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Voluntary Disclosure, Credibility, and Triggering Factors of Voluntary Disclosure: An Overview of Beneficial Study Reviews

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ABSTRACT

The economic development as a trigger of mandatory disclosure has no longer provided information needed by stakeholder, especially the primary users including investors and creditors. The high information demand from stakeholder urges company to reveal their information through voluntary disclosure. An inquiry to voluntary disclosure has been an interesting discussion and extensively studied in Indonesia as well as the rest of the world. It is obvious because the subject solidates relationship between company with investors, attracts potential investors, and reduces capital risk. The ultimate factor of voluntary disclosure (either in Indonesia or worldwide) is size of company. Those companies which reveal voluntary disclosure in the form of information content, wheter good news or bad news, might obtain feedback from the market in form of price increase or price decrease in stock prices.

Keywords: Information Content; Size of Company; Voluntary Disclosure

INTRODUCTION

Constituents or stakeholders of companies require relevant information for decision-making processes. The required information by the constituents is beyond the information obligated to be disclosed by the Financial Accounting Standards Board. Healy and Palepu (1993) state that management and investors need to establish better communication through disclosure strategy in order to reduce the asymmetry between them. If a company has a greater disclosure, there will be more information available to the stakeholders (Putra, 2008). Disclosure is expected to increase the accountability in financial statements as well as information transparency to stakeholders in the companies.

Companies are supposed to provide information more than the one regulated by the Standards Board or known as voluntary disclosure with the purpose of reducing the asymmetry of information to the constituents, particularly the primary users (investors and creditors). Wardani (2012) explains that voluntary disclosure is utilized by the stakeholders to monitor the situation within companies to predict the companies' future prospects. Voluntary disclosure is able to reduce information asymmetry and therefore lowers the agency cost of the company (Watson, Shrivs, and Marston, 2002; Fontana and Macagnan, 2013).

Voluntary disclosure is one of the methods to enhance the credibility of financial statements, so it could help investors to understand the business strategy of companies (Healy and Palepu, 1993). Pownall and

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Waymire (1989) elaborate that disclosure with lacking credibility, e.g. the absence of information content, would be neglected. The credibility of voluntary disclosure has long become a major concern from Securities and Exchange Commission (SEC), where the credibility of which shown by the company management is not perfect yet; it contains private information (Stocken, 2000). SEC itself is a regulatory agency of stock market in America. At first, Securities and Exchange Commission (SEC) was formed because there was stock market crash in 1929 and then the emerging idea of “invisible hand”, so the US. Congress established SEC as the supervisory agency of stock market (Tian and Chen, 2009; Wolk, Dodd, and Rozycki, 2013).

SEC disallows disclosure which is only based on historical and verifiable events, but obliges disclosure to be more forecast-oriented and insists on less verifiable information as it has low credibility (Pownall and Waymire, 1989). SEC issues a statement supporting ‘forward looking information’ by adopting the provision of “safe harbors” which helps to protect management from liability penalty from each company prospect where projection is not made in good faith (Stocken, 2000; Wolk, Dodd, and Rozycki, 2013).

The credibility of voluntary disclosure depends on the degree of contained useful information. Stocken (2000) argues that management focusing on voluntary disclosure will attempt to disclose private information. This sort of information could be signaling the investors. Raffournier (1995) and Williams (2001) explain that there are some factors from the company, e.g. the size of company, profitability, debt, monopoly rate, and the ratio of market value to company book value which motivate the management in either performing or voluntary disclosure or hiding the information.

Voluntary disclosure is not only used to protect the primary users but also to help investors and creditors to forecast the company performance. Voluntary disclosure may contain either good news encouraging the management incentive which eventually affects the stock price or bad news (Wijaya, 2009). Basically, when being related, the information contained in company disclosure would point out the signal given by the company to its stakeholders. The information given in voluntary disclosure is not entirely representative. Stocken (2000) uses cheap talk game and its results show that management would provide costless information to the investors and could manipulate voluntary disclosure through noisy signal in the form of opportunity’s earnings and management private information owned by a company.

Studies on voluntary disclosure have been carried out many times. Research done by Lang and Lundholm (1996) has shown similar result; disclosure could stimulate investors’ interest, reduce information asymmetry and minimize company's cost of capital. Levinshon (2001) in his article states that voluntary disclosure served by a company in informative manner could be useful for investors to help them understand the company’s strategy, determining factors of company’s success, management framework, and steps taken by the company to ensure their sustainability.

Wardani (2012) has conducted studies on factors affecting the extent of voluntary disclosure. The result of which demonstrates that the size of company and profitability is positively correlated to the extent of voluntary disclosure. Meanwhile, the company’s age is negatively correlated to voluntary disclosure. Research by Stocken (2000) on credibility of voluntary disclosure reveals that the quality improvement of mandatory disclosure would raise the quality of voluntary disclosure. In a longer term, penalties toward management would be effective so they would be encouraged to provide real and non-manipulated information in voluntary disclosure.

Voluntary disclosure would become an effective strategy for companies as it enables them to develop the trust from primary users and to win the market because of the presence of economic globalization and stock market. Information contained in voluntary disclosure does not depend on information within mandatory disclosure; information revealed in voluntary disclosure could be bad news and good news (Bagnoli and Watts, 2007). Market would respond to the information disclosed by management; the better the information (good news) the more positive the response given by the market will be. Langberg and Sivaramakrishnan (2010) elaborate that market would give a much quicker response toward bad news disclosed by a company. Such response would be seen through the change of stock price, either the increase or decrease of company’s stock price.

CONCEPTUAL FRAMEWORK

Financial Statement

Kieso (2010) states financial statements are means to provide information to external parties. Financial statements provide information related to historical transaction and recorded in monetary unit. These statements would be later on made use by the user, particularly investors to make a decision.

Godfrey, *et al* (2010) explains that financial statements are part of financial reports. Financial statements include statements of financial position, income statements, statement of equity changes, cash flow statements, and disclosure.

Disclosure

Disclosure covers all information contained in financial statements and their additional supporting communication, such as footnotes, post-reporting events, management discussions and analysis for future operations, forecasts of operating and finance, summary of accounting policies, and additional financial statements, which include segment disclosure and expansions other than historical cost (Wolk, Dodd, and Rozycki, 2013). Wardani (2012) argues that there are two sorts of information disclosed by an institution, i.e. mandatory disclosure or is oftentimes defined as disclosure which is obligatory fulfilled by a company and voluntary disclosure or described as disclosing information voluntarily besides the obligated ones.

There are two functions of disclosure defined by SEC, i.e. protective disclosure which means the information disclosure given to SEC to protect investors from unfair business practices, and informative disclosure which is a complete information disclosure intended to investment analysis (Wolk, Dodd, and Rozycki, 2013). Table 1 would elaborate the difference between voluntary disclosure and mandatory disclosure.

Table 1. The Difference between Voluntary Disclosure and Mandatory Disclosure

| Aspect | Voluntary Disclosure | Mandatory Disclosure |
|--------------------|--|---|
| Definition | Other than mandatory disclosure, information disclosed by companies is intended to project company's image, to maintain relation with the investors, and to avoid the risks. | The mandatory information to disclose is based on securities law, accounting principles, and regulatory agents. |
| Motive | Communicating the information with the purpose of self-interested between companies and stakeholders. | Implementing the law and regulations to adjust the communication of information between companies and stakeholders. |
| Content | Companies' future strategy, research and development plans, information forecasts, purchase and merger forecasts, investment project analysis, financial information analysis. | Company orientation, basic financial information, information about the Board and top managers, the explanation of essential items. |
| Carrier | Annual report, public announcement, website, road show | Annual report, interim report, season report |
| Time | At the right time | One-period fixed time |
| Mechanism | Design mechanism of <i>corporate governance</i> and effectiveness | Regulatory law and its execution |
| Root of disclosure | Economic and market stock globalization | Monopoly of information by companies |

Source: Tian and Chen (2009)

Voluntary Disclosure

Voluntary disclosure is a disclosure system broader than the mandatory one (Tian and Chen, 2009). McIntyre (1997) explains that voluntary disclosure is an accurate maneuver strategy and something simple for a company to do. FASB (2001) defines voluntary disclosure as:

“... the provision of information by the company management which is not explicitly required by the existing regulation such as generally accepted accounting principles or an SEC.”

The connecting dots of voluntary disclosure are the provision of information by the management which is beyond the existing regulation as the company's strategy to establish relation with primary users. A study carried out by Gu and Li (2007) as well as Langberg and Sivaramakrishnan (2010) show advantages and feedback received by companies from providing voluntary disclosure. In their study, Gu and Li (2007) explains that voluntary disclosure is an innovative strategy which is positively related to the reaction of stock price preceded by insider purchase transaction.

Langberg and Sivaramakrishnan (2010) conduct a study on voluntary disclosure and feedback analysis where the result of which is in line with Gu and Li's, i.e. voluntary disclosure provides feedback to the company and in a short term, there is an implication in price, while in a longer term, the feedback would be in a form of company profit efficiency. Langberg dan Sivaramakrishnan's study (2010) also results in bad news affecting greater response by the market toward the stock price compared to good new; the manager disclosing bad news information would receive response on the decrease of stock price.

According to McIntyre (1997), the underlying purpose of performing voluntary disclosure is to encourage free information flow, establish relation among stakeholders, implement the existing regulation effectively and avoid violation. Manager's incentive in both short and long terms has huge implication in determining the strategy to reveal the information through company's disclosure as well as the response given by the market (Langberg and Sivaramakrishnan, 2010). The conclusion drawn from voluntary disclosure performed by a company is the improvement of financial statements quality through enhancing the flow of information and strengthening the relation among stakeholders. Eventually, this would affect the market's response towards the companies which is reflected through the stock price.

Voluntary Disclosure Credibility

Stocken (2000) did a study to assess the credibility of voluntary disclosure through cheap talk game with the purpose of testing information disclosure performed by management. The result of the study shows that the manager would always make determined attempts to disclose private information and disclosure credibility could be seen from mandatory disclosure and it has been able to increase voluntary disclosure credibility.

Meanwhile Gu and Li (2007) conducted research on disclosure as innovative strategy for hi-tech companies. Gu and Li (2007) assume that hi-tech companies have a possibility of making big insider trading transaction, so information asymmetry is higher. The result of their study shows that disclosure credibility relies on whether or not the information given is trusted. The degree of trust built up by the investors toward the information is measured through market's reaction to stock price and new information. The research reveals that investors perceive disclosure performed by hi-tech companies as good news or in other words, insider purchase transaction increases disclosure credibility; high disclosure credibility is resulted from companies with high information asymmetry.

Studies on Factor Affecting Voluntary Disclosure in Indonesia and Some Other Countries

Studies on factors which affect voluntary disclosure on companies have been conducted many times. The research intends to investigate voluntary disclosure in the United Kingdom, United States, European continent, New Zealand, Australia, Japan and Indonesia.

Watson, Shrikes, and Marston (2002) carry out research to test the factors affecting voluntary disclosure to 313 companies in the UK. The testing is done by measuring the ratio of disclosure to company profitability, return on investment, gearing, liquidity, company efficiency, size and industry. The result

suggests that the performance, size and industry of the company significantly affect the ratio of company disclosure.

Meek, Roberts, and Gray (1995) study the factors affecting the reports of voluntary disclosure in 64 companies in the UK, 116 companies in the U.S. and 26 companies in European continent. The result of the study demonstrates that factors which affect voluntary disclosure in the three countries are the size and location of the company, as well as other additional variables, i.e. listing status and profitability.

The next research conducted by Hossain, Perera, and Rahman (1995) examines voluntary disclosure in New Zealand. This study tests the relation among 5 specific characteristics, i.e. company size, financial leverage, asset proportion, types of auditors, and listing status in the areas which emphasize the importance of voluntary disclosure toward its practice in companies in New Zealand. The outcome of the study shows that particular characteristics, such as size, leverage, and listing status of the company is strongly related to voluntary disclosure in companies in New Zealand. The companies in New Zealand utilize voluntary disclosure as their strategy to attract the investors' interest.

Mitchell, Chia, and Loh (1995) analyze the actors influencing voluntary disclosure in mining and oil companies in Australia. Their study examines whether these factors influence voluntary disclosure: company size, financial leverage, asset proportion, earnings volatility, diffusion, owner, and the interest of the minority toward voluntary disclosure in Australia. The finding suggests that the size of the company as well as financial leverage have significant influence toward the degree of disclosure in the companies.

Meanwhile, a study conducted by Cooke (1992) investigates the factors which affect the voluntary disclosure in the reports of companies in Japan. Japan has a unique business environment and reporting regulation. The outcome of Cooke's study (1992) shows that company size, listing status, and types of industry have significant influence toward voluntary disclosure in the information contained in the companies' financial statements.

Wardani (2012) conducts studies examining the factors that influence voluntary disclosure in Indonesia. The samples of the study are 79 companies in Indonesia and the research is conducted through testing the factors of company size, i.e. leverage, the percentage of shares owned by public, company liquidity, company profitability, and the company's age toward the extent of voluntary disclosure of the information contained the companies' financial statements in Indonesia. The study reveals that the size and profitability of the company positively affect the extent of voluntary disclosure, while company's age negatively affects voluntary disclosure.

Table 2 presents the summary of the previous research findings on factors affecting the extent of voluntary disclosure in companies' financial statements, both in Indonesia and abroad.

Table 2. Factors Significantly Affecting Companies' Voluntary Disclosure in Indonesia and Abroad

| Author(s) | Year | Country | Factors with Significant Influence |
|------------------------------|-------------|---|---|
| Watson, Shrives, and Marston | 2002 | United Kingdom | The performance, size and industry of the company |
| Meek, Roberts, and Gray | 1995 | United States, United Kingdom, European continent | The company's size, location of establishment, listing status and profitability |
| Hossain, Perera, and Rahman | 1995 | New Zealand | The company's size, leverage and listing status |
| Mitchell, Chia, and Loh | 1995 | Australia | The size and financial leverage of the company |
| Cooke | 1992 | Japan | The company's size, listing status, and types of industry |
| Wardani | 2012 | Indonesia | The company's size and profitability positively affect the extent of voluntary disclosure, while the company's age negatively affects voluntary disclosure. |

The aforementioned studies show that the factors affecting voluntary disclosure both in Indonesia and other foreign countries; in general, most companies are affected by the company size. The conclusion drawn is that the bigger the company size, the broader the voluntary disclosure is produced. Big-sized companies oftentimes utilize voluntary disclosure as an innovative strategy to build up the relationship, particularly with the investors.

Other influential factors in voluntary disclosure are mostly similar among companies, such as listing either in the U.S., UK—as a country using Anglo American Model prior to IFRS convergence, as well as European continent and Japan—both last time used Continental Model before IFRS convergence.

In Indonesia, the influential factor in the research conducted by Wardani (2012) suggest that big-sized companies would likely have incentives to perform more voluntary disclosure compared to small-sized companies and the big ones usually have bigger profitability. The company's age has negative ratio to voluntary disclosure in companies in Indonesia. Therefore, even though the company's age is older, it does not mean that the company fully understands the information required by the stakeholders.

Signaling Theory

Signaling Theory explains that companies would perform voluntary disclosure to public with the purpose of lowering the capital risk, developing the ability to compete in capital market and increasing company value as public positive response (Wolk, Dodd, and Rozycki, 2013). In addition, Bagnoli and Watts (2007) elaborate that the information within the companies, either good or bad news, would determine whether or not companies would give voluntary disclosure.

Voluntary disclosure would trigger public feedback (Langberg and Sivaramakrishnan, 2010). Furthermore, Wolk, Dodd, and Rozycki (2013) state that companies with good news information would likely raise the company earnings, while companies containing bad news information would undergo decrease of earnings. Gu and Li (2007) believe that disclosure of good news in company's disclosure would increase the company's strategy value and this is supported by Langberg and Sivaramakrishnan (2010); they reveal that public would respond more quickly to companies with bad news information rather than those with good news information.

CONCLUSION

There are four conclusions that could be drawn according to this analysis of literature. Firstly, voluntary disclosure is performed by big-sized companies as an innovative strategy to establish communication and attract customers as well as lowering the capital risk. Voluntary disclosure is an effective means used by companies to gain positive appraisal from the stakeholders.

Secondly, companies' voluntary disclosure in United Kingdom, United States, New Zealand, European continent, Australia, Japan, and Indonesia, is generally affected by the size of the company. The bigger the size, the broader the voluntary disclosure would be resulted from. Thirdly, another factor affecting the coverage of voluntary disclosure relies on where the companies are situated. Diverse locations of companies could result in cultural differences and various types of demand from the stakeholders. Consequently, the voluntary disclosure performed would also be different.

Fourth, when companies publish voluntary disclosure, they are affected by the information contained in the companies. Either bad news or good news information would determine how markets respond to company's stock price. Good news information would likely increase the value of company's stock market, while bad news information would lower the company's stock market value.

There are several recommendations for the development of the future research based on this voluntary disclosure analysis. First, during the situation of uncertainty due to COVID-19 pandemic, the upcoming research could take account of carrying out comparative study on voluntary disclosure among companies on the national level. Secondly, the future studies could consider state ownership within companies.

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