

# **POLITICAL CONNECTION AND CORPORATE SOCIAL RESPONSIBILITY: EVIDENCE FROM INDONESIA**

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## **ABSTRACT**

This paper aims to investigate the influence of political connection on Corporate Social Responsibility (CSR) expense in Indonesia. We use a sample of 682 firm-year observations between 2010 and 2015. Using the individual-level of political connections, we find that the political connection is an important determinant of CSR expense. The political connection effect is analyzed based on the different characteristics of ownership structure, board structure, and affiliated party. We find that state-owned enterprises and privately-owned enterprises that politically connected are positively associated with CSR expenses. Interestingly, the evidence shows that politically connected board of commissioners are more willing to spend in CSR activities, while politically connected board of directors have no significant concern regarding CSR. Furthermore, politically connected firms that contribute to CSR are from government-leaning firms, while opposition-leaning firms show different matters. The findings are robust using different measures of political connection and controls.

**Keywords:** Political Connection, Corporate Social Responsibility, Corporate Governance, Indonesia.

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## **1. INTRODUCTION**

Study on the relationship between political connection and firm performance has been increased since the early 2000s. Political connections are found to determine payout (Benjamin, Zain, & Wahab, 2016; Su, Fung, Huang, & Shen, 2014; Trinugroho, 2017) and financing policies (Claessens, Feijen & Laeven, 2008; Leuz & Oberholzer-Gee, 2006; Li, Meng, Wang, & Zhou, 2008). However, study on the influence of political connection on corporate allocation choice is limitedly explored, especially on Corporate Social Responsibility (CSR) decision.

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We aim to examine the link between political connection and CSR using Indonesian data. There are several reasons that motivate this study which are: firstly, Indonesia's Corruption Perception Index (CPI) scores are below the median seven years in a row (<https://www.transparency.org/>), indicating a high level of corruption and low transparent systems (Faccio, 2006). Secondly, foreign investment tends to avoid countries such as Indonesia that are particularly practicing political connections in the business process (Boubakri, Cosser, & Saffar, 2008; Chen, Li, Su, & Sun, 2011; Faccio, 2006). Thirdly, Indonesia is the first country that mandate CSR activities through the Law of 2007 No. 40. Therefore, the motive of 'grabbing hand' with the government is more pronounced, reflecting not only awareness of social situations but also communicate their concern for regulation compliance. Our study is the first that examines the effects of political connection and CSR expense in a mandatory setting country.

This study contributes to political connection and CSR literature by examining a unique feature of political connection using ownership type, political affiliations and board structure to CSR three measurements i.e. environmental, social and economic expenses (e.g. Giuli & Kostovetsky, 2014; Lin, Tan, Zhao, & Karim, 2015). Our study also extends the discussion regarding the critical influence of political connections on firms' strategic decisions such as CSR (Chen & Hung-Baesecke, 2014; Faccio, 2006; Leuz & Oberholzer-Gee, 2006; Li & Zhang, 2010; Yu & Lee, 2016).

Results show that political connections affect corporate social responsibility expenses, particularly social expense. This finding is in line with Trihermanto & Nainggolan (2019) that found Indonesian listed firms dominantly allocate their resources on social donations and charitable giving. The evidence in this study also suggests that government ownership positively affect all aspect of CSR activities, while privately-owned enterprises with political connections are more concern about charitable donations and environmental protection activities. However, we find no significant evidence for the effect of the politically connected board of directors. Other notable findings are the fact that government-leaning firms are better at overall social responsibility activities and charitable donations, while opposition-leaning firms negatively affect environmental protection, infrastructure project, and community development activities. The findings hold using alternative measures of political connections.

The findings of this research can be beneficial for stakeholders. Understanding the importance of political connection to CSR expense may help investors to select companies that promote social responsibility, particularly firms that have politically connected board of commissioners. Also, it could be a consideration for foreign firms that plan to operate their business in Indonesia or to acquire Indonesian firms with regards to political connection. For Indonesian government, considering Indonesian listed firms outperform merely on charitable giving and social donations, may make a policy that requires firms to spend more on environmental protection and business partnership regulations in the future.

This paper is organized as follows. Section 2 describes the hypothesis development of this study. Section 3 explains the data and methodology. Section 4 presents the results of this study and reports the robustness tests. Lastly, section 5 concludes the paper.

## 2. LITERATURE REVIEW

Historically, corporate social responsibility is a voluntary choice from the corporation to express their willingness for managing environment sustainability and enhancing social welfare (Frederick, 1960). However, in Indonesia, CSR activities is mandatory for state-owned enterprises through the Law Number 236 of 2003, such firms must allocate 1-3% of their net profit for social programs (*Program Kemitraan dan Bina Lingkungan*). Further, based on the Law Number 40 of 2007, all companies that operate their business in the field of natural resources must implement CSR. It states that the implementation of CSR must be calculated and budgeted as corporate costs, with sanction imposed when the firms fail to comply. This is supported by Financial Service Authority Rule No. 51/POJK.03/2017 which requires all listed firms to disclose their annual sustainability reports. Albeit the standard of CSR implementation stated in the regulations is ambiguous, the CSR disclosure in Indonesia has been increasing over time (Nainggolan, Famiola, Siahaan, & Trihermanto, 2017).

Besides mandatory, there are other reasons behind CSR compliance, such as, reputation concerns, stakeholder preferences, and particular firm characteristics that directly influence CSR decisions (Arendt & Brettel, 2010; Benabou & Tirole, 2010; Giuli & Kostovetsky, 2014; Harrison & Freeman, 1999; Trihermanto & Nainggolan, 2019; Zivin & Small, 2005). Recent empirical literature shows a critical role of stakeholder preferences, proxied by political connections, on CSR choice (Giuli & Kostovetsky, 2014; Lin et al., 2015). It entrusts pro-social behavior, which determines social responsibility (Benabou & Tirole, 2010).

When politicians have control over a firm, they might use it to meet their political objectives by ruling firms' strategic decisions (Shleifer & Vishny, 1994). To achieve this, politicians could use CSR as a strategic tool for reputation building (Den Hond, Rehbein, de Bakker, & Lankveld, 2014). Further, CSR may reflect the social identity of the firm (Arendt & Brettel, 2010). According to organizational identity study, the corporate policy is drawn based on the shared understandings of the members, because they need symbolic resources for identity reconfirmation (Brown & Humphreys, 2006; Gioia & Chittipeddi, 1991; Whetten, 2006). Empirical studies show some evidence that politically connected firms have higher CSR than non-connected firms (Giuli & Kostovetsky, 2014; Kim, Koo, & Paz, 2017; Li & Zhang, 2010; Lin et al., 2015; Rahman & Ismail, 2016). Hence, we propose the first hypothesis for Indonesian case:

### *H1. Political connection has a positive relationship with CSR*

The spending of politically connected firms on CSR varies, those who desire higher benefits spend more resources. In Indonesia, state-owned enterprises have higher concerns on CSR because the regulation may be more enforced in a governmental organization and stronger actuation of social identity might play an important role as well. Empirical studies report that government ownership has a positive influence to CSR (Li & Zhang, 2010; Rahman & Ismail, 2016).

On the other hand, Lin et al. (2015) found no association between state-owned enterprises and CSR. Taking setting in more corrupt environments, Lin et al. (2015) show that CSR spending in privately-owned firms is higher because it needs more government protection, hence CSR is used as a tool to build a good connection with the government. However, Li & Zhang (2010) found a negative effect of political connection to CSR in the privately-owned enterprise. This study

suggests that non-SOE has a higher urgency on maximizing shareholders' wealth rather than supporting public services. Hence, we propose the second hypothesis as follow:

*H2a. State-owned enterprises tend to spend higher on CSR than non-state-owned enterprises*

Ofoegbu, Odoemelam, & Okafor (2018) utilize a cross-section data of 303 firm-year observations to examine the influence of board characteristics on environmental disclosure. They find that board independence, audit committee independence, and environmental committee have positive effects on environmental disclosure. However, this study does not account for individual characteristics of the board members, i.e., board gender, board age, and board political connection which may affect the environmental disclosure choices.

Specific attribute of the board members such as gender and relational capital play a critical role on CSR concerns (Malinn & Michelin, 2011). This study measures relational capital using the average value of directorships on the community influential and non-executive directorships. It suggests that high relational capital enhance reputation concern due to greater prestige and awareness of sensitive issues. Taking this evidence as an important base to examine the individual attribute of board members on CSR choices, we fill the gap by investigating political influences relied on the board members. We differ the analysis for politically connected board of commissioners and board of directors to understand where the prominent effects rely.

Indonesia conducts dual board system to promote the implementation of Good Corporate Governance (GCG), consisting board of directors (BoD) and board of commissioners (BoC) that both report to the shareholders independently. According to the Law of 2007 No. 40, the main role of the board of directors are to operate the business and ensure it meets the strategic guidance, while board of commissioners are responsible to oversee the ethical conducts and provide suggestions. Board members perform a central role in the corporate strategic policies as guiding firms' governance system to protect shareholders' values (Fama & Jensen, 1983). Recent studies show the presence of non-executive boards affect firms' environmental concerns, indicating ethical conquest of supervisory boards on public services (Post, Rahman, & McQuillen, 2014). We expect:

*H2b. Politically connected board of commissioner is positively associated with CSR expense*

Political environment could be used as a natural measure of CSR preferences (Giuli & Kostovetsky, 2014). Giuli & Kostovetsky (2014) examines CSR concerns of Democrats and Republican affiliated firms in the US and find significant effects of political affiliations to CSR. They found democratic-leaning firms are more willing to conduct socially responsible business as it in line with their political agenda on environmental protection, anti-discrimination laws, and social welfare.

As this study uncovers a strong relationship between political views and CSR, we contribute to the literature by analyzing the influences of political affiliations on CSR by taking unique setting in multi-party system of Indonesia. Government-leaning firm is the closest organization that can assist on several important issues (Lin et al., 2015). Friedman (1970) suggests that the government often asks the corporation to help them providing public services when additional funding is needed, namely through infrastructure donations or charitable giving.

On the other hand, opposition-leaning firms are less affected by government demands (Giuli & Kostovetsky, 2014). The desire to conduct CSR then merely relies on their willingness to engage in socially responsible activities namely for reputation building or purely altruism. Such firms are able to utilize their resources on profitmaking than appointed social projects. Thus we expect

*H2c. Government-leaning firms tend to spend higher on CSR than opposition-leaning firms*

### 3. METHODOLOGY

To provide a clearer understanding of the economic value of CSR activities, we employ CSR expenses database from Nainggolan et al. (2017) obtained from the companies' annual or sustainability reports. Some companies divided their CSR expense into three categories i.e. environment, social, and economic while the rest only provided the overall CSR cost, then transform it into the natural logarithm of CSR (*CSR*) to account for large variability of the dataset (Lin et al., 2015). Following most of reporting format on CSR expenses, we divide CSR expenses into three categories to emphasize the contributions of each element of CSR namely, 1) Environmental (*CSREnv*) for CSR spending disclosed on environmental protection and natural conservation activities; 2) Social (*CSRSoc*) for CSR spending disclosed on charitable giving, education scholarships, and other social donations; and 3) Economic (*CSREco*) for CSR spending disclosed on community developments, business partnerships, and infrastructure projects (Huang & Zhao, 2016). Differing three bottom lines of CSR enables us to shed light which area of CSR that must be improved. To deliver robust evidence, we use other alternative measures of CSR, i.e. CSR expense to total assets (*CSRTA*), CSR expense to net profits (*CSRNP*) and CSR expense relative to the industry expense (*RelCSR*), we calculate *RelCSR* data following the procedure used in Monzur & Habib (2017):

$$RelCSR_{it} = \frac{CSR_{it} - MinCSR_{jt}}{MaxCSR_{jt} - MinCSR_{jt}}$$

where  $CSR_{it}$  is the overall CSR expense of firm  $i$  year  $t$ ,  $MinCSR_{jt}$  is the minimum value of CSR spending in industry  $j$  year  $t$ , and  $MaxCSR_{jt}$  is the maximum value of CSR spending in industry  $j$  year  $t$  (Kim, Li, & Li, 2014; Monzur & Habib, 2017).

Our main explanatory variable is the political connection score (*PolconScore*). The firm is identified as politically connected if (a) it is a state-owned enterprise (Faccio, 2006; Hovey & Naughton, 2007); (b) one of its Board of Director/Board of Commissioner is a member/former of parliament, military, ministry, or regent (Faccio, 2006); or (c) it contributes in the presidential election campaign (Leuz & Oberholzer-Gee, 2006). Political connection score is measured using several ways (Boubakri et al., 2008): 1) proportion of politically connected boards to total board members; 2) a dummy for firm contribution to 2009 or 2014 elections; it is 1 for firms that contributed to elections (*PolconDummy*), otherwise zero; 3) a dummy for government ownership; 1 if it is a state-owned enterprise (*PSOE*), otherwise zero (*PNSOE*); and 4) a dummy of one if political connection can be measured using at least one of the three measures of political connection, otherwise zero (*PolconDummy*).

We also classify the source of political connection whether it is through the board of directors (*PBOD*) or board of commissioner (*PBOC*). This is to shed light on which type of board that is more concern to social responsibility. *PBOD* is calculated by the ratio of politically connected board of directors to total board of directors. Similarly, *PBOC* is calculated by the ratio of politically connected board of commissioners to total board of commissioner. Lastly, we separate government-leaning firms (*PolconGOVT*) and opposition-leaning firms (*PolconOPP*), based on the information disclosed on Bloomberg BusinessWeek (December 11, 2014), Kompas (May 28, 2014), and Tempo (October 26, 2014), to confirm the stakeholder preference hypothesis (Giuli & Kostovetsky, 2014).

The control variables used in the regression models are: Return-on-assets (*ROA*), is the one-year lag ratio of net income to total assets to measure prior accounting performance (Benlemlih and Bitar, 2018; Giuli & Kostovetsky, 2014; Trihermanto & Nainggolan, 2019). High-performance firms tend to spend more on CSR (Giuli & Kostovetsky, 2014). Hence, we expect a positive sign between *ROA* and *CSR*. Book-to-market (*BTM*) is calculated by the one-year lag book value of equity divided into the market value of equity, to measure firms' growth opportunities (Giuli & Kostovetsky, 2014). Firms with lower *BTM* have higher growth opportunities, resulting in lower *CSR* spending (Giuli & Kostovetsky, 2014). Hence, we expect a negative relationship between *BTM* and *CSR*. Firm Size (*Size*) is calculated by the one-year lag natural logarithm of total assets to measure firms' visibilities (Gnanaweera & Kunori, 2018; Huang & Zhao, 2016; Lin et al., 2015; Rahman & Ismail, 2016). Larger firms are more likely to spend higher on *CSR* (Lin et al., 2015; Rahman & Ismail, 2016; Trihermanto & Nainggolan, 2019; Zhuang & Chang, 2018). Therefore, we expect a positive relationship between firm size and *CSR*.

Leverage (*Leverage*) is calculated by the one-year lag book value of total liabilities to total assets, to measure the monitoring role from the creditors (Giuli & Kostovetsky, 2014; Jo & Harjoto, 2012; Lin et al., 2015). Firms with a high leverage ratio are more likely to spend less on *CSR* expenses (Giuli & Kostovetsky, 2014; Jo & Harjoto, 2012; Kim et al., 2017). Hence, we expect a negative relationship between leverage ratio and *CSR*. Cash holding (*CashTA*) is calculated by the one-year lag sum of cash and cash equivalent to total assets, to measure the available resources for *CSR* spending (Lin et al., 2015; Trihermanto & Nainggolan, 2019). Firms with higher cash holding have a better pool of resources to spend in *CSR* activities (Lin et al., 2015; Trihermanto & Nainggolan, 2019). Therefore, we expect a positive sign of cash holding and *CSR*. Retention ratio (*retention*) is calculated by one-year lag of retained earnings to net income (Li & Zhang, 2010) to measure the growth opportunity of the firms. Higher retention ratio shows that the company is not on the mature stage; such firms are more likely to spend higher *CSR* expense (Li & Zhang, 2010; Trihermanto & Nainggolan, 2019). Therefore, we expect a negative relationship between retention and *CSR*. We run the regression model as follows:

$$CSR_{it} = \alpha_0 + \beta_1 PolCon_{it} + \beta_2 ROA_{it-1} + \beta_3 BooktoMarket_{it-1} + \beta_4 Size_{it-1} + \beta_5 Leverage_{it-1} + \beta_6 CashHolding_{it-1} + \beta_7 Retention_{it-1} + \varepsilon_{it}$$

We include industry effects to account for each industry's unique features, and time effects to account for the change in economic conditions. Also, a robust standard error is employed to adjust heteroscedasticity and non-normality dispersions (White, 1980). We conduct F-test, Breusch-Pagan LM test and Hausman test before we decide the employed estimator of our models

(Wooldridge, 2012). The results show our data is best estimated using Generalized Least Square (GLS) or random effect panel data.

## 4. RESULTS AND DISCUSSION

### 4.1 Descriptive Statistics

Table 1 presents the summary statistics of CSR, political connections, and firm characteristics (See Appendix for variable definitions). It shows the total observation, mean, standard deviation, minimum and maximum value for each variable used in this study. Panel A shows statistics on corporate social responsibility expense, Panel B presents measures of political connection, and Panel C presents control variables used in this study.

**Table 1: Summary Statistics**

Variable	Obs	Mean	Median	Std. Deviation	Min	Max
<b>Panel A: Corporate Social Responsibility Expense</b>						
<i>CSR (bil.)</i>	715	173.357	12.000	591.647	0.0037	5.130.000
<i>CSREnv (bil.)</i>	62	95.445	11.745	273.140	0.0000	1.410.000
<i>CSRSoc (bil.)</i>	136	66.153	0.5445	267.170	0.0000	1.830.000
<i>CSREco (bil.)</i>	50	71.874	15.600	140.808	0.0000	733.800
<i>CSRNP</i>	711	0.0402	0.0061	0.4908	-93.774	50.921
<i>CSRTA</i>	711	0.0012	0.0004	0.0025	0.0000	0.0240
<i>RelCSR</i>	714	0.0391	0.0026	0.1291	0.0000	10.000
<b>Panel B: Political Connection</b>						
<i>PolconScore</i>	716	0.9103	10.476	0.9956	0.0000	30.857
<i>PolconDummy</i>	715	0.5063	10.000	0.5003	0.0000	10.000
<i>PSOE</i>	715	0.0867	0.0000	0.2816	0.0000	10.000
<i>PNSOE</i>	715	0.4224	0.0000	0.4943	0.0000	10.000
<i>PolconGOVT</i>	715	0.1203	0.0000	0.3255	0.0000	10.000
<i>PolconOPP</i>	715	0.0727	0.0000	0.2599	0.0000	10.000
<b>Panel C: Firm Characteristics</b>						
<i>ROA (-1)</i>	685	62.567	47.080	106.218	-633.464	831.019
<i>BTM (-1)</i>	682	0.6797	0.6627	32.690	-508.781	76.529
<i>Size (-1) (bil.)</i>	685	80.257	81.920	15.847	21.773	118.558
<i>Leverage (-1)</i>	685	0.5113	0.4907	0.3381	0.0039	43.015
<i>CashTA (-1)</i>	685	0.1163	0.0832	0.1112	0.0001	0.7687
<i>Retention (-1)</i>	711	-26.782	29.267	821.304	-14.080.570	2.191.275

The data distribution is skewed due to the distinct results of the mean and median presented in Table 1. In Panel A, we find that CSR spending of Indonesian listed firms is inadequate to meet the government demands, the median of *CSRNP* is only 0.6%, while the government requires 1-

3% of the net profits. Mean of CSR spending is at IDR 17.336 billion. The CSR activity is concentrated on infrastructure projects, community development, and business partnership activities (median of *CSREco* is higher than *CSRSoc* and *CSREnv*). Panel B shows the median of *PolconScore* is 10.48 (max of 30.9) and higher than the mean (0.910). It indicates the medium intensity of political connectedness in Indonesia as of about 50% are politically connected. Political connection through SOE is lower than through privately owned firms (mean of 0.09 vs. 0.42) but through government leaning is higher than through opposition leaning (mean of 0.12 vs. 0.07). Panel C shows the data used in this study consist of profitable firms (median of *ROA* is 47.08), overvalued (median of *BTM* is 0.663), large firm (median of *Size* is 81.92), low level of debt to total assets (median of *Leverage* is 0.491), financially unconstrained (median of *CashTA* is 8.3%) and high growth opportunity (median of *Retention* is 29.27).

**Figure 1: Politically Connected Firms across Industry from 2010 -2015**

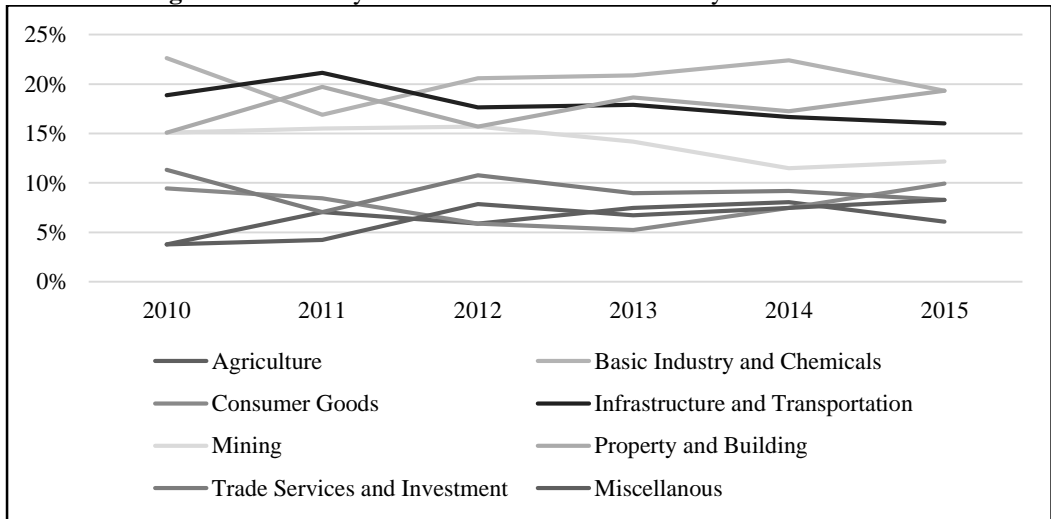


Figure 1, shows that basic industry and chemicals consistently dominate politically connected firms in Indonesia, occupying more than 15% of the data set. According to the Ministry of Industry (2012) Republic of Indonesia, basic industry and chemicals are the top contributors to Indonesian GDP and unemployment. Intuitively, this connection is maintained to occupy the politicians/officials’ urgency on stabilizing economic conditions in Indonesia. Furthermore, we see that politically connected firms in the mining industry decrease over time. PwC reports political risks in the mining industry has been increased as policymaking takes on a populist flavor, for instance, the establishment of Law of 2009 No. 4. There may be a political tendency in Indonesia to avoid dabbling in mining business operations as the awareness regarding environmental sustainability has raised.



## 4.2 Political Connection and CSR

To test the hypotheses, we employ multivariate regression analysis. The regression estimation results for the relationship between political connections and CSR expenses are presented in Table 2.

Columns 1, 2 & 4 in Table 2 show that using most measures, political connections have a positive relationship with CSR expenses. The estimated coefficient of *PolconScore* in model 1 is 0.3132 (t-stat of 3.41), meaning one-unit increase in political connection score increases 36.78% ( $\text{EXP}(0.3132)$ ) in the CSR expense. This is consistent with the findings of a positive relationship between *PolconScore* and *CSRTA* or *RelCSR*. This finding is consistent with the evidence in a voluntary setting, namely in China (Huang & Zhao, 2016) and in Malaysia (Rahman & Ismail, 2016). Furthermore, in Indonesia, we find that politically connected firms tend to engage in social donations and charitable giving rather than other CSR activities, such as environmental and economic activities (coefficient of *LnCSRSoc* is 0.8826 and significant at 1%, while the estimated coefficients of *LnCSREnv* and *LnCSREco* are not significant). This evidence is consistent with Trihermanto and Nainggolan (2019).

More profitable firms (*ROA*), overvalued (*BTM*), larger size (*Size*), low debt (*Leverage*), high cash holding (*CashTA*), and high growth opportunity (*Retention*) are also associated with CSR expenses. Profitable firms have more resources to generate free cash flow, resulting in higher allocated budget for CSR compared to less profitable firms (Campbell, 2007; Zhuang & Chang, 2018). Such firms also face higher pressures. Fields, Lys, & Vincent (2001) explain that 'overly' profitable firms might get more spotlight from the public, as a result, they need to show that they operate the business under acceptable norms and responsible ways. Our result is consistent with Giuli & Kostovetsky (2014), Huang & Zhao (2016), Lin et al. (2015), and Trihermanto & Nainggolan (2019).

Similarly, large firms are more 'visible' and socially constrained (Gamerschlag, Möller, & Verbeeten, 2011; Gnanaweera & Kunori, 2018). The information related to those firms are more accessible thus the pressure to manifest in socially responsible business is pronounced (Chih, Chih, & Chen, 2010). Besides that, large firms are better at occupying the CSR costs compared to small firms (Giuli & Kostovetsky, 2014). Our finding of positive association between *Size* and CSR is consistent with Huang & Zhao (2016), Li & Zhang (2010), Lin et al. (2015), Rahman & Ismail (2016), and Zhao (2012).

Highly leveraged firms are obtained less CSR demand from creditors, such firms are imposed to generate more profits from the stakeholders (Brammer & Pavelin, 2008). The negative association between *Leverage* and CSR is consistent with Lee & Choi (2018). Furthermore, unconstrained firms have a better pool of resources to spend in corporate goodness activities (Kubik, Scheinkman, & Hong, 2011). High cash holding indicates less constraint to invest in socially responsible projects (Lin et al., 2015). Our result is consistent with Lin et al. (2015) that found positive association between cash holding (*CashTA*) and CSR. However, it is not consistent with Giuli & Kostovetsky (2014) that found cash holding does not explain CSR in the voluntary setting.

**Table 2: Political Connection and CSR**

	<i>LnCSR</i>	<i>CSRTA</i>	<i>CSRNP</i>	<i>RelCSR</i>	<i>LnCSRE<sub>nv</sub></i>	<i>LnCSR<sub>Soc</sub></i>	<i>LnCSR<sub>Eco</sub></i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
<i>PolconScore</i>	<b>0.3132***</b> (3.41)	<b>0.0001***</b> (2.58)	-0.0296 (-0.91)	<b>0.0138**</b> (2.10)	0.7391 (0.85)	<b>0.8826***</b> (3.33)	1.761.878 (1.40)
<i>ROA (-1)</i>	<b>0.0124**</b> (2.32)	<b>0.00001*</b> (1.71)	-0.001 (-0.96)	0.0002 (1.18)	0.0118 (0.35)	<b>0.0348*</b> (1.82)	<b>-0.100***</b> (-3.31)
<i>BTM (-1)</i>	-0.0076 (-0.4)	<b>-0.00006**</b> (-2.34)	-0.0028 (-0.67)	-0.0015 (-1.37)	<b>0.8209*</b> ** (3.16)	-3.54E-01 (-1.17)	0.0412 (0.04)
<i>Size (-1)</i>	<b>0.7278***</b> (11.14)	-0.00008 (-1)	0.0039 (0.32)	<b>0.019***</b> (3.69)	-0.1977 (-0.43)	<b>0.344***</b> (2.63)	-23.494 (-1.54)
<i>Leverage (-1)</i>	0.25778 (0.88)	<b>-0.0006*</b> (-1.65)	-0.0754 (-1.25)	-0.0163 (-1.02)	31.309 (1.25)	-0.2292 (-0.4)	<b>-7.473***</b> (-3.48)
<i>CashTA (-1)</i>	<b>1.2783***</b> (2.66)	0.0021 (1.64)	0.0039 (0.04)	<b>0.0975*</b> (1.94)	33.901 (0.8)	12.463 (1.12)	87.278 (1.2)
<i>Retention (-1)</i>	-0.0004 (-1.27)	<b>-0.000**</b> (-1.96)	<b>-0.002***</b> (-2.99)	-2.00E-06 (-0.25)	0.0013 (0.78)	-0.0003 (-0.34)	-0.0067 (-1.28)
Constant	<b>-6.4212***</b> (-11.18)	<b>0.0011*</b> (1.81)	0.09637 (0.88)	<b>-0.142***</b> (-3.38)	-34.072 (-0.88)	<b>-4.3171***</b> (-3.30)	252.503 (1.58)
Obs	682	682	682	682	55	129	38
Industry Control	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Time Control	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R-squared	0.6248	0.1738	0.1273	0.2447	0.6055	0.6541	0.2758

Notes: \*\*\*significant at 1%, \*\*significant at 5%, and \*significant at 10%.

Next, this study investigates the consistency of political connection influence on CSR decision under several measurements. First, we divide the ownership structure into two categories: state-owned enterprises (*PSOE*) and non-state-owned enterprises that are politically connected (*PNSOE*) (Lin et al., 2015).

Table 3 shows that the estimated coefficients of state-owned enterprises are positive and significant in models 1 – 6, consistent with Rahman & Ismail (2016). The government highlights CSR spending on state-owned enterprises through the Law of 2003 No. 236 with sanction imposed when such firms do not spend 1-3% of their net profits to CSR.

Interestingly, politically connected of non-state-owned firms also are positively associated with high CSR expense, consistent with the evidence in China (Huang & Zhao, 2016), indicating sound effects of political connection regardless of the ownership structure. Private firms are unable to acquire regulation privileges, resulting in more prominent needs for tying a good relationship with stakeholders. Since CSR engagement quickly obtains approval of 'doing good' from the public (Ma & Parish, 2006), privately-owned firms can use this to obtain opportunities & tax preferences from the government and trust from the society. However, the estimation result for *RelCSR* (model 3) is not significant although the sign is also positive. The distinct results between *PSOE* and *PNSOE* are the magnitude of the coefficients. Generally, the estimated coefficients in *PSOE* are more prominent compared to *PNSOE*, meaning that SOEs are more willing to spend in CSR (Rahman & Ismail, 2016).

For the estimation results of three bottom line approach, we find positive association between state-owned enterprises (*PSOE*) and privately-owned enterprises (*PNSOE*) with environmental expenses (*LnCSREnv*). Similarly, we find evidence for the influence of political connection on social expenses (*LnCSR Soc*), and economic expenses (*LnCSREco*), both in state-owned and privately-owned enterprises.

The results of our control variables in Table 3 are consistent with Table 2. More profitable, overvalued, financially unconstrained, and high growth opportunity firms are positively associated with CSR expenses. These findings are consistent with Giuli & Kostovetsky (2014), Huang & Zhao (2016), Lin et al. (2015), and Rahman & Ismail (2016). However, we find an inconsistent result for *Size*. Firm size (*Size*) is positive and significant in model 1 (*LnCSR*), 3 (*relCSR*), and 5 (*LnCSREco*) (Giuli & Kostovetsky, 2014).

**Table 3: Ownership Structure and CSR**

	<i>LnCSR</i> (1)	<i>CSRTA</i> (2)	<i>RelCSR</i> (3)	<i>LnCSREnv</i> (4)	<i>LnCSR Soc</i> (5)	<i>LnCSREco</i> (6)
<i>PSOE</i>	<b>2.3454***</b> (6.85)	<b>0.0036***</b> (3.26)	<b>0.1705**</b> (2.54)	<b>3.541*</b> (1.78)	<b>3.5272*</b> (1.76)	<b>2.7445***</b> (3.49)
<i>PNSOE</i>	<b>0.3699**</b> (2.34)	<b>0.0003*</b> (1.65)	0.0019 (0.14)	<b>2.499*</b> (1.94)	<b>2.5072*</b> (1.96)	<b>1.6867***</b> (3.31)
<i>ROA (-1)</i>	<b>0.0134**</b> (2.55)	<b>0.00001**</b> (2.04)	<b>0.0003*</b> (1.66)	0.0259 (0.77)	0.0253 (0.76)	<b>0.0339*</b> (1.66)
<i>BTM (-1)</i>	-0.0064 (-0.34)	<b>-0.00006**</b> (-2.32)	-0.0016 (-1.48)	<b>-0.797***</b> (-3.45)	<b>-0.796***</b> (-3.47)	-0.3321 (-1.09)
<i>Size (-1)</i>	<b>0.7113***</b> (11.4)	<b>-0.0001*</b> (-1.88)	<b>0.0183***</b> (3.36)	-0.4774 (-1.21)	-0.4692 (-1.18)	<b>0.3522***</b> (2.95)
<i>Leverage (-1)</i>	0.2839 (1.01)	-0.0005 (-1.55)	-0.0144 (-0.94)	30.390 (0.35)	31.165 (1.49)	-0.1986 (-0.37)
<i>CashTA (-1)</i>	<b>1.0649**</b> (2.35)	0.0015 (1.4)	<b>0.0759*</b> (1.76)	<b>1.352</b> (0.35)	<b>1.4887***</b> (3.80)	13.069 (1.17)
<i>Retention (-1)</i>	-0.0005 (-1.59)	<b>-0.0002**</b> (-2.2)	-9.00E-06 (-1.06)	0.0012 (0.77)	0.0011 (0.75)	-0.0007 (-0.85)
Constant	<b>-6.2686***</b> (-11.37)	<b>0.0016***</b> (2.63)	<b>-0.130***</b> (-2.97)	<b>17.767***</b> (5.84)	-30.543 (-1.00)	<b>-4.5741***</b> (-3.62)
Obs	682	682	682	55	55	129
Industry Control	Yes	Yes	Yes	Yes	Yes	Yes
Time Control	Yes	Yes	Yes	Yes	Yes	Yes
R-Squared	0.6522	0.2683	0.3194	0.6666	0.6633	0.6783

Notes: \*\*\*significant at 1%, \*\*significant at 5%, and \*significant at 10%.

Secondly, taking benefits of dual board structure system in Indonesia, we investigate the link between political connection and CSR using two distinct criteria, namely, politically connected board of directors (*PBOD*) and politically connected board of commissioners (*PBOC*) to understand the key driver of CSR decision.

On the other hand, the primary role of board of commissioners (BoC) are to monitor the managers, to provide suggestions, and to emphasize corporate governance mechanism (Schilling, 2002). Our study provides evidence that politically connected BoC is positively associated with CSR expense.

Models 1 – 5 in Table 4 present *PBOC* consistently have positive and significant relationships with CSR expenses. The result indicates one-unit change in political connection score of board of commissioners (*PBOC*) increases 1.8 times higher (EXP(1.0291)) than in overall CSR expense (*LnCSR*) of non-*PBOC*. Similarly, one-unit change in political connection score of board of commissioners (*PBOC*) increases 9 times higher in social expenses (*LnCSRSoc*) and increases 77 times higher in economic expenses (*LnCSREco*).

Huang (2010) shows the number of BoC is negatively associated to firm performance in Taiwan, our results extend this study by providing evidence that BoC seems to be more concern into ethical issues. The results also are consistent with Ofoegbu et al. (2018) regarding board characteristics that determine CSR. As best to author's knowledge, this is the first study that proves politically connected board of commissioners determine CSR expenses.

Generally, the results for firm characteristics are similar to the previous discussion. More profitable, overvalued, less levered, financially unconstrained, and high growth opportunity firms are positively associated with CSR expenses.

**Table 4: Board Structure and CSR**

	<i>LnCSR</i>	<i>CSRTA</i>	<i>RelCSR</i>	<i>LnCSRSoc</i>	<i>LnCSREco</i>
	(1)	(2)	(3)	(4)	(5)
<i>PBOD</i>	19.223 (0.93)	-0.0043 (-0.74)	-0.0566 (-0.82)	-12.863 (-0.22)	0.673 (0.12)
<i>PBOC</i>	<b>1.0291***</b> (3.57)	<b>0.0016*</b> (1.7)	<b>0.0522*</b> (1.66)	<b>2.3033***</b> (3.1)	<b>4.3512***</b> (4.19)
<i>ROA (-1)</i>	<b>0.0127**</b> (2.43)	<b>0.00001*</b> (1.77)	0.0002 (1.26)	0.0305 (1.5)	<b>-0.0932***</b> (-2.95)
<i>BTM (-1)</i>	-0.0095 (-0.47)	<b>-0.00007**</b> (-2.39)	-0.0016 (-1.38)	-0.3474 (-1)	-0.4952 (-0.76)
<i>Size (-1)</i>	<b>0.7568***</b> (12.32)	-0.00005 (0.57)	<b>0.0207***</b> (3.49)	<b>0.5556***</b> (5.23)	-17.308 (-1.63)
<i>Leverage (-1)</i>	0.2746 (0.9)	<b>-0.0006*</b> (-1.75)	-0.0172 (-0.96)	-0.0060 (-0.01)	<b>-6.2379**</b> (-2.4)
<i>CashTA (-1)</i>	<b>1.3218***</b> (2.76)	0.0021 (1.63)	<b>0.0999*</b> (1.95)	0.9583 (0.87)	48.365 (0.97)
<i>Retention (-1)</i>	-0.0005 (-1.43)	<b>-0.000002**</b> (-2.04)	-4.00E-06 (-0.42)	-0.0004 (-0.59)	-0.0056 (-1.22)
Constant	<b>-6.6093***</b> (-12.19)	0.001 (1.44)	<b>-0.1526***</b> (-3.81)	<b>-5.922***</b> (-5.21)	<b>20.5719*</b> (1.71)
Obs	682	682	682	129	38
Industry Control	Yes	Yes	Yes	Yes	Yes
Time Control	Yes	Yes	Yes	Yes	Yes
R-Squared	0.6237	0.2055	0.2505	0.6401	0.856

Notes: \*\*\*significant at 1%, \*\*significant at 5%, and \*significant at 10%.

Next, we shed light the motive of 'grabbing hand' with the government by separating the connection between government-leaning connection (*PolconGovt*) and opposition-leaning connection (*PolconOpp*). This study adopts the concept used in Giuli and Kostovetsky (2014) that compares CSR decision between Democrats-leaning firms and Republican-leaning firms, then add

regime control to understand the political environment effects in Indonesia. Regime dummy (*Regime*) is added to control for regime changes, 1 for SBY regime and 0 for Jokowi regime.

Table 5 shows that political affiliations matter in Indonesia. In model 1 of Table 5, government-leaning firms (*PolconGovt*) has a positive association to CSR expense (*LnCSR*). The spending is concentrated on social expenses (*LnCSRSoc*), rather than environmental (*LnCSREnv*) or economic expenses (*LnCSREco*). This study finds for one-unit change in political connection score of government-leaning firms (*PolconGovt*) increases 44.82% (EXP(0.3703)) in CSR expense (*LnCSR*) and increases 59.86% (EXP(0.4691)) in social expenses (*LnCSRSoc*). This finding is in line with Giuli & Kostovetsky (2014).

Interestingly, opposition-leaning firm (*PolconOpp*) is negatively associated with environmental (*LnCSREnv*) and economic expenses (*LnCSREco*). For one-unit change in political connection score of opposition-leaning firms (*PolconOpp*) decreases 483% (EXP(1.7634)) on environmental expenses (*LnCSREnv*) and decreases more than 17 times than non-*PolconOPP* on economic expenses (*LnCSREco*). This finding is also the first evidence reporting negative association between opposition-leaning firms and CSR. The willingness of opposition-leaning firms to engage in CSR is not as high as government-leaning firms due to lower pressure from the officials.

Particularly in the Indonesian context, from 2010 to 2015, which was the second regime of SBY and the first regime of Joko Widodo, the infrastructure projects were aggressively implemented.

**Table 5: Political Affiliations and CSR**

	<i>LnCSR</i> (1)	<i>LnCSR</i> (2)	<i>LnCSREnv</i> (3)	<i>LnCSREnv</i> (4)	<i>LnCSRSoc</i> (5)	<i>LnCSRSoc</i> (6)	<i>LnCSREco</i> (7)	<i>LnCSREco</i> (8)
<i>PolconGOVT</i>	<b>0.3703***</b> (2.83)		-0.00587 (-0.01)		<b>0.4691**</b> (2.33)		0.0161 (0.04)	
<i>PolconOPP</i>		0.0135 (0.14)		<b>-1.7634**</b> (-2.44)		-0.2538 (-0.65)		<b>-2.9175**</b> (-2.09)
<i>ROA (-1)</i>	<b>0.0121**</b> (2.50)	<b>0.0124***</b> (2.58)	0.0172 (0.40)	0.0004 (0.01)	0.028 (1.34)	0.0291 (1.28)	<b>-0.0826**</b> (-2.17)	<b>-0.0671*</b> (-1.82)
<i>BTM (-1)</i>	-0.0076 (-0.41)	-0.0077 (-0.40)	<b>-0.6991***</b> (-2.73)	-0.4145 (-1.31)	-0.2922 (-0.96)	-0.2937 (-0.94)	-0.2842 (-0.24)	-0.7162 (-0.68)
<i>Size (-1)</i>	<b>0.7703***</b> (12.71)	<b>0.8066***</b> (12.39)	0.1395 (0.49)	0.4497 (1.10)	<b>0.5812***</b> (5.05)	<b>0.6972***</b> (4.73)	-14.563 (-0.81)	-0.6911 (-0.45)
<i>Leverage (-1)</i>	0.3242 (1.11)	0.3463 (1.15)	30.277 (1.22)	193.627 (1.04)	0.0952 (0.19)	0.39809 (0.85)	<b>-6.4817***</b> (-2.79)	-17.254 (-0.57)
<i>CashTA (-1)</i>	<b>1.0935**</b> (2.27)	<b>1.3093***</b> (2.65)	38.598 (0.93)	-0.0522 (-0.01)	0.4945 (0.43)	0.5921 (0.53)	97.024 (1.12)	0.8618 (0.11)
<i>Retention (-1)</i>	-0.0004 (-1.35)	-0.0004 (-1.47)	0.0011 (0.66)	0.0008 (0.46)	0.0003 (0.47)	0.0002 (0.30)	-0.0103 (-1.46)	<b>-0.0149*</b> (-1.67)
<i>Regime</i>	-0.0729 (-0.69)	-0.0997 (-0.92)	-0.4666 (-0.47)	-0.3294 (-0.36)	-0.2649 (-0.72)	-0.2231 (-0.60)	-11.559 (-1.30)	-0.1832 (-0.21)

Constant	<b>-6.7058***</b> (-12.24)	<b>-6.9753***</b> (-12.37)	-47.528 (-1.46)	<b>-6.07636*</b> (-1.91)	<b>-6.0061***</b> (-5.30)	<b>-7.0637***</b> (-5.85)	199.567 (1.03)	10.402 (0.58)
Obs	682	682	55	55	129	129	38	38
Industry Control	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Time Control	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R-Squared	0.6330	0.6057	0.3985	0.3411	0.0335	0.0268	0.2557	0.1906

*Notes:* \*\*\*significant at 1%, \*\*significant at 5%, and \*significant at 10%.

At the beginning of SBY reign, his main concern was to stabilize the economic conditions while in the second period of his regime, then SBY started stimulating the economic growth. Building infrastructure facilities was an agenda to spur economic activities. Joko Widodo is also known as Indonesian president that has a high concern to infrastructure projects. With regard to this fact, we suggest that government officials push affiliated firms to assist them in social projects although the government spending is mainly for infrastructure programs (Friedman, 1970; Lin et al., 2015). Therefore, opposition-leaning firms spend less CSR because such firms are less pressured by government officials. We suggest opposition-leaning firms in Indonesia might have more interests in profit-motivated projects than social-motivated projects.

On control variables, in general we find similar results like in previous tables.

### 4.3 Further Robustness Check

For robustness check, this study changes the measurement of political connection and the controls. We use a dummy variable of political connection as an alternative explanation of political connection (*PolconDummy*) (Faccio, 2006; Lin et al., 2015), 1 if politically connected, otherwise 0. Other variables used as control variables are the same with the main models. The regression models used to account for industry effect and time effect. The results show that in general, our findings hold using alternative measures of political connection, namely political connection dummy (*PolconDummy*). After that, we test the main models without industry and time controls, following Giuli & Kostovetsky (2014). The results do not change our main findings (Results are available upon request).

## 5. CONCLUSION

This study uses a quantitative approach to explain the link between political connection and corporate social responsibility of non-financial listed firms in Indonesian Stock Exchange from 2010 – 2015. This study finds that political connection has a positive influence on CSR expenses, prominently on charitable giving and other social donations. Politically connected firms tend to comply with the regulations and the public expectations for establishing socially responsible firms. The results hold under different ownership structure, both state-owned enterprises and privately-owned enterprises are willing to spend high CSR expense. A notable finding of this study is the evidence of politically connected board of commissioners have a positive impact on CSR spending, while politically connected board of directors do not imply the same concerns. Our findings do not

change much using different measures of political connection and different set of controls. However, this study has some limitations. First, extending the sample period may further check the robustness of the findings. Second, albeit this study considers the different values of political connection, it does not account for the interaction effects of different ownership structure and board structure. Therefore, we suggest further research to establish more comprehensive proxies of political connections and account for different types of connected officials.

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### Appendix A: Variable Definitions

<i>Panel A: Dependent Variables</i>			
Variable	Calculation		Reference
<i>CSR</i>	Natural logarithm of CSR overall expense		Huang & Zhao (2016)
<i>CSREnv</i>	Natural logarithm of environmental expense (environmental protections and natural conservations activities)		Huang & Zhao (2016)
<i>CSRSoc</i>	Natural logarithm of social expense (charitable givings, education scholarships, and other social donations)		Huang & Zhao (2016), Lin et al. (2015)
<i>CSREco</i>	Natural logarithm of economic expense (community developments, business partnerships, and infrastructure projects)		Huang & Zhao (2016)
<i>CSRTA</i>	CSR overall expense divided by total assets		Trihermanto & Nainggolan (2019)
<i>CSRNP</i>	CSR overall expense divided by net profits		Lin et al. (2015)
<i>RelCSR</i>	$\frac{CSR_{jt} - \text{Min}CSR_{jt}}{\text{Max}CSR_{jt} - \text{Min}CSR_{jt}}$ The overall CSR expense subtracted to minimum CSR spending in the industry, divided to the maximum CSR spending subtracted to minimum CSR spending in the industry		Kim et al. (2014); Monzur & Habib (2017); Nainggolan et al. (2017)
<i>Panel B: Independent Variables</i>			
Variable	Calculation	Expected Sign	Reference
<i>PolconScore</i>	Final weighted political connection score by indicators	+	Boubakri et al. (2008); Claessens et al. (2008); Faccio (2006)
<i>PolconDummy</i>	Political connection dummy is equal to 1 if politically connected, otherwise 0	+	Claessens et al. (2008); Faccio (2006)
<i>PSOE</i>	State-owned enterprise dummy is equal to 1 if politically connected, otherwise 0	+	Faccio (2006)
<i>PNSOE</i>	Politically connected firms that privately-owned is equal to 1 if politically-connected, otherwise 0	+	Huang & Zhao (2016)
<i>PBOD</i>	Ratio of politically connected board of directors to total board of directors	+	Nietsch (2005)

<b>PBOC</b>	Ratio of politically connected board of commissioners to total board of commissioner	+	Schilling (2002)
<b>PolconGOVT</b>	Government leaning politically-connected firms dummy is equal to 1 if politically-connected, otherwise 0	+	Giuli & Kostovetsky (2014)
<b>PolconOPP</b>	Opposition-leaning politically-connected firms is equal to 1 if politically-connected, otherwise 0	-	Giuli & Kostovetsky (2014)
<b>ROA</b>	Return on assets; net profit to total assets	+	Giuli & Kostovetsky (2014); Huang & Zhao (2016); Lee & Choi (2018); Li & Zhang (2010); Lin et al. (2015)
<b>BTM</b>	Book-to-market (book value of equity to market value of equity)	-	Giuli & Kostovetsky (2014); Lin et al. (2015); Monzur & Habib (2017)
<b>Size</b>	The natural logarithm of total assets	+	Huang & Zhao (2016); Lee & Choi (2018); Li, Lin, & Yang (2016); Li & Zhang, (2010); Lin et al. (2015)
<b>Leverage</b>	Total liabilities to total assets	-	Giuli & Kostovetsky (2014); Kim et al. (2017); Lee & Choi (2018); Li & Zhang (2010); Lin et al. (2015)
<b>CashTA</b>	Sum of cash and cash equivalent to total assets	+	Giuli & Kostovetsky (2014); Lin et al. (2015)
<b>Retention</b>	Retained earning to total income	-	Lee & Choi (2018); Monzur & Habib (2017)
<b>Regime</b>	Dummy variable is equal to 1 if the sample period is on the SBY regime, and 0 if it is on the Joko Widodo regime.	-	Giuli & Kostovetsky (2014)

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