the distribution of the residuals was plotted. The distribution approximated a normal curve, suggesting that the data conform to the normality assumption. To test for multicollinearity, Variance Inflation Factor (VIF) was calculated for each of the predictor variables. The largest VIF (1.216) was far below the threshold (VIF=10) as being suggested by Hair et al. (1995). It indicates that there is no existence of multicollinearity problem. Furthermore, residuals from the regression model were plotted against the predicted value of voluntary disclosure and against each explanatory variable to determine whether the error terms of the model had constant variances. A visual inspection of the distribution of residuals using scatter plot and normal plot of regression-standardized residuals suggested an absence of heteroscedasticity.

c. Discussion of Results.

The empirical evidence based on multiple regression analysis indicates that the board of directors' composition is statistically related to the level of information voluntarily disclosed by Indonesian manufacturing public-listed companies (p < 0.01) in their annual reports. These findings provide support for hypotheses 1. This finding supports the evidence that board of directors' composition is related to the board's effectiveness at reducing agency costs, assist firms to overcome financial distress (Frank and

Table 3. Regression Results.

	Variables in the Equation			
	Intercept (β ₀)	Board of Dir. Compstn. (β ₁)	Audit Committee (β ₂)	Firm Size (β ₃)
Value	.105	.0093	.00052	.0048
T	2.075	3.581	.124	3.102
P*	.040	.000	.901	.002
F = 8.774 p = .000		R Square = .150 Adjusted R Square = .133		

* p < 0.05.

Tourous, 1989; Daily and Dalton, 1994), and reducing the experience of financial statement fraud by firms (Beasley, 1996). Empirical evidence shows that most of Indonesian companies' employ outside persons to be the board members. In Indonesia, the board of directors is meant as '*Dewan Komisaris*' (or board of commissioner) since the Indonesian Companies Act still follows the Dutch system. Persons who sit in the boardroom usually are directly chosen by the shareholders in the shareholders annual meeting. Most of the board members have professional skills and consist of academicians, lawyers, government officials, and some public accountants. Shareholders hope that the inclusion of outside persons as members of board directors will increase the board's effectiveness and companies' performance. Presenting complete information in the annual reports is one of management responsibilities to fulfill shareholders' needs, usually through voluntary disclosures. Before the reports are published, board of directors usually reviews and give advice to management about the content and the amount of information disclosed in the annual reports. This might be the reason why the higher the proportion of outside members on the board of directors, the more information is disclosed in the firms' annual reports.

The finding that the audit committee is not statistically significant in explaining voluntary disclosure might be caused by several factors. This could be due to the fact that in the early 1990's, the banking industry was required by government (i.e. Central Bank or Bank of Indonesia) to have an audit committee, but in 1998, this requirement was taken out due to the economic crisis. It could also be due to the fact that an audit committee is not required by government (or not mandated) because of the companies might not placed much importance to having an audit committee. This is supported by the fact that only 40% (62 of 153) of the companies have audit committees. It can be implied that the level of voluntary disclosure is high even for companies with no audit committee. This might be the reason why audit committee variable has no significant relationship with the level of disclosure. Most of managers interviewed stated that there is no need to have an audit committee since they already have an internal auditor who in their opinion can handle the role of the audit committee equally well.

Size is also a factor that influences the level of voluntary items. It is consistent with the findings of previous studies (Singhvi and Desai, 1971; Buzby, 1975; McNally et al., 1982; Chow and Wong-Boren, 1987; Cooke, 1991; McKinnon and Dalimunthe, 1993; Hossain et al., 1994; Klumpes, 1995, and Supto, 1998). It would appear that voluntary disclosure does help manager of companies overcome agency costs. As the firms grow in size, shareholders become more dispersed, and the number of employees becomes bigger and they become aware of the importance of company's information. Managers of large firms are likely to choose voluntary disclosure policies (such as information about social activities, fund-spent employees' welfare, and sponsor of research and education awards) that reduce reported earnings, and thereby limit the cost of political intervention (such as higher taxation). Large firms tend to be 'public eye' (Firth, 1979). They tend to disclose more voluntary information to enhance their corporate reputation and employee image. Another explanation of resulting size as a factor that have a significant influence on voluntary disclosure level is in its relation to seeking new fund. It can be argued that large corporations usually operate in many industries and produce multi-product. Their marketing channels cover large geographic area, including overseas. Consequently, large firms may go to stock markets for finance more often than those smaller firms. Therefore, large firms significantly increase disclosure whenever they seek new funds by providing more information in their annual reports.

CONCLUSION AND LIMITATIONS

This research has sought to investigate the impact of the board of director composition, the audit committee, and firm size on the level of voluntary disclosure practices in the annual reports of Indonesian manufacturing public-listed companies. In doing so, first of all, voluntary disclosure items were determined by observing information published in firms' annual reports and by referring to a large number of voluntary items found by previous researchers. A preliminary list of voluntary items was derived, by comparing the voluntary items to Indonesian Accounting Standard and the Capital Market Agency's (BAPEPAM) regulations and also through discussions with a group of

professional. A final list consisting of 58 voluntary items was then derived. The level of voluntary disclosure is measured cross-sectionally for 1999 annual reports using a general disclosure index formula consisting of 58 voluntary disclosure items. Using the multiple linear regression analysis, the result of this study provides empirical evidence that the board of directors' composition and firm size have statistically significant (at $p < 0.01$) relationship with the level of voluntary disclosure, while the audit committee is not statistically significant. These results mean that hypothesis 1 and 3 were accepted while hypothesis 2 was rejected.

Similar to any other research, this study also has its limitations. The voluntary disclosure items included in this study may not have been exhaustive. However it is exhaustive up to the date of the research. Future researchers should update the number of voluntary disclosure items because there are bound to be changes due to some renewal or additional regulations from the Indonesian Capital Market Agency and Accounting Standards concerning the items that should be disclosed in firm's annual reports.

The analysis of this study only focused on the level of disclosure derived from the calculation of disclosure index based on the existence of such items presented in annual reports. The length of items disclosed, the number of words of items disclosed, location that it is disclosed and also how it is disclosed was not done. Future research can be done focusing on a more detailed measurement of voluntary disclosure. In other words, future research can concentrate on the 'quality' of disclosure rather than just 'presence or absence' of the voluntary disclosure items. Finally, this study only covers three variables that are expected to have impact on the level of voluntary disclosure. Some other variables relating to board's characteristics (such as numbers of board meetings, proportion of outsiders on audit committee, and the board's size) are suggested to be included in further research.

Nevertheless, despite this study has such limitations, it can be considered that the findings of this study have contributed to the existing research in voluntary disclosures from the perspective of a developing country and that it has provided an interesting dimension to the literature of international accounting.

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