The Role of Environmental Performance on Sustainability Reports in Indonesia Companies

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Abstract

The sustainability report reflects the company's contribution to sustainable development. Indonesia seeks to contribute to sustainable development, one of which is by conducting an assessment of companies using PROPER regarding environmental management. The study aims to determine whether environmental performance by PROPER measurement can play a significant role in disclosing sustainability reports to companies in Indonesia. Companies listed on the Indonesia Stock Exchange that publish annual and sustainability reports within five consecutive years are the population of this study. This study uses 85 units of analysis obtained by purposive sampling; data analysis using WarpPLS. The study results show an increase in the disclosure of sustainability reports when the audit committee and the board of directors meet effectively. However, companies without governance committees focus more on improving governance than disclosing sustainability reports. Environmental performance (PROPER), when associated with the type of industry and governance committee, will increase the disclosure of sustainability reports. However, a company with good environmental performance (PROPER) will make the audit committee and directors focus on other responsibilities because the community already understands that a company with good PROPER means managing the environment well and considers the company aware of the importance of sustainable development. This study concludes that environmental performance measured by PROPER plays a role in disclosing sustainability reports related to the type of industry, governance committee, audit committee, and board of directors of companies in Indonesia. The Indonesian government must support, facilitate and encourage companies to achieve the gold category in PROPER and encourage more massive disclosure of sustainability reports to contribute to sustainable development.

Keywords: Industry Type; Governance Committee; Independent Commissioner; Audit Committee; Board of Directors; Environmental Performance; Sustainability Reports; PROPER

JEL: M41, Q56

INTRODUCTION

Sustainable Development Goals (SDGs) are a significant global issue that applies to all countries with the involvement of many parties. Companies, as one of the private sectors, must be able to take part in realizing the SDGs. In general, companies are established to obtain large profits to develop better activities and improve the welfare of stakeholders (Madona & Khafid, 2020). However, the company must also be able to meet other aspects as listed in the Tripple P button, namely Profit, People, and Planet. Transparency of profit, people, and planet information can be found in the sustainability report. The Indonesian government supports the importance of this sustainable report with the issuance of POJK Number 51 (2017), which explains that all companies IDX (listed on the Indonesia Stock Exchange) must disclose sustainability reports starting in 2019. The company's sustainability report contains disclosures regarding environmental, social, and economic impacts as a form of contribution to the sustainable development goals (Global Reporting Initiative, 2016). According to Falikhatun et al. (2020), a sustainability report is a publication that displays governance models, organizational values, and links about business strategies and commitments to a sustainable economy globally.

Liputan6.com (2019) states that out of 629 companies as of 23 April 2019, only 110 sustainability reports have been published; this is based on the Global Reporting Initiative (GRI) and IDX. According to Arumsari & Asrori (2019), only 12.90% of the average sustainability report disclosure in companies listed on the IDX in 2014-2015. In the 2016-2018 range, it was only 46% Azzaki (2019). Meanwhile, Indrianingsih & Agustina (2020) show that the average non-financial company discloses a sustainability report of 35.59%. Previous data and research show that companies on the IDX still need to be more optimal in disclosing sustainability reports. Therefore, research still needs to be done to determine what influences the disclosure of sustainability reports in Indonesia and how to increase disclosure.

LITERATURE REVIEW

Székely & Vom Brocke (2017); Adams (2020); and La Torre et al. (2020), stated that sustainability reports are an essential means of making environmental, social, and transparent disclosures as well as expanding information related to company policies, actions, and strategies for the environment in which companies operate. Therefore, Junior et al. (2014) and La Torre et al. (2020) stated that a sustainability report is not just an ordinary report because of the comprehensive and detailed coverage of the report's contents regarding environmental, social, and economic performance. Sustainability reports become an instrument for maintaining and enhancing corporate image, accountability for using natural resources related to company activities, and stimulating

competitive competition between companies (Adams & Whelan, 2009; Correa-Garcia et al., 2020; and Tumwebaze et al., 2022).

Previous research on sustainability reports has presented various aspects that can affect it. Bhatia & Tuli (2017) and Sinaga & Fachrurrozie (2017) show that industry types positively impact sustainability reports. Dissanayake et al. (2019) and Hidayah et al. (2019) concluded that industry type does not influence sustainability reports. Then, Aniktia & Khafid (2015) and Safitri & Saifudin (2019) stated that the governance committee positively affected the sustainability report. However, Azzaki (2019) and Hidayah et al. (2019) show that the results of the governance committee have no impact on the sustainability report. Madona & Khafid (2020) and Nuraeni & Darsono (2020) explained that independent commissioners positively impact sustainability reports. Meanwhile, Dewi & Pitriasari (2019) and Indrianingsih & Agustina (2020) explained that independent commissioners have no impact on sustainability reports.

Aniktia & Khafid (2015) and Ruhana & Hidayah (2020) stated that audit committees could influence sustainability reports. Meanwhile, Arumsari & Asrori (2019) and Dewi & Pitriasari (2019) showed that the audit committee did not affect the sustainability report. Latifah et al. (2019) and Sinaga & Fachrurrozie (2017) explained that the board of directors positively impacts sustainability reports. However, it was Bhatia & Tuli (2017) and Lucia & Panggabean (2018) showed that the board of directors did not affect the sustainability report. The inconsistency of the results of previous research on the influence of variables of the industry type, governance committee, independent commissioners, audit committees, and board of directors on sustainability reports is interesting to re-examine. In addition, inconsistent results are suspected to be due to other factors that influence in strengthening or weakening of these results. The conditions for disclosing sustainability reports in Indonesia are not yet optimal and various existing research provide opportunities for more profound research related to this matter in Indonesia.

Deegan (2004) revealed a stakeholder theory that explains that *stakeholders* can obtain information about company activities that can influence their decision-making. Donaldson & Preston (1995) argue that stakeholder theory makes an organization extend responsibility to all *stakeholders*, not to investors or organizational owners alone. According to Rahayu & Cahyaningsih (2020), legitimacy theory explains that the company seeks to obtain guarantees that operations are ongoing and follow the norms prevailing in society so that the company realizes the disclosure of sustainability reports.

Industrial type is a characteristic of the company that relates to risk, type of business, environment, and company employees. Industrial types are classified into *low-profile* and *high-profile*. An entity with a high profile will receive more attention from the public because it interacts with various parties in its business operations. (Sinaga & Fachrurrozie, 2017). So that companies

with high profiles consider expanding disclosures, such as sustainability reports, to reduce pressure from environmental and social activists. In line with legitimacy theory, high-profile entities will disclose sustainability reports to gain public trust and legitimacy regarding operations that are carried out sustainably and are still within the norms prevailing in the surrounding environment. Bhatia & Tuli (2017) and Sinaga & Fachrurrozie (2017) show that industry types positively impact *sustainability reports*.

The governance committee is tasked with supporting the board of commissioners to thoroughly review GCG (good corporate governance) policies and improve the consistency of their implementation, including those related to social responsibility and business ethics (KNKG, 2006). In line with *stakeholder* theory, the existence of a *governance committee* in the company will make the implementation and consistency of GCG implementation run well, and the governance *committee* can recommend a broader range of environmental and social responsibility that can be reported through *sustainability reports* as a form of transparency principles from GCG. Aniktia & Khafid (2015) and Safitri & Saifudin (2019) show that *governance committees* positively influence *sustainability reports*.

The audit committee is responsible and tasked with reviewing the information to be published by the entity; reviewing legal and regulatory compliance. Audit committee meetings establish good communication and coordination so that GCG runs well and can motivate entities to disclose sustainability reports as a form of corporate responsibility to stakeholders. This action is in line with stakeholder theory; the more frequent the frequency of audit committee meetings, the more motivated companies are to disclose sustainability reports because disclosure of sustainability reports is also a form of compliance with existing regulations. In addition, sustainability reports are also a form of providing comprehensive information about company activities to stakeholders. Aniktia & Khafid (2015) and Ruhana & Hidayah (2020) stated that audit committees can influence *sustainability reports*.

The board of directors is the party appointed to lead and manage the company. KNKG (2006) mentions five functions of the board of directors: risk management, management, communication, internal control, and social responsibility. KNKG (2006) also explains that directors must pay attention to implementing corporate social responsibility. Therefore, better communication and coordination of the directors established in the board of directors' meetings will encourage companies to carry out social responsibility with their reporting. In line with stakeholder theory, board of directors meetings will impact disclosing sustainability reports to fulfill duties and maintain good relations with stakeholders. Latifah et al. (2019) and Sinaga & Fachrurrozie (2017) revealed that the board of directors positively impacted the *sustainability report*.

High profile or *low profile* is a measurement of industry-type variables. Solikhah & Winarsih (2016) explained that companies with a high level of sensitivity would pay attention to the disclosure of environmental performance more broadly and well to gain legitimacy and reduce pressure from environmental and social activists. *Legitimacy theory* explains that there is a tendency for entities that have excellent environmental performance to carry out *higher sustainability report* disclosures. A *high-profile* company will get more attention from the public. If the company has good capabilities in terms of the environment, the company's probability of implementing *a sustainability report* disclosure is higher to gain legitimacy from the public.

A *governance committee* in the company makes the actualization of corporate governance take place properly and can encourage entities to carry out social responsibility and reporting. Environmental performance is an entity's ability that is relatable to the surrounding environment. In line with legitimacy theory, companies with good environmental performance will receive public scrutiny; to gain public legitimacy, companies disclose sustainability reports. Companies with a governance committee will have stronger sustainability report disclosures if they have good environmental performance. Because in addition to carrying out their responsibilities to stakeholders, companies must also gain legitimacy from the public for their company activities, namely by disclosing a sustainability report.

The audit committee, which is assessed by the frequency of meetings, establishes good communication and coordination so that the study of information to be published by the company and the review of compliance with laws and regulations go better. Good communication and coordination of the audit committee will make GCG run well and motivate companies to carry out sustainability report disclosures as a form of corporate responsibility. Legitimacy theory explains that companies with good environmental performance will increasingly apply sustainability report disclosures. When environmental performance is good, accompanied by sufficient frequency of audit committee meetings, it will motivate companies to comply with regulations by disclosing sustainability reports. In addition, this disclosure is also an effort to gain legitimacy from the public for sustainable company activities and provide comprehensive information about company activities to stakeholders.

Directors who communicate and coordinate well in the board of directors meetings will move the company to carry out social responsibility and reporting to fulfill social responsibility functions related to management functions. Companies whose boards of directors have a high frequency of meetings and have good environmental performance will better disclose comprehensive information; this is because obtaining a high PROPER rating will provide responsibility for the board of directors to disclose *sustainability reports* as a report on the excellent management of the company's environment. This action is a form of providing benefits to *stakeholders,* fulfilling the functions and

responsibilities of the board of directors, namely the function of social responsibility, and an effort to gain public legitimacy toward the sustainability of the company.

Sustainability reports are essential to disclose, so it is important to encourage their improvement. The novelty of this study is on environmental performance measurement as a moderator variable; by measuring environmental performance using the Assessment Results of Company Performance Ratings in Environmental Management (PROPER). The PROPER assessment in the context of research in Indonesia is important and interesting because the Indonesian Ministry of Environment and Forestry issued it. In addition, PROPER is also a reference that is easy for the Indonesian people to understand to see whether the company has carried out its environmental obligations properly in its business processes. Antara et al. (2020) explain that business entities with good environmental performance will disclose sustainability reports more. In line with the theory of legitimacy, companies seek to maintain the trust and support of the public because disclosure sustainability reports present economic, social, and environmental activities. The study aims to determine whether environmental performance with PROPER measurement can play a significant role in the disclosure of sustainability reports to companies in Indonesia, so the hypothesis of this study is:

H_1: Industry type positively affects sustainability report

H_2: Governance committee positively affects sustainability report

H_3: The audit committee positively affects the sustainability report

H_4: The board of directors positively affects the sustainability report

H_5: Environmental performance moderates the relationship between industry types and sustainability reports

H_6: Environmental performance moderates the relationship between governance committees and sustainability reports

H_7: Environmental performance moderates the relationship between the audit committee and the sustainability report

H_8: Environmental performance moderates the relationship between the board of directors and the sustainability report

METHOD

The study obtained data from the IDX website and the official website of each company in the form of secondary data on sustainability reports and annual reports. Based on purposive sampling, 40 companies were obtained with the following criteria: 1) For five consecutive years, the company published sustainability reports and annual reports, 2) Companies that disclose sustainability reports using guidelines from GRI-G4; and Global Reporting Initiative (GRI) standards, and 3) Companies

that follow PROPER for five consecutive years. In the end, 85 units of analysis were obtained, which were processed for hypothesis testing using WarpPLS.

Sustainability report concerning the GRI-4; dividing the number of items found in the report by the total of all GRI items. The industry type is measured by a dummy (1 for High-Profile code and 0 for Low-Profile code). A dummy measures Governance Committee (1 if you have a governance committee and 0 if you do not). The number of meetings a year measures the Audit Committee and Board of Directors variables. At the same time, the Environmental Performance measurement variable uses the rating issued by the ministry of environment and forestry of the Republic of Indonesia [PROPER] (5 for the Gold level, 4 for the Green level, 3 for the Blue level, 2 for the red level, and 1 for the Black level).

RESULTS

The standard deviation value in table 1 for the variables of sustainability reports, independent commissioners, audit committees, directors, and environmental performance is smaller than the average value, so it can be concluded that the data distribution is almost the same or not much different.

Table 1. Descriptive Statistical Analysis

	N	Minimum	Maximum	Mean	Std. Deviation
Audit Committee	85	4	77	14.447	14.314
Board of Directors	85	12	66	30.035	14.131
Environmental Performance	85	3	5	3.659	0.665
Sustainability Report	85	0.088	0.956	0.362	0.181
Valid N (*listwise*)	85				

Source: Processed secondary data

The variables of the type of industry and *governance committee* are *dummy* variables, so they are tested using frequency distributions. The results of the frequency distribution in industrial types explain that the *low-profile* type is smaller than *the high profile*, and the company *has a low* profile of 23.50% and *a high profile* of 76.50%. Then, the frequency distribution of companies with a governance committee is 41.20%, while companies that do not have a *governance committee* are 58.80%.

Table 2. Model Fit and Quality Indices

Criterion	Value	Admission Limits	Conclusion
APC	0.018	≤ 0.05	Model Fit
ARS	0.002	≤ 0.05	Model Fit
AARS	0.016	≤ 0.05	Model Fit
AVIF	1.787	Ideal if ≤ 3.3	Ideal
AFVIF	1.834	Ideal if ≤ 3.3	Ideal
Tenenhaus GoF	0.520	Large if ≥ 0.36	Big
SPR	0.750	Acceptable if ≥ 0.7	Acceptable
RSCR	0.782	Acceptable if ≥ 0.9	Unacceptable
SSR	1.000	Acceptable if ≥ 0.7	Acceptable
NLBCDR	0.938	Acceptable if ≥ 0.7	Acceptable

Table 2 shows only one unacceptable index, but the model is still said to be good and can be used for hypothesis testing. Not all indices must be appropriate and accepted when a study aims to

test a hypothesis (Kock, 2017). A summary of the hypothesis test in this study can be seen in Table 3.

Table 3. Summary of Hypothesis Test Results

		Hypothesis	β	Sig	Result
1.	H_1:	Industry type positively affects *sustainability report*	0.042	0.349	Rejected
2.	H_2:	*Governance committee* positively affects sustainability *report*	-0. 230	0.013**	Rejected
3.	H_3:	The Audit committee positively affects *sustainability report*	0.429	<0.001***	Accepted
4.	H_4:	The Board of directors positively affects *sustainability report*	0.145	0.083*	Accepted
5.	H_5:	Environmental performance moderates the influence of industry types on *sustainability reports*	0.194	0.031**	Accepted
6.	H_6:	Environmental performance moderates the influence of *governance committees* on *sustainability reports*	0.174	0.048**	Accepted
7.	H_7:	Environmental performance moderates the audit committee's influence on *sustainability* reports	-0. 138	0.094*	Accepted
8.	H_8:	Environmental performance moderates the influence of the board of directors on *sustainability* reports	-0. 137	0.096*	Accepted

Source: Secondary Data Processed, 2021.
*** significant 1%
** significant 5%
* significant 10%

DISCUSSION

Industry type does not affect *sustainability report*. These findings do not support *the legitimacy theory;* this is because the type of industry here only explains the difference between the group of companies and the company's characteristics about risks, the field of business, the environment, and the company's employees. Environmental and social activists are not only focused on *high-profile* companies but rather on entities that do not seek to control environmental and social impacts. In addition, support for the SDGs is getting stronger from all countries to disclose sustainability reports. In Indonesia, attention to social, environmental, and reporting activities is indicated by several regulations, namely Law Number 40 (2007) concerning Limited Liability Companies and POJK Number 51 (2017); this discloses *sustainability reports* that were initially voluntary and became mandatory for Financial Services Institutions, Issuers, and Public Companies.

Disclosure of sustainability reports is a form of management awareness of existing regulations. Complying with applicable regulations will make the company gain legitimacy so that the sustainability of the company can be guaranteed better. Thus, high and low profile companies cannot affect the level of disclosure of sustainability reports. A disclosure is based on how much awareness the company needs to maintain its business's sustainability by complying with applicable regulations. This result is supported by Hidayah et al. (2019) and Dissanayake et al. (2019); the type of industry has no impact on the *sustainability report*. However, the results are not in line with Adiatma & Suryanawa (2018), Bhatia & Tuli (2017), and Sinaga & Fachrurrozie (2017), showing that industry type has a positive effect on sustainability reports.

The governance committee negatively impacts the sustainability report, so it does not confirm the stakeholder theory. Based on the data, more sample companies do not have a governance

committee. The absence of this committee has caused the company to focus more on ensuring corporate governance runs well through the organs it owns. The point of view regarding the importance of governance committees stems from the potential for conflict in the view of agency theory (Ruwanti et al., 2019). Focusing on governance with an organizational structure without a special committee (governance committee) is challenging to deal with various agency problems, especially for companies that list on the stock exchange so that they can go to concern. Financial problems can arise due to problems in corporate governance (Rajput, 2015), which causes companies to be more reluctant to present a broad Sustainability Report. The results support Ariyani & Hartomo (2018), who explained that the governance committee negatively affects the sustainability report. Nevertheless, it does not support the findings of Safitri & Saifudin (2019), Aniktia & Khafid (2015), and Suharyani et al. (2019), who showed that governance committees have a positive effect on the disclosure of sustainability reports as well as Azzaki (2019) and Hidayah et al. (2019) who explained that the governance committee does not affect the sustainability report.

The audit committee positively affects sustainability reports. The audit committee's responsibility ensures that management produces reports that provide information regarding the company's business results, financial condition, plans, and long-term commitments. The audit committee can encourage the company to produce a complete report with integrity (Dewi & Pitriasari, 2019). The frequency of meetings conducted by the audit committee makes communication and coordination related to the implementation of corporate responsibilities well-established and smooth. Therefore, the audit committee can motivate companies to fulfill their responsibilities to stakeholders and comply with regulations by disclosing sustainability reports; this can be proven in PT. Timah (Persero) Tbk. 2019 held 77 meetings, and the disclosure rate of sustainability reports was relatively high at 0.597. Meanwhile, PT. Indika Energy Tbk. 2015 held five meetings with a deficient sustainability report disclosure of 0.099. This finding is in line with Indrianingsih & Agustina (2020) and Ruhana & Hidayah (2020), which proved that the audit committee positively impacted the disclosure of sustainability reports. However, the result is not in line with Arumsari & Asrori (2019); Azzaki (2019); Dewi & Pitriasari (2019); Madona & Khafid (2020); and Sinaga & Fachrurrozie (2017), who explained that the audit committee could not affect the sustainability report.

KNKG (2006) states that the board of directors carries out five functions: risk management, management, communication, internal control, and social responsibility; the board of directors must also pay attention to the implementation of corporate social responsibility. The company's communication with stakeholders through sustainability reports will benefit the company. Understanding of the importance of sustainability reports will increase when the board of directors can communicate and coordinate properly, which is reflected through a board of directors' meetings, thus encouraging companies to carry out social responsibility with their reporting.

Table 1 show that meetings held by the board of directors are held 30 times in one year. This meeting effectively discusses matters that are important to the company, including sustainability reports, because of the smooth communication between various parties in the direction of the board of directors. In line with stakeholder theory, the board of directors meeting will impact the disclosure of sustainability reports to fulfill their duties and maintain good relations with stakeholders. Latifah et al. (2019) and Sinaga & Fachrurrozie (2017) revealed that the board of directors positively impacted the *sustainability report*. However, it does not support the findings of the research of Bhatia & Tuli (2017), Fuadah *et al*. (2018), and Indrianingsih & Agustina (2020) , which found that the board of directors did not affect the sustainability report.

High profile or *low profile* is a measurement of industry-type variables. The frequency distribution results revealed that 76.5% of the samples were high-profile companies that were sensitive to the public's response to the impact of the production. High sensitivity in a company will make the company pay attention to broader and better disclosure of environmental performance to gain legitimacy and avoid pressure on environmental and social management (Solikhah & Winarsih, 2016). In this case, the company's good environmental performance encourages high-profile companies always to display sustainability reports. *Legitimacy theory* explains that there is a tendency for entities that have excellent environmental performance to carry out *higher sustainability report* disclosures. High-profile companies will get more attention from the public, and companies with good management skills related to the environment will have the possibility of companies carrying out *sustainability report* disclosures is higher, to gain legitimacy from the public.

The company's environmental performance can weaken the negative influence of the governance committee, meaning that companies with good environmental performance are more willing to present a sustainability report. Distribution statistics show that more sample companies do not have a governance committee. When a company with a limited governance committee only focuses on corporate governance, the presentation of a sustainability report is not a priority. Therefore, the sustainability report will be better if the company has environmental performance. In line with legitimacy theory, companies with good environmental performance will receive public scrutiny so that public legitimacy will be obtained by disclosing sustainability reports. This action is carried out with confidence because the company already has environmental performance that is publicly recognized.

Environmental performance weakens the audit committee's influence on sustainability reports. Table 1 shows that an average audit committee meeting was conducted 14.47 times in one year and environmental performance with an average of 3.66 fell into the blue category. The data in table 1 shows that the sample companies have had good environmental performance (blue category). Environmental performance in the blue category makes the audit committee focus on other

responsibilities following POJK Number 55 (2015), including related audit activities (internal and external), implementation of risk management, providing advice on potential conflicts of interest, and ensuring the confidentiality of company documents or information. Therefore, companies with good environmental performance show that the process of managing entities to meet stakeholder expectations for the environment has been running properly to reduce the burden on the audit committee's role on one aspect related to the fulfillment of regulations related to sustainability reports.

Environmental performance weakens the board of directors' influence on sustainability reports. Table 1 shows that the average environmental performance is 3.66 in the blue category, while board meetings are held 30 times in one year. The presentation of the sustainability report uses components in the Global Reporting Initiative (GRI), while the PROPER environmental performance carried out by the Indonesian government is in the form of color ratings ranging from gold to black. For Indonesian stakeholders, it is easier to understand the concept of PORPER than to read a sustainability report with a GRI fill-in. The results showed that environmental performance with an average score of 3.66 was included in the blue rating, meaning it was pretty good. Indonesians understand that a company with good PROPER means managing the environment well for its business operations. The community considers that good management of the environment shows the company's awareness of sustainable development; this is stated by Baumgartner (2014), who cites Baumgartner (2010) that protecting the environment is the core of the sustainability issue. So for the board of directors, revealing a sustainable report is not a priority when getting an excellent PROPER assessment.

CONCLUSION

The objective of this study is to determine whether environmental performance with PROPER measurements can play a significant role in the disclosure of sustainability reports to companies in Indonesia. The findings of this study indicate that companies disclose higher sustainability reports when communication and coordination of information review and regulatory compliance are carried out properly by the audit committee and directors. Companies without special committees (such as governance committees) will focus more on improving and improving corporate governance than disclosing sustainability reports. Environmental performance assessment in companies in Indonesia through PROPER is generally not optimal because it has yet to enter the gold category, In general in the blue category (two levels below the gold category). Environmental performance can make companies increase disclosure of sustainability reports when related to industry types and governance committees. However, environmental performance will decrease the disclosure of sustainability reports when linked to the audit committee and the board of directors.

PROPER in Indonesia has a role in the disclosure of sustainability reports. However, companies in Indonesia should rely on more than just PROPER to provide information to the public.

Companies also need to disclose sustainability reports to expand the reach of disclosures so that the global community, not only in Indonesia, can understand that companies in Indonesia have contributed to sustainable development. In addition, companies in Indonesia also need to improve their environmental performance in order to achieve a gold category PROPER assessment. The Indonesian government should pay attention, facilitation, and encouragement to companies to achieve the gold category by implementing all the instruments it has because good environmental management is also part of the contribution to sustainable development.

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