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The Effect of ESG-Corporate, Company Size, and Size of Board Director on Financial Performance with Audit Quality as a Moderating Variable in Public Companies in Indonesia

Haniffia Hamidah [1], Dewita Puspawati [2]

[1]*Muhammadiyah University of Surakarta, Indonesia.*
[2]*Muhammadiyah University of Surakarta, Indonesia.*

ABSTRACT: *This study aims to determine the effect of ESG, company size, and the size of the board of directors on the company's financial performance, with audit quality as a moderating factor. This research was conducted on companies listed on the Indonesia Stock Exchange for the 2017–2021 period. The number of samples used was 50 companies with 198 observations. The sample was determined using the purposive sampling method. The research data used moderate regression analysis. The results of this study indicate that ESG does not affect the company's financial performance. The size of the company and the size of the board of directors have an impact on the company's financial performance. Audit quality cannot moderate the influence of ESG, company size, and board size on the company's financial performance.*

Keywords: *ESG-Corporate; Company Size; Size of Board Director; Financial Performance; Audit Quality.*

I. INTRODUCTION

Over the last two decades, there has been an increase in the awareness of business people about supporting environmental sustainability and the positive impact of conducting socially responsible business activities. Business activities are now not only focused on how to generate significant profits but also on operational activities that have an impact on environmental damage. One of the causes of environmental damage is the inappropriate use of resources and ignorance of applicable regulations or norms. This action can affect social conflict because the company's performance parameters are often measured only based on high profits. Previously, investors considered ESG performance irrelevant and expensive (Putra & Adrianto, 2019). However, a growing consensus is that companies should include ESG when measuring financial performance. ESG refers to three core factors that measure sustainability and ethical impact and are used to make investment decisions in a particular company. These three factors are environmental, social, and corporate governance (Septiana & Dewita, 2022). According to Derwall et al. (2005) shows that a good issuer will have a high ESG score. That is, ESG is directly proportional to ROA and company profitability. In addition, an assessment of a company's environmental performance will significantly impact the firm value (Eccles et al., 2012). As a result, companies that disclose ESG performance can achieve a higher rate of ROA and continue to grow sustainably (Hassel, 2013).

However, in practice, there are still problems that arise in Indonesia related to the company's operational activities that pay little attention to the surrounding environmental conditions—especially companies whose activities are related to natural resource management. Several cases were found, such as environmental pollution due to the accumulation of waste and burning forests to clear areas, and many

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companies still do not disclose environmental performance in their annual reports (Zahroh & Hersugondo, 2021).

This phenomenon is proof that there are still many companies that only focus on achieving profits and set aside responsibility for environmental, social, and corporate governance performance. This behavior is contrary to Financial Services Authority Regulation Number 29/POJK.04/2016 concerning Annual Reports of Issuers or Public Companies, which must contain at least a general description of critical financial data, stock information, reports of directors, reports of the board of commissioners, company profiles, analysis and discussion of management, corporate governance, corporate social and environmental responsibility, audited financial statements, and statements of members of the board of directors and board of commissioners regarding the responsibility for annual reporting. Public companies that do not implement ESG can influence the investment decisions of their shareholders. This action also affects the business climate in Indonesia, which has a direct impact on the success of the company's performance and good reputation (Triyani et al., 2021).

Thus, this study combines several variables that influence a company's financial performance, such as ESG-Company, company size, board of director size, and audit quality, as moderating variables. There is research that discusses the company's financial performance, including Ahmad et al. (2021), Zahid et al. (2022), Nguyen et al. (2021), Risna & Aditya (2021), Majeed et al. (2020), and Manyaga et al. (2019). With inconsistent results and differences in research, the researchers tried to re-examine it by adding an update to the board of directors' size variable as an independent variable.

II. MATERIAL AND METHODS

2.1. Financial Performance

Financial performance is the level of achievement the organization achieves to achieve sound financial management results. Financial statement analysis can be used to evaluate financial performance. Financial ratio analysis integrates the parts of the plan and profit and loss calculations to measure the success and efficiency of the company (Sanjaya, 2018).

2.2. ESG-Corporate, Company Size, and Size of Board Director

ESG has three factors broadly defined as environmental, social, and governance. Environmental aspects concern the company's physical relationship with the environment, social elements concern the company's social impact on society, and governance factors concern how the company is managed (Stobierski, 2021). ESG has now become a significant aspect of corporate social responsibility or sustainability. This guide responds to investors by integrating ESG issues into investment analysis and providing recommendations on a standard set of procedures. Company size is a scale based on the total assets of a company or organization that integrates and manages many resources to produce goods or services for sale (Brigham & Houston, 2013). Company size can be classified into several categories, including micro, small, medium, and large businesses.

The board of directors is an organ that is authorized and entirely responsible for managing the company for the benefit of the company by following the stated aims and objectives and representing the company both inside and outside the company. The board of directors is a party in the corporation whose role is to carry out the operations and management of the company. With such a prominent role in running this corporation, the directors have enormous control rights in managing corporate resources and investor capital (Adestian, 2015).

2.3. Audit Quality

Audit quality is the possibility that the auditor will find and report substantial misstatements in the client's financial statements (Watkins et al., 2004). Auditor quality can be seen in the performance of the public accounting firm (KAP) in the audit process by following auditing standards. A shorter audit duration is a KAP way to protect its reputation and avoid possible client loss. However, almost all KAPs in Indonesia follow the same audit method based on auditing standards and Indonesian legal regulations. International public accounting firms, often known as The Big Four, require less time to conduct audits because these KAPs are believed to be more efficient and have a degree of schedule flexibility to complete the audit on time. Because their reputation is at stake, the Big Four KAP prefers to take the right attitude, issue legal opinions, and have the technical ability to detect the company's continuity.

The Effect of ESG-Corporate on Financial Performance

Companies must pay attention to the environmental conditions in which they carry out their operations. If the company gets a high score in terms of environmental concern, then the survival of the company will also be high. Research conducted by Hwang et al. (2021), De Lucia et al. (2020), and Fernández et al. (2019) shows that ESG performance has a significant influence on a company's financial performance. This result is in line with stakeholder theory, where companies will gain the trust of the public and all company stakeholders and also influence investors' decisions to invest in the company.

H1: ESG affects the company's financial performance

The Effect of Company Size on Financial Performance

Company size tells about the company's size, which can be calculated using the company's total assets. According to Prasetyorini (2013), company size impacts financial performance because the more significant the company, the easier it is to secure internal and external funding sources. Research conducted by Umukoro et al. (2021), Cincalová et al. (2020), and Sekarwati et al. (2018) show that company size has a significant influence on the company's financial performance. This result is in line with signaling theory, where the bigger a company is, the better the signal it sends to outsiders, and this affects the company's financial performance.

H2: Company size affects the company's financial performance

The Effect of the Size of Board Director on Financial Performance

Directors have tremendous power over the management of company resources and investor capital. The greater the number of directors on a board, the more those who monitor the administration of company resources. Previous research by Majeed et al. (2020) and Sulistyowati (2017) show that the greater the number of board directors in a company, the easier coordination and communication will be, resulting in better financial performance.

H3: The size of the board of directors affects the company's financial performance

Audit Quality Moderate The Effect of ESG-Corporate on Financial Performance

Public accounting firms with good reputations have good human resources to carry out the audit process according to procedures to guarantee audit quality. The Big Four KAPs help ensure the company's financial reports are reliable, transparent, and meet high-quality audit standards. In addition to supporting a good company's ESG, audit quality can help improve a company's financial performance. Previous research by Zahid et al. (2022) stated that audit quality affects the influence of ESG on the company's financial performance.

H4: Audit quality moderates the influence of ESG on the company's financial performance

Audit Quality Moderate The Effect of Company Size on Financial Performance

Audit services will affect investor confidence that the resulting financial reports are of high quality and can be used to make decisions. Large companies will choose credible KAP services to guarantee audit quality and help improve the company's financial performance. The company's financial performance goes well, along with the increase in the size of the company, because reasonable internal control will minimize errors in operations and the preparation of financial reports. Previous research by Santoso et al. (2017) stated that audit quality strengthens the relationship between company size and financial performance.

H5: Audit quality moderates the influence of company size on the company's financial performance

Audit Quality Moderate the Effect of The Size of Board Director on Financial Performance

The board of directors is fully responsible for all operational operations and management of the company to achieve company goals. The Board of Directors controls managing company resources and investor funds. The greater the number of directors on a board, the more those who monitor the administration of company resources so that financial performance can run well according to company procedures. Based on previous research examining the relationship between board size and financial performance, no one has added audit quality as a moderating variable. Therefore, this study tries to fill this gap. This research will examine how audit quality can affect the relationship between board size and company financial performance.

H6: Audit quality moderates the influence of board size on the company's financial performance

III. RESEARCH METHOD

The type of research used in this study is quantitative with data sources obtained from annual reports of companies listed on the Indonesia Stock Exchange (IDX) for the 2017-2021 period and the Thomson Reuters Database. The total number of samples in this study was 198 observations using the purposive sampling method. Table 1 describes the criteria for the sample used.

Table 1. Research Sample Criteria

Selection Criteria	Research Period					Total
	2017	2018	2019	2020	2021	
Companies listed on the IDX during the study period	566	619	688	713	766	3352
Criteria:						
Companies that do not provide financial statement data	(70)	(52)	(40)	(6)	(46)	(214)
Companies that do not have a Thomson Reuters ESG score	(456)	(525)	(605)	(661)	(670)	(2917)
Companies that do not have complete data according to IDX requirements	-	-	-	-	-	-
Total Sample Study	**40**	**42**	**43**	**46**	**50**	**221**
Total Outlier Sample						**(23)**
Amount Sample						**198**

Source: IDX data that has been processed, 2023

The dependent variable in this study is the company's financial performance proxied by ROA and MBV, while the independent variables consist of ESG, company size, and board size, as well as audit quality as moderating variables in this study. An explanation of the variables and measurement indicators is in table 2 below.

Table 2. Research Variable and Indicators

Dependent Variable	Indicator	Source
Company's Financial Performance (FP)	$ROA = \frac{\text{Net Income}}{\text{Total Assets}} \times 100\%$ $MBV = \frac{\text{Price Per Share}}{\text{Book Value Per Share}} \times 100\%$	Kusumawati et al., 2018
Independent Variable ESG-Corporate (ESG) Company Size (CS) Size of Board Director (SBD)	 **Thomson Reuters ESG Score** **CS = Ln (Total Assets)** **SBD = ∑ Board of Director**	 www.thomsonreuters.com Odalo et al., 2016 Majeed et al., 2020
Moderating Variable Audit Quality (AQ)	 **Dummy Variable 0 and 1**	 Zahid et al., 2022

The data sources used are financial and company annual reports, which are then processed using the moderation regression analysis method with the help of statistical software, namely IBM SPSS version 26.

IV. RESULT

Moderation regression analysis tested the hypothesis in this study. This analysis is part of multiple linear regression, which combines interaction elements in the regression, namely the multiplication of two or more independent variables with a moderating variable). Moderation regression analysis aims to find out whether the moderating variable can strengthen or weaken the relationship between the independent and dependent variables (Ghozali, 2018). The results of the moderation regression analysis can be seen in Tables 3 and 4 below.

Table 3. Moderation regression analysis (Y= ROA)

Variable	Regression Coefficient	T_{Count}	Sig.	Information
Constant	86,314	6,897	0,000	
ESG	0,011	0,539	0,590	H_1 rejected
Company Size	-2,676	-6,152	0,000	H_2 accepted
Size of Board Director	0,639	2,594	0,010	H_3 accepted
X_1 * Audit Quality	0,072	1,118	0,265	H_4 rejected
X_2 * Audit Quality	-0,895	-0,563	0,574	H_5 rejected
X_3 * Audit Quality	0,501	0,758	0,449	H_6 rejected
R^2 = 0,185		F_{Count} = 14,640		
Adjusted R^2 = 0,172		Sig. = 0,000		

Source: SPSS output, 2023

Table 4. Moderation regression analysis (Y= MBV)

Variable	Regression Coefficient	T_{Count}	Sig.	Information
Constant	1514,391	4,059	0,000	
ESG	0,109	0,178	0,859	H_1 rejected
Company Size	-43,729	-3,372	0,001	H_2 accepted
Size of Board Director	12,045	1,639	0,103	H_3 rejected
X_1 * Audit Quality	-0,130	-0,068	0,946	H_4 rejected
X_2 * Audit Quality	100,617	2,143	0,033	H_5 accepted
X_3 * Audit Quality	20,767	1,064	0,289	H_6 rejected
R^2 = 0,062		F_{Count} = 4,307		
Adjusted R^2 = 0,048		Sig. = 0,006		

Source: SPSS output, 2023

The Effect of ESG-Corporate on Financial Performance

Based on the results of testing the first hypothesis, the result is that ESG does not affect the company's financial performance as measured through the ROA indicator. This result can be explained by the fact that expenses for environmental and social purposes can increase expenses and reduce company profitability. Likewise, the test results measured through the MBV indicator show the same thing. The result can be explained that the company's low profitability will affect the book value stock price. These results support the research of Zahid et al. (2022), which revealed that the ESG factor does not affect the company's financial performance.

The Effect of Company Size on Financial Performance

Based on the results of testing the second hypothesis, it was found that company size affects the company's financial performance as measured by the ROA indicator. This result can be explained by the higher the size of the company, the higher the company's ability to generate profits with its assets. Likewise, the test results measured through the MBV indicator show the same thing. This result can be explained by the fact that high company assets produce good book values and stock prices, thus increasing investor interest. These results support the research of Nguyen et al. (2021), which revealed that company size affects the company's financial performance.

The Effect of the Size of Board Director on Financial Performance

Based on the results of testing the third hypothesis, it was found that the board of director's size affects the company's financial performance as measured by the ROA indicator. This result can be explained by the fact that the larger the size of the board of directors, the more it influences the quality of better decision-making to help improve the company's financial performance. These results support the research of Majeed et al. (2020), which revealed that the size of the board of directors significantly affects the company's financial performance. However, the test results are measured through the MBV indicator, which shows that the size of the board of directors does not affect the company's financial performance. The larger size of the board of directors will limit the responsibilities of the board of directors, which has the potential to cause problems in the communication process in decision-making. This matter will have an impact on decreasing the company's financial performance.

Audit Quality Moderate the Effect of ESG-Corporate on Financial Performance

Based on the results of testing the fourth hypothesis, it is found that audit quality cannot moderate the effect of ESG on the company's financial performance as measured by the ROA indicator. This result can be explained by the fact that the ESG value does not affect the company's financial performance because spending funds for environmental and social purposes will reduce its profitability. So that no matter how good the quality of the audit used will not be able to moderate the relationship between ESG and the company's financial performance. Likewise, the test results measured through the MBV indicator show the same thing. This result can be explained by the fact that low profitability will affect the company's stock price. So that no matter how good the quality of the audit used will not be able to moderate the relationship between ESG and the company's financial performance. These results support the research of Zahid et al. (2022), which revealed that the interaction of ESG with audit quality does not affect the company's financial performance.

Audit Quality Moderate the Effect of Company Size on Financial Performance

Based on the results of testing the fifth hypothesis, it was found that audit quality cannot moderate the effect of company size on the company's financial performance as measured by the ROA indicator. This result can be explained by the fact that the bigger the company, the better it is at managing its assets, so its profitability also increases. With good audit quality, it cannot moderate the relationship between company size and financial performance. However, the test results, as measured by the MBV indicator, show that audit quality moderates the effect of company size on the company's financial performance. This result can be explained by the more significant the company is and the better it manages its assets to increase its market capitalization. Good audit quality can support an increase in the company's stock price. These results support the research by Santoso et al. (2017), which revealed that the interaction between company size and audit quality affects the company's financial performance.

Audit Quality Moderate the Effect of The Size of Board Director on Financial Performance

Based on the results of testing the sixth hypothesis, it was found that audit quality cannot moderate the effect of board size on the company's financial performance as measured by the ROA indicator. This result can be explained by the fact that the larger the size of the board of directors of a company, the better the quality of decision-making. Making the right decision can improve the company's financial performance. With good audit quality, it is not necessarily able to moderate the relationship between the size of the board of directors and the company's financial performance. Likewise, the test results measured through the MBV indicator show the same thing. This result can be explained that the larger the board of directors, the better the director's independence level and allows them to make the right decisions. So with good audit quality, it is not necessarily able to moderate the relationship between the size of the board of directors and the company's financial performance.

V. CONCLUSION

This study proves that ESG does not affect ROA or MBV. Company size affects ROA and MBV. The size of the board of directors affects ROA, but it does not affect MBV. Audit quality does not moderate the influence of ESG on the company's financial performance, both ROA and MBV. Audit quality does not moderate the effect of company size on ROA, but it does moderate the effect of company size on MBV. Audit quality does not moderate the effect of board size on the company's financial performance, both ROA and MBV.

By the results of the research that has been done, the suggestions for future researchers are expected to improve the research by adding other indicators to measure the effect of ESG on company financial performance and other variables not examined by researchers. Thus it is expected to see whether there are differences in results when using independent variables and other measurement indicators.

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