



## **THE EFFECT OF PROFITABILITY, FUNDINGS, AND FINANCING FOR CORPORATE SOCIAL RESPONSIBILITY DISCLOSURE IN ISLAMIC BANKING**

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### **ABSTRACT**

*The purpose of this study is to analyze the effect of profitability, fundings, and financing on the disclosure of Corporate Social Responsibility in Islamic Banks in Indonesia. The sample used was 11 Islamic banks in Indonesia which were listed on the Indonesia Stock Exchange and consistently published financial statements and corporate social responsibility reports for the period 2012-2018. The analysis of this study uses the multiple regression method (multiple regression). The results of the study explained that Profitability, Fundings and Financing together have a significant positive effect on CSR (Corporate Social Responsibility). Constraints that are still commonly found in the implementation of CSR are cost issues, competent human resources, distribution of activities and determination of targets, forms of activities, licensing and regulatory issues, lack of partnerships, socialization of activities, understanding of implementation and evaluation in the field, and many persons who carry out illegal levies on the ground.*

***Keyword: Corporate Social Responsibility, Profitability, Fundings, Financing, Islamic Banking***

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## **INTRODUCTION**

The beginning of the development of the global Islamic Financial Institutions began since it was founded in the mid-1970s and continues to experience rapid development. Data from the Islamic Financial Service Board (IFSB) in the IFSI Stability Report which shows the value of total assets owned by global Islamic financial institutions was around 1.9 trillion USD in 2016. Basically all financial institutions, both conventional and sharia, play an important role in society . Therefore financial institutions are expected to be more responsive to the needs of its stakeholders who have a broad scope (Molyneux, et al, 2014).

The development of sharia banking in Indonesia began with banking deregulation in 1983. Bank Indonesia gave banks the freedom to set their own interest rates. The deregulation gave rise to the concept of a Sharia Bank, namely the idea of a revenue sharing system by the government. The first Islamic bank in Indonesia is PT Bank Muamalat Indonesia (BMI) which is the result of a working group formed by the Indonesian Ulema Council (MUI) in 1990 in an effort to establish an Islamic Bank in Indonesia. PT Bank Muamalat Indonesia was established on November 1, 1991 and officially began operating on May 1, 1992. During the pioneering phase of Islamic Banks in Indonesia, there were no regulations that specifically governed sharia banking. The legal basis which contains the new sharia system is contained in one paragraph concerning "banks with profit sharing systems" in Law number 7 of 1992. Details on the operations of sharia banks such as the legal basis and types of businesses that were permitted at that time still did not exist.

In general, companies have a goal to seek the highest profit, now the goal is seen as the business world is no longer acceptable (Weshah, et al, 2012). The company is not only concerned with the owners of capital and the interests of management but also maintains relationships with employees, consumers, the community and the environment, this can be realized with social responsibility or CSR (Corporate social responsibility). According to (Cajias, et al, 2014), the stronger the financial condition of a company, the more it will reveal its broader social responsibility and the greater or more active implementation of CSR. Social responsibility is considered important in an organization where stakeholders will ask for disclosure of social responsibility to be included in the company's annual report to balance the company with the community and the environment. CSR is good for companies to make investment decisions.

Disclosure of Corporate Social Responsibility (CSR) is no less important than disclosure of financial performance. One of the advantages of revealing CSR is that parties outside the company can find out how far the company cares about its social environment. capital market indices that include the category of shares of companies that have practiced and disclosed CSR. For example, the New York

Stock Exchange has the Dow Jones Sustainability Index (DJSI), the London Stock Exchange which has a Socially Responsible Investment (SRI) Index and the Financial Times Stock Exchange (FTSE) which has FTSE4Good. And the Indonesia Stock Exchange (IDX) has the SRI Kehati Index which was launched in 2009 (Khlif, et al, 2015).

Public recognition of the importance of social activities carried out by companies, especially financial institutions, increasingly makes the demand for Islamic banks increase. Normative principles that exist in the teachings of Islam concerning people who care about each other and share, become a social responsibility that must be carried out by the Sharia Bank (Dhaliwal, et al., 2011) because Islam is based on the principle of equal rights owned by each individual and also maximizes prosperity socially, Islamic banks that follow Islamic principles are an important task to take part in social activities that benefit many people.

The phenomenon of the application of Islamic law-based economies (sharia) throughout the world continues to increase significantly, including in the banking world (Baird & Roberts, 2012). This is indicated by the increasing operation of Sharia-based Banks in all parts of the world including Indonesia. Islamic banking institutions which in their operations are based on Islamic law or Islamic law with reference to the Qur'an and Al Hadith. Thus, in every business interaction and company activities with all stakeholders, including the social environment of the surrounding community, it is based on Islamic sharia (Adeyanju, 2012).

Furthermore, the Government of Indonesia and the House of Representatives (DPR) in 1998 made improvements to Law No.7 of 1992 to Law No.10 of 1998, which states clearly that there are two types of banking systems operating in Indonesia, namely banking with conventional systems and banking with sharia system. The legal basis for sharia banking continues to be complemented and refined including the Government enacting several laws to stimulate Islamic financial market activities. The next phase began to emerge other Islamic banks such as Bank Syariah Mandiri, Bank IFI, and other Islamic banks. In the end, the Government issued a special regulation on Islamic banks in Law No.21 of 2008 concerning Islamic banks that contained details about the regulations and operations of Islamic banks in Indonesia.

Islamic bank activities use the profit sharing principle that replaces the principle of interest in conventional banks (Wu & Shen, 2013). The view of the progressive Ulama group states that there is no need to create new banking products in the global banking industry, Sharia Banks only need to change the products offered by conventional banking so that they meet Islamic legal requirements. On the other hand there are Ulama who oppose the practice of conventional finance so that Islamic banking needs to apply sharia law and social responsibility into sharia bank business practices strictly (Kiliç, et al, 2015).

Islamic banks are expected to carry out the role of wealth redistribution (through profit sharing) into investments that are considered to be able to contribute to the progress and welfare of the community. This Islamic Bank practices the philosophy of "moral economy" outlined as a reason for religious ethics and supports the inclusion of social and environmental objectives in their investment policies. Thus the Islamic Bank must strive to strike a balance between providing returns for shareholders and their customers, while not forgetting social responsibility and commitment to various stakeholders (Becchetti, et al, 2012).

The Islamic Bank's social role is expected to provide economic and social benefits to the stakeholders by fulfilling its social responsibility or CSR (corporate social responsibility) as well as reporting. (Taskin, 2015) states that the reporting of social responsibility is concrete evidence of Islamic Bank involvement in social activities. Islamic financial institutions may not publish reports on their social responsibilities, even if they carry out these activities.

International institutions such as the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) have developed standards for Islamic Financial Institutions in Islamic financial, legal and ethical aspects. In the standards made by AAOIFI it is explained that CSR is all activities carried out by Islamic financial institutions as financial intermediaries for individuals and institutions to fulfill responsibilities to religion, economics, regulations, ethics, and others. In accordance with this AAOIFI standard, reporting activities carried out by Islamic banks in fulfilling their social responsibilities will be different from conventional banks (Cornett et al, 2016).

Research on CSR in Islamic Banks has not been done much. Most studies use content analysis methods to calculate the number of CSR activities reported in Sharia Bank annual reports. The standard for calculating CSR for Islamic institutions has not been clearly stated in the policy. In this research content analysis is used to see how far Islamic banks carry out CSR practices (Servaes, & Tamayo, 2013). The measurement used to see the relationship of CSR uses the amount of fund expenditures undertaken by Islamic Banks in Indonesia in carrying out its CSR activities. This method is used to find out whether the greater distribution of CSR funds can provide returns that can increase bank motivation towards the practice of CSR distribution.

(Migdad, 2017) examines CSR practices at Islamic Banks in Palestine in the perspective of contributions to socio-economic development. Research findings indicate that CSR practices are highly prioritized by Islamic banks in Palestine, but the contribution of CSR to Islamic banks in Palestine is small and has a marginal effect on the socio-economic development of the community. (Ahmed & El-belihy, 2017) investigated the disclosure of corporate social responsibility of Islamic banks in the UK, the results showed a tendency for poor disclosure among Islamic banks in Muslim countries, these results were also

supported by British Islamic banks, which left their status quo on CSR disclosures. (Platonova et al, 2016) examined the impact of corporate social responsibility disclosure through financial performance as evidence from the GCC of the Islamic banking sector.

(Matuszak & Róžańska, 2017) assessed the relationship between CSR Disclosures and financial performance in banks in Poland, the results found a positive relationship between bank CSR disclosures and profitability as measured by ROA and ROE. However, the relationship between CSR disclosures and NIMs is negative. The Bank's CSR activities in Poland are not the main objective of profitability. (Hapsoro & Sulistyarini, 2019) examined the effect of profitability and liquidity on CSR disclosures and saw how their implications for economic consequences, the results obtained indicate that profitability has a significant and positive effect on CSR disclosure, whereas liquidity does not affect CSR disclosure. Furthermore, CSR disclosure has a negative effect on bidask spread, CSR disclosure has a positive effect on trading volume, while CSR disclosure does not affect stock price volatility.

The research framework compiled in this study is based on a theoretical study and the presence of several previous research results that have been reviewed. Below is the research framework in this study:

So the hypothesis appears as follows:

- H1: Profitability (EBIT) partially influences CSR (Social Responsibility) partially.*
- H2: Corporate Fundings have a positive effect on CSR disclosure (Social Responsibility) partially.*
- H3: Financing has a positive effect on CSR (Social Responsibility) partially.*
- H4: Profitability (EBIT), Fundings, and Financing have a positive effect on CSR (Social Responsibility) simultaneously.*

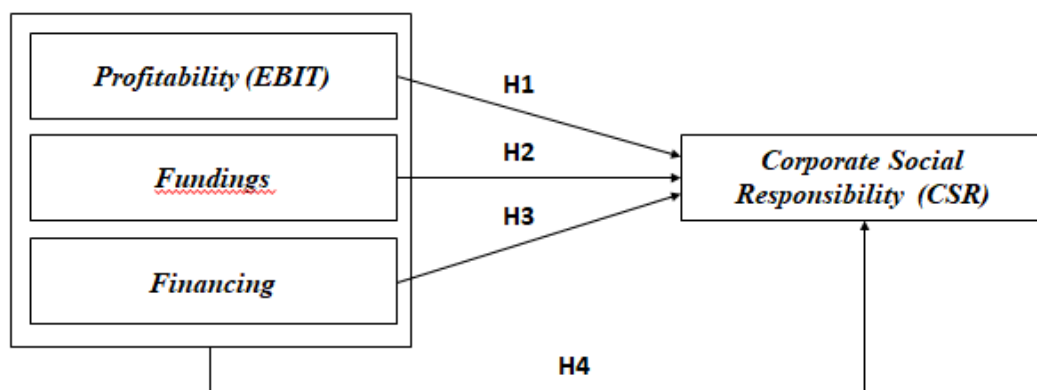


Figure 1  
Research Framework

## **METHODOLOGY**

The type of data used in this study is secondary data. The population in this study is the Shariah Bank of Indonesia on the Indonesia Stock Exchange for the period 2012-2018. The sample used was 11 Islamic banks in Indonesia. Sampling in this study uses purposive sampling with the criteria (1) Companies that always report their financial statements during the 2012-2018 period, and (2) companies whose shares are always owned by management during the observation period (2012-2018). The analysis of this study uses the multiple regression method (multiple regression). Information on social responsibility can be calculated using CSDI (Corporate Social Responsibility Disclosure Index) (Dixon-Fowler, et al, 2013).

$$CSDIt = \frac{Items\ Revealed}{Total\ Items}$$

Variable profitability is proxied by EBIT. EBIT is an indicator of a company's profitability, calculated as revenue minus costs, excluding taxes and interest. The EBIT formula is:

$$EBIT = Net\ Income + Interest + Tax$$

The formula for Fundings is:

$$Total\ Fundings = the\ amount\ of\ current\ accounts + deposits + certificates\ of\ deposit + savings$$

Variable formulation of the amount of financing is the total amount of financing carried out by Islamic banks.

$$Total\ Financing = Amount\ of\ financing\ for\ sale\ and\ purchase + Amount\ of\ finance\ for\ rent + amount\ of\ financing\ for\ profit\ sharing$$

## **RESULT**

The statistical method used to test the hypothesis is multiple regression, this is in accordance with the formulation of the problem, objectives and hypotheses of this study. The multiple regression method links one dependent variable with several independent variables in a single predictive model. Multiple regression tests are used to test the effect of profitability, fundings, and financing to CSR (Corporate Social Responsibility).

Statistically the accuracy of the sample regression function in the actual estimation can be measured from the statistical value of t, the statistical value of F and its coefficient of determination. A statistical calculation is called statistically significant if its statistical test value is in a critical area (the area where Ho is

rejected). On the other hand, it is called insignificant if the value of the statistical test is in the area where  $H_0$  is accepted. Hypothesis testing uses time series data analysis which aims to see the effect of independent variables on the dependent variable and the ability of the model to explain CSR (Corporate Social Responsibility) in Profitability, Fundings, and Financing.

The results of multiple regression tests are as follows:

Table 1  
Multiple Regression Test Results

| Model |            | Unstandardized |            | Standardized | T     | Sig.  |
|-------|------------|----------------|------------|--------------|-------|-------|
|       |            | Coefficients   |            | Coefficients |       |       |
|       |            | B              | Std. Error | Beta         |       |       |
| 1     | (Constant) | 10,198         | 0,105      |              | 3,562 | ,571  |
|       | ebit       | 0,618          | 0,461      | 0,644        | 1,740 | 0,006 |
|       | Fundings   | 0,028          | 0,467      | 0,143        | 2,129 | 0,014 |
|       | Financing  | 0,772          | 1,102      | 0,091        | 4,782 | 0,000 |

Source: SPSS output results, 2019

### Partial Test Results

The t test is known as a partial test, which is to test how the effect of each independent variable individually on the dependent variable. This test can be done by comparing t arithmetic with t table or by looking at the column of significance on each t arithmetic. T test is carried out to test the significance of independent variables on the dependent variable individually, this is done by comparing t arithmetic with tables at the level of significant 5% with the following test criteria:

$H_0: \beta = 0$  means that there is no significant influence of independent variables on the dependent variable.

$H_0: \beta \neq 0$  means that there is a significant influence of the independent variable on the dependent variable.

1. If t arithmetic < 5% significant level then  $H_0$  is accepted and  $H_1$  is rejected
2. b. If t arithmetic > 5% significant level then  $H_1$  is accepted and  $H_0$  is rejected

Partial test results can be seen in Table 1; The results of t-test analysis in Table 1 show that the coefficient of profitability is 0.618 and the probability value is 0.006 with a significance level of 5% ( $\alpha = 0.05$ ). The hypothesis is accepted if the probability value < 0.05. T test analysis results show that the probability value of 0.006 < 0.05, it can be concluded that profitability has a significant effect on CSR (Corporate Social Responsibility). With a significant positive effect, it can be interpreted that for each increase or increase of 1% profitability, CSR

(Corporate Social Responsibility) increases by 0.618. This is because the effect of profitability on CSR (Corporate Social Responsibility) is positive, so the addition of profitability will increase CSR (Corporate Social Responsibility). T test results Profitability variables can also be concluded from the analysis of t count with t table with the following assessment criteria:

1. If  $t_{\text{arithmetic}} < t_{\text{table}}$  then  $H_0$  is accepted and  $H_1$  is rejected
2. If  $t_{\text{arithmetic}} > T_{\text{table}}$  then  $H_1$  is accepted and  $H_0$  is rejected

The results showed the t count on the profitability variable (X1) was 1,740, while the t table with the number of samples  $n = 77$ ,  $df = 3$  and the significance level of 5% was 1,664. It can be concluded that  $t_{\text{arithmetic}} > T_{\text{table}}$  then  $H_1$  is accepted.

T test analysis results in Table 1 shows that the coefficient value of Fundings is 0.028 and the probability value is 0.014 with a significance level of 5% ( $\alpha = 0.05$ ). The hypothesis is accepted if the probability value  $< 0.05$ . Regression analysis results show that the probability value of 0,000  $< 0.05$ , it can be concluded that Fundings significantly influence CSR (Corporate Social Responsibility). With this significant effect, it can be interpreted that for every increase or increase of 1% of Fundings, CSR (Corporate Social Responsibility) increases by 0.028. This is because the influence of Fundings on CSR (Corporate Social Responsibility) is positive, so the addition of Fundings will add to CSR (Corporate Social Responsibility). The results showed the t count on the variable Fundings (X2) was 2.129, while the t table with a sample size of  $n = 120$ ,  $df = 3$  and a significance level of 5% was 1.664. It can be concluded that  $t_{\text{arithmetic}} > T_{\text{table}}$  then  $H_2$  is accepted.

The results of the t-test analysis in Table 1 show that the coefficient value of the Financing is 0.774 and the probability value is 0,000 with a significance level of 5% ( $\alpha = 0.05$ ). The hypothesis is accepted if the probability value  $< 0.05$ . Regression analysis results show that the probability value of 0,000  $< 0.05$ , it can be concluded that the financing significantly influences CSR (Corporate Social Responsibility). With this significant influence, it can be interpreted that for every increase or increase of 1% of the Financing, CSR (Corporate Social Responsibility) increases by 0.774. This is because the effect of Financing on CSR (Corporate Social Responsibility) is positive, so the addition of Financing will add to CSR (Corporate Social Responsibility). The results showed t count on the variable financing (X3) was 4.782, while t table with a sample size of  $n = 120$ ,  $df = 3$  and a significance level of 5% was 1.657. It can be concluded that  $t_{\text{arithmetic}} > T_{\text{table}}$  then  $H_3$  is accepted.



**Simultaneous Test Results**

The t test is known as the simultaneous test, which is to test how the effect of all the independent variables together on the dependent variable. This test can be done by comparing f arithmetic to f table or by looking at the column of significance in f arithmetic. The testing criteria are as follows:

Ho:  $\beta_1 = \beta_2 = \dots \beta_k = 0$  means that there is no significant effect between all independent variables and the dependent variable.

H o :  $\beta_1 \neq \beta_2 \neq \dots \beta_k \neq 0$  means that there is a significant influence between all independent variables on the dependent variable.

1. If F arithmetic <the level of significant 5% then Ho is accepted and H1 is rejected
2. If F arithmetic > 5% significant level then H1 is accepted and Ho is rejected

The following are the results of the F test or simultaneous test:

Table 2  
Simultaneous / ANOVA Test Results

|   | Model      | Sum of Squares | df  | Mean Square | F      | Sig.  |
|---|------------|----------------|-----|-------------|--------|-------|
| 1 | Regression | 0,446          | 3   | 0,223       | 11,074 | 0,009 |
|   | Residual   | 11,833         | 117 | 0,208       |        |       |
|   | Total      | 12,278         | 120 |             |        |       |

Source: SPSS output results, 2019

The results of the f test analysis in the above table show that the calculated f value is 11.074 and the significance / probability value is 0.009 with a significance level of 5% ( $\alpha = 0.05$ ). The hypothesis is accepted if the probability value <0.05. The results of the f test analysis show that the probability value of 0,000 <0.05, it can be concluded that the independent variables together have a significant effect on CSR (Corporate Social Responsibility). The test results f can be concluded from the analysis of f arithmetic f table with the following evaluation criteria:

1. If F arithmetic <F table then Ho is accepted and H1 is rejected
2. If F arithmetic > F table then H1 is accepted and Ho is rejected

The results showed the f count was 11,074, while the f table with the number of samples was n = 120, df = 3 and the significance level of 5% was 3.15. It can be concluded that F arithmetic > F table then H4 is accepted.

### **Determination Coefficient Test Results**

The purpose of this test is to test the level of closeness or attachment between the dependent variable and the independent variable which can be seen from the magnitude of the coefficient of determination (adjusted R-square). The coefficient of determination is between zero and one. A small R<sup>2</sup> value means that the ability of the independent variables in explaining their attachment to the dependent variable is very limited while a value close to one means that the independent variables provide almost all the information needed to predict the variation of the dependent variable. The results of the coefficient of determination test are as follows:

Table 3  
Determination Coefficient Test Results

| Model | R     | R Square | Adjusted R Square |
|-------|-------|----------|-------------------|
| 1     | 0,591 | 0,636    | 0,602             |

Source: SPSS output results, 2019

From the table above it can be seen the value of the coefficient of determination as indicated by the adjusted R-square of 0.602. This shows that the ability of independent variables in explaining their attachment to the dependent variable is 60.2%, while the remaining 39.8% is explained by other variables not included in the model.

### **The Effect of Profitability (EBIT), Fundings, and Total Sharia Bank Financing on CSR (Corporate Social Responsibility)**

The first hypothesis states that "H1 = Profitability has a significant positive effect on CSR (Corporate Social Responsibility)". Statistical test results show that profitability proxied by EBIT variables has a significant positive effect on CSR (Corporate Social Responsibility), so H1 is accepted. These results are consistent with the theory that disclosure is used by company managers to investors and to help support sustainability and management compensation (Busch & Hoffmann, 2011). High profitability shows good company performance, and with high profits the company has enough funds to collect, classify, and process information to be more useful and can present a more comprehensive disclosure (Tafti, et al, 2012). Therefore the higher the profitability of the company, the higher the completeness of annual report disclosure (Siregar & Bachtiar, 2010). In this study profitability is proxied by earnings before interest and tax (EBIT). EBIT is an indicator of a company's profitability, calculated as revenue minus costs, excluding taxes and interest (Nollet, et al, 2015).

The second hypothesis states that "H2: Fundings have a significant positive effect on CSR (Corporate Social Responsibility)" The results of statistical tests

show that Fundings have a significant positive effect on CSR (Corporate Social Responsibility), so H2 is received. The results of this study are in accordance with the theory which states that Fundings (deposits) are funds entrusted by the public to banks based on fund storage agreements in the form of demand deposits, deposits, certificates of deposit, savings, and other forms (Albu & Krasodomska, 2016). The importance of funding sources from the wider community, due to sources of funds from the wider community is the most important source of funds for banks. The source of funds, also called Fundings sources, aside from being easy to find, is also widely available in the community (Chen & Wang, 2011). If Fundings increase, the financing will increase resulting in high profitability. High profitability encourages companies to increase CSR disclosure, so that indirectly an increase in Fundings can increase CSR disclosure (Torres, et al, 2012).

The second hypothesis states that "H3: Total Financing has a significant positive effect on CSR (Corporate Social Responsibility)." Statistical test results show that the amount of financing has a significant positive effect on CSR (Corporate Social Responsibility), so that H3 is accepted. The results of this study are in accordance with the theory which states that financing is the provision of money or bills that can be likened to it, based on an agreement or agreement between the bank and another party that requires the party to be paid to return the money or the bill after a certain period of time in return or for results (Shen, et al, 2016). Distribution of funds to customers, in outline financing products. If financing increases, banks will produce high profitability (Dumitrescu & Simionescu, 2015). High profitability encourages companies to increase CSR disclosure, so indirectly an increase in funding is able to increase CSR disclosure (Soana, 2011).

## **CONCLUSION**

Based on the results of the research and discussion in advance, it can be concluded that: (1) Profitability proxied by Earnings before interest and tax (EBIT) has a significant positive effect on CSR (Corporate Social Responsibility). This is indicated by the significance value of  $0.006 < \alpha = 0.05$  and the correlation coefficient of 0.618. T test results also indicate that  $t_{\text{arithmetic}} > t_{\text{table}}$  so it can be concluded that H1 is accepted. (2) Fundings have a significant positive effect on CSR (Corporate Social Responsibility). This is indicated by the significance value of  $0.014 < \alpha = 0.05$  and the correlation coefficient of 0.028. T test results also indicate that  $t_{\text{arithmetic}} > T_{\text{table}}$  so that it can be concluded that H2 is accepted. (3) Financing has a significant positive effect on CSR (Corporate Social Responsibility). This is indicated by the significance value of  $0,000 < \alpha = 0.05$  and the correlation coefficient of 0.772. T test results also indicate that  $t_{\text{arithmetic}} > T_{\text{table}}$  so that it can be concluded that H3 is accepted. (4) Profitability, Fundings, and Financing together have a significant effect on CSR (Corporate Social

Responsibility). This is indicated by the significance value of the f test of  $0.009 < \alpha = 0.05$ . Constraints that are still commonly found in the implementation of CSR are cost issues, competent human resources, distribution of activities and determination of targets, forms of activities, licensing and regulatory issues, lack of partnerships, socialization of activities, understanding of implementation and evaluation in the field, and many persons who carry out illegal levies on the ground.

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