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Types of Industries, Financial Performance and Corporate Governance on the Sustainability Report: Insight from Indonesia

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ABSTRACT

This study aimed to examine financial performance and corporate governance mechanisms on sustainability reports based on stakeholder theory and legitimacy theory. Profitability, leverage, and liquidity were the financial performance characteristics investigated in this study. Meanwhile, the corporate governance system variable includes the board of directors, independent commissioners, and audit committees. This study additionally tested the effect of financial factors and corporate governance variables on the sustainability report using industry type as a moderating variable. Except for enterprises in the financial sector, the population of this study included companies listed on the Indonesia Stock Exchange (IDX) that published annual reports and Sustainability reports for the years 2017-2021 with 130 total samples. The data in this study were analyzed using Structural Equation Modelling (SEM) Warp-PLS 7.0. The findings revealed that the financial performance variable was not significantly proven as an indicator of the sustainability report, however, the corporate governance variable was. Furthermore, the kind of industry was discovered to be a pure mediator in the effect of financial performance indicators and corporate governance variables on the sustainability report in this study.

INTRODUCTION

The establishment of the Sustainable Development Goals (SDGs) in 2015 has had consequences for transforming the corporate paradigm (Tilt et al., 2021). The single P (Profit) business paradigm, which focuses the company's attention solely on company profits, has now evolved into a triple bottom line business paradigm (Profit, People, Planet), which focuses on three things: profit, which pays attention to the interests and welfare of shareholders, people, which is more concerned with the welfare of society, and the planet, which is a form of the company's active participation in environmental preservation (Harymawan et al., 2020).

According to the triple bottom line concept, companies must be able to expand sustainably by focusing on factors other than company revenues. This demonstrates that corporate information disclosure is not restricted to one area of financial performance, but also includes total sustainability performance indicators, such as economic, social, and environmental performance (Ong and Djajadikerta, 2020). In this light, the sustainability report becomes an important document that the corporation must present as a form of corporate social and environmental responsibility.

Disclosure of economic, social, and environmental data in sustainability reports is an effective medium for companies to establish community credibility (Schaltegger et al., 2017). In the study of legitimacy theory, sustainability reports can be evidence of the company against the community's assessment that the company's operating activities are following societal norms (Schaltegger et al., 2017; Tilt *et al.*, 2021). Meanwhile, the stakeholder study theory explains that companies are responsible not only to company owners, but also to other stakeholders, companies can use voluntary disclosure of information about economic, social, and environmental performance to gain recognition that they pay attention to all stakeholder interests (Amidjaya and Widagdo, 2020; Stocker et al., 2020). Much research on sustainability reports has been undertaken. Researched the influence of financial performance factors on sustainability reports, as done by (Schaltegger et al., 2017; Wardhani et al., 2019). While other research conducted by (Schaltegger *et al.*, 2017; Al-Shaer and Zaman, 2019; Amidjaya and Widagdo, 2020; Ong and Djajadikerta, 2020; Stocker *et al.*, 2020), that examined the influence of corporate governance on the sustainability report.

Various research on the determinants of the issuance of sustainability reports has found discrepancies in the impact of the company's financial performance and corporate governance on the sustainability report. Based on this, the industry type variable is added as a moderating variable in this study, which is projected to diminish or increase the effect of the company's financial performance and corporate governance variables on the sustainability report.

1. LITERATURE REVIEW

1.1 Stakeholder Theory

Stakeholder is any group or individual who can influence or is influenced by the attainment of corporate goals. Stakeholder theory explains which parties the corporation is accountable to (Valentinov and Chia, 2022). Companies must maintain connections with their stakeholders by meeting their wants and requirements, particularly those who influence the availability of resources required for the company's operational operations, such as workers, the market for the company's products, and others (Freeman et al., 2021). The rise of stakeholder theory as the prevailing paradigm reinforces the idea that companies are accountable not just to their shareholders but also to their stakeholders (Dissanayake *et al.*, 2019). All stakeholders, according to stakeholder theory, have the same right to acquire information about all firm operations.

1.2 Legitimacy Theory

Legitimacy theory asserts that companies have social contact with communities around the company's operating environment because companies use both human and natural resources around the company's environment (Akhter et al., 2022). As a result, the organization will continue to endeavor to function within the framework and standards that exist in the community or area in which it is located. Companies strive to guarantee that their actions (companies) are considered legitimate by outsiders (Ogunode, 2022).

The social contract and the company's concern for the environment are examples of corporate social responsibility to benefit the environment (Talbot and Boiral, 2018). If a company makes social disclosures, it believes that its existence and operations will gain legitimacy from the community or environment in which the company works (Tarmuji et al., 2016; Drempetic et al., 2020). According to legitimacy theory, the practice of exposing corporate responsibility must be conducted in such a way that the community may accept the company's activities and performance (Lanis and Richardson, 2013). Companies employ environmental-based performance and disclosure of environmental information to legitimate their actions in the eyes of the public.

1.3 Sustainability Reporting

According to the Global Reporting Initiative (GRI), sustainability reporting is the process of measuring, revealing, and holding organizations accountable for their efforts to achieve sustainable development goals to both internal and external stakeholders (He, 2022). Sustainability reporting is a broad phrase that is used to describe reports on economic, environmental, and social implications (Adhariani and du Toit, 2020). A sustainability report is a report that comprises not only financial performance information but also non-financial information such as information on social and environmental activities that help organizations to expand sustainably (sustainable performance). A sustainability report provides a balanced and fair picture of the sustainable performance of the organization, including positive and negative contributions (Martín and M Moneva, 2018; Aggarwal and Singh, 2019; Amidjaya and Widagdo, 2020).

1.4 Financial Performance

Financial performance is a description of a company's financial situation within a specific period (Amidjaya and Widagdo, 2020). The financial performance of the firm is concerned with the elements of raising and distributing cash. Furthermore, financial performance is an indicator of the firm's achievement, which may be understood as the results of numerous operations carried out by the organization. Financial performance may be described through an examination of the outcomes or accomplishments attained by the firm's management in carrying out its role of properly managing company assets over a given period (Wahyuningtyas et al., 2022). Financial ratios such as profitability, liquidity, and leverage are one approach to assessing financial performance .

Profitability is a company's ability to earn profits over a specific period. Profitability allows management the freedom and flexibility to reveal social responsibility to shareholders (Aggarwal and Singh, 2019). As a result, the bigger the degree of firm profitability, the greater the amount of social information sharing. If a firm is liquidated, leverage is its capacity to satisfy its financial commitments, both short and long-term (Wardhani et al., 2019). Organizations with a high degree of leverage are heavily reliant on external loans to finance their assets, whereas companies with a low level of leverage fund their assets with their resource. Meanwhile, liquidity is a measure used to assess a company's capacity to fulfill maturing debts. Companies with a high degree of liquidity have great economic performance. This can motivate organizations to reveal more information to their stakeholders to demonstrate their credibility. A high liquidity ratio indicates the company's strength, which is related to a high level of transparency.

1.5 Corporate Governance

Corporate governance is a set of methods that represent a good corporate management structure in defining how rights and obligations are distributed among the many stakeholders engaged in the organization. Shareholders, the board of directors, independent commissioners, the audit committee, and other interested parties are among the many parties (Amidjaya and Widagdo, 2020). The person designated to run the company is the board of directors, which can be the individual who owns the company or a professional person nominated by the company owner (Ong and Djajadikerta, 2020). The board of directors is a component of a company's control structure, with two functions: monitoring and decision-making (Al-Shaer and Zaman, 2019). An independent commissioner is a member of the board of commissioners who has no commercial or familial ties to the controlling shareholder, other members of the board of directors and commissioners, or the firm itself (Al-Shaer and Zaman, 2019). The term independent commissioners refer to their role as representatives of independent shareholders as well as investors' interests. As part of the implementation of strong corporate governance, the presence of an independent board of commissioners will push corporations to make greater disclosures to their stakeholders, one of which is the publication of sustainability reports (Ong and Djajadikerta, 2020).

The Audit Committee is defined as a committee constituted and accountable to the board of commissioners to assist in carrying out the board of commissioners' duties and activities. The presence of an audit committee might encourage corporations to publish a thorough and trustworthy report. The existence of an audit committee can help ensure disclosure so that the control system will run well (Hoseini et al., 2019).

1.6 Industry Type

The industry type is a categorization of businesses based on their primary activity. The industry type of a firm indicates its scope of activities, corporate risk, and capacity to address business issues (Lanis and Richardson, 2013). The distinction between high-profile and low-profile industries is used to determine industry type. In general, high-profile corporations attract public attention because their operating operations can cross with broad interests. Society is more sensitive to this sort of industry in general since the company's neglect in ensuring the manufacturing process and production outcomes can have a significant influence on society (Lanis and Richardson, 2013).

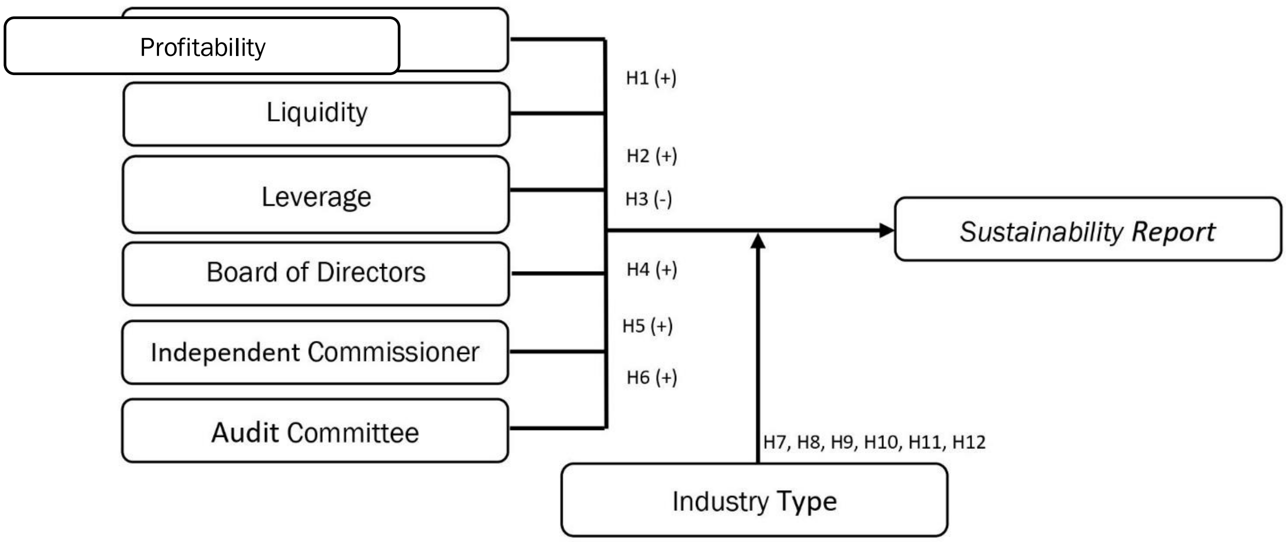

Figure 1. Theoretical Framework

Source: own

1.7 Research Hypothesis

The hypotheses of this study taken from the framework of thinking as written in Figure 1.:

H1: Profitability has a positive and significant effect on the disclosure of the sustainability report

H2: Liquidity has a positive and significant effect on the disclosure of the sustainability report

H3: Leverage has a negative and significant effect on the disclosure of the sustainability report

H4: The board of directors has a positive and significant effect on the disclosure of the sustainability report

H5: Independent Commissioner has a positive and significant effect on the disclosure of the sustainability report

H6: The audit committee has a positive and significant effect on the disclosure of the sustainability report

H7: Industry type significantly moderates the relationship between profitability and sustainability reports

H8: The type of industry significantly moderates the correlation between liquidity and the sustainability report

H9: The type of industry significantly moderates the correlation of leverage to the sustainability report

H10: The type of industry significantly moderates the correlation between the board of directors and the sustainability report

H11: The type of industry significantly moderates the correlation of the independent commissioner to the sustainability report

H12: The type of industry significantly moderates the correlation between the audit committee and the sustainability report.

2. METHODS

The purpose of this study was to use quantitative research to investigate the effect of financial performance and corporate governance variables on the sustainability report. Except for the banking sector, the population of this research consists of firms listed on the Indonesia Stock Exchange (IDX) that submit annual reports and sustainability reports for the years 2017-2021. These sectors include agriculture, mining, basic and chemical industries, different industry sectors, commodities and consumption, real estate property and building construction, infrastructure, utilities, and transportation. The financial sector was excluded from the research sample since it has little responsibility for environmental consequences in comparison to the other industries included in the IDX. SEM Warp-PLS version 7.0 was used for data analysis in this study, which is a powerful structural equation (SEM) technique for identifying non-linear correlations between latent variables and correcting path coefficient values (Zeng et al., 2021).

Table 1. Purposive Sampling

No	*Criteria*	*Not Entry Criteria*	*Total*
	Population		592
1	Non-financial companies listed on the IDX during the 2017-2021 period	(0)	592
2	Non-financial companies that issue sustainability reports separately from financial reports during the 2015-2018 period using the GRI G4 and/or GRI guidelines in sustainability reports	(566)	26
3	Year of Observation		5
	Total Units of Analysis		130

Source: own

3. RESULT AND DISCUSSION

Table 2. Descriptive Statistics

Variable	*n*	*Minimum*	*Maximum*	*Mean*	*Std. Deviation*
SRDI (Y)	130	0.0769	0.7532	0.323	0.1552
ROA (X1)	130	-0.558	0.4666	0.0461	0.1128
DER (X2)	130	-3.335	0.2576	1.3128	1.1486
CR (X3)	130	0.2229	4.8866	1.5312	1.0174
D (X4)	130	5	66	30.525	14.516
IC (X5)	130	20	75	37.385	8.2424
AC (X6)	130	4	45	12.242	10.193
IT (M)	130	0	1	0.8077	1.0538
Valid N (listwise)	130				

Source: own

3.1 Outer Model Test

Table 3. Convergent Validity Test Summary

Variable	*Factor Loading*	*Remark*
Profitability (ROA)	1.000	Valid
Leverage (DER)	1.000	Valid
Liquidity (CR)	1.000	Valid
Board of Directors (D)	1.000	Valid
Independent Commissioner (IC)	1.000	Valid
Audit Committee (AC)	1.000	Valid
Industry Type (IT)	1.000	Valid
Sustainability Report (SRDI)	1.000	Valid

Table 4. Discriminant Validity Test Summary (AVE)

Variable	ROA	DER	CR	IC	AC	IT	SRDI	ROA
	1.000	0.233	0.241	0.147	0.158	0.204	0.215	0,234
DER	0.233	1.000	0.219	0.184	0.223	0.263	0.187	0,252
CR	0.241	0.219	1.000	0.194	0.391	0.210	0.182	0,246
D	0.147	0.184	0.194	1.000	0.276	0.251	0.179	0,221
IC	0.158	0.223	0.391	0.276	1.000	0.214	0.142	0,216
AC	0.204	0.263	0.210	0.250	0.214	1.000	0.138	0,237
IT	0.215	0.187	0.182	0.179	0.142	0.138	1.000	0,250
SRDI	0.249	0.252	0.246	0.221	0,216	0.237	0.250	1,000

Source: own

Table 5. Reliability Test Summary

Variable	*Cronbach's Alpha*	*Remark*
Profitability (ROA)	1.000	Reliable
Leverage (DER)	1.000	Reliable
Liquidity (CR)	1.000	Reliable
Board of Directors (D)	1.000	Reliable
Independent Commissioner (IC)	1.000	Reliable
Audit Committee (AC)	1.000	Reliable
Industry Type (IT)	1.000	Reliable
Sustainability Report (SRDI)	1.000	Reliable

Source: own

3.2 Inner Model Test

Table 6. R-Square and Q-Square Test Summary

Endogen Latin Variable	R-Square	Q-Square
Sustainability Report (SRDI)	0.365	0.378

Source: own

Table 7. The goodness of Fit Test Summary

Model	*Value*	*Threshold*	*Remark*
Average Path Coefficient (AVC)	0.184, P=0.038	P<0.05	Fit
Average block VIF (AVIF)	2.676	<5	Accepted

Source. own

3.3 Hypothetical Test Hypothesis

According to the findings of testing and data analysis on table 8. the financial performance variable was not significantly proved to be one of the factors that affect the sustainability report. While the findings of corporate governance variable testing and data analysis revealed substantial results as one of the factors that affect the sustainability report. Based on the findings of this study, the company should pay close attention to the corporate governance variable, as it has a substantial effect on the level of the company's sustainability report. Increasing the company's sustainability report will pique the interest of investors. Further testing revealed that the industry type variable was a pure moderator in the effect of financial factors and corporate governance on sustainability reporting.

Based on the findings of this study's investigation of the effect of the financial performance variable on the sustainability report, the financial performance variable was not substantially demonstrated as an indicator of the sustainability report. The P-value statistical variables of profitability, leverage, and liquidity were more than the P-value threshold (>0.05). According to the legitimacy theory, the corporation will attempt to send positive information to parties outside the organization to obtain legitimacy, such as the fact that the company functions efficiently and effectively and has strong performance (Schaltegger *et al.*, 2017). Based on this, companies with strong financial performance will opt to emphasize the publication of financial performance information above information concerning voluntary sustainability reports (Schaltegger et al., 2017). Disclosure of sustainability reports is a kind of business attention directed only toward stakeholders and is not solely motivated by the corporation's feeling of duty to stakeholders (Ogunode, 2022).

Table 8. Hypothetical Test Hypothesis Summary

Path	*Direct Effect*			*Remark*
	B	*P-Value*	*P-Value (Threshold)*	
ROA	0.23	0.097	<0.05	Not significant
DER	-0.61	0.103	<0.05	Not significant
CR	0.16	0.096	<0.05	Not significant
AC	0.73	0.032	<0.05	Significant
D	0.36	0.010	<0.05	Significant
IC	0.59	0.021	<0.05	Significant
IT	1.52	0.073	<0.05	Not significant
Path	*Indirect Effect*			Remark
	B	P-Value	P-Value (Threshold)	
ROA*IT	0.47	0.022	<0.05	Significant
DER*IT	-0.71	0.041	<0.05	Significant
CR*IT	0.29	0.019	<0.05	Significant
AC*IT	0.64	0.036	<0.05	Significant
D*IT	0.29	0.024	<0.05	Significant
IC*IT	0.48	0.039	<0.05	Significant

Source: own

The results of the data test in this study also revealed that the corporate governance variable had an impact on the sustainability report, as evidenced by a statistically significant value between the corporate governance variables, namely the audit committee variable, the board of Directors variable, and the independent commissioner variable, P-value threshold (0.05). Companies, according to stakeholder theory, are supposed to prioritize not just the interests of management and capital owners (investors and creditors), but also the interests of employees, consumers, and the larger community. Stakeholder theory may also be used to help corporations give transparent, accountable information, as well as to help with organizational/company governance. According to the stakeholder theory, it compels the company to reveal more of its operations, including its social initiatives, one of which is through a sustainability report.

The test findings on the industry type moderating variable revealed that it was an industry type as a pure moderator in the effect of financial performance and corporate governance factors on the sustainability report. According to the stakeholder theory, the company is responsible not only to the company's owner but also to the interested parties. As stated by high-profile companies receive greater attention from interested parties, including the general public than low-profile companies. Because a few mistakes committed by high-profile corporations might have devastating effects on the community, the public will be more sensitive to them (Lanis and Richardson, 2013; Drempetic *et al.*, 2020). For example, inappropriate waste management by high-profile enterprises will garner more public notice. To prevent this issue, the corporation will opt to mention it in its sustainability report.

CONCLUSION

The purpose of this study is to collect empirical information on the Effect of financial performance and corporate governance variables on sustainability report disclosure in companies listed on the Indonesia Stock Exchange between 2017 and 2021, with industry type acting as a moderating variable. Based on the findings of this study's testing and data analysis, it is possible to infer that the financial performance variables (profitability, leverage, and liquidity) have no demonstrable effect on the sustainability report. In contrast, corporate governance variables (audit committee, board of directors, and independent commissioners) had a substantial impact on the quantity of disclosure in the sustainability report. This means that management considers corporate governance and prioritizes corporate transparency and accountability to demonstrate that the company is concerned with the interests of all stakeholders, such as by submitting a report on the company's social activities in the form of a sustainability report. The findings of the tests on the industry-type moderating variable reveal that there is a pure moderator in the effect of financial performance and corporate governance variables on the sustainability report.

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APPENDIX

Variable Measurement

Variable and Concept	*Measurement*
Sustainability Report (Y) Company The Practice of Accountability for Organizational Performance in Achieving Sustainability Development Goals	SRDI = the Number of Items Disclosed by the Company Expected Item Quantity
Profitability Company's Ability to Generate Profit	ROA = Net Profit after Tax Total Assets
Leverage Company Ability to Fulfill Obligations	DER = Total Liability Total Equity
Liquidity Company's Ability to Maximize Current Assets to Fulfill Short Term Obligations	CR = Current Assets Current Liability
Audit Committee	AC =Number of Annual Audit Committee Meetings/Year
Board of Directors	D = Frequency of Meeting Members of the Board of Directors/Year
Independent Commissioner	IC = Σ Independent Commissioner Σ Board of Commissioners
Industry Type	IT= High Profile = have good consumer visibility, a high level of political risk, and high competition = score 1 Low Profile = have low consumer visibility, low level of political risk, and low competition = score 0