JAMBURA ECONOMIC EDUCATION JOURNAL
Volume 6 No 1 January 2024
E-ISSN: 2656-4378 *P-ISSN:* 2655-5689
https://ejurnal.ung.ac.id/index.php/jej/index,

Volume 6 No 1 2024

hlm. 17 - 37

THE IMPACT OF ESG ON FIRM VALUE WITH AUDIT COMMITTEE AS VARIABLE MODERATING

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ABSTRACT

This research aims to present empirical evidence regarding the impact of environmental, social and governance (ESG) factors on company value, by including audit committee attributes (Expertise, length of service, gender and total) as moderating elements. This study uses a sample of companies that have an ESG score index and are listed on the IDX during the 2018-2022 research period. The sample selection method used is purposive sampling. The results prove that environmental, social, and governance (ESG) have a negative effect on firm value. The audit committee in this study was not able to moderate the relationship between environmental, social and,governance (ESG) and firm value. The implications of this study are enormous because it provides support for the application of stakeholder, legitimacy and agency theories. However, it is important to underline that the scope of this study is limited to companies in Indonesia, therefore the conclusions may not be directly transferable to other countries.

Keywords: *ESG Score, Firm Value, Audit Committee*

INTRODUCTION

Investor interest in environmental-related hazards, as well as non-financial factors like social responsibility and good governance, is putting pressure on companies. Investors, workers, suppliers, consumers and governments increasingly expect companies to be aware of these, take appropriate mitigation measures and report on them properly. The implementation of ESG reporting is being encouraged globally, and it has recently emerged as one of the most important subjects. Furthermore, as most organizational stakeholders think that disclosing ESG information will improve future business performance, risk management, and reputation, it should be done. Moreover, the company's reputation will be enhanced by ESG disclosure (Rabaya & Saleh, 2022).

ESG Score is a phrase used in the ESG (Environmental, Social, and Governance) concept. The ESG score, which refers to Environmental, Social, and Governance, is a statistic used to analyze a company's performance in regards to social and environmental responsibility, and also strong corporate governance. ESG scores are designed to assess a company's total impact on the environment, society, and internal governance. The ESG Score is calculated using a variety of indicators and measures that vary depending on the rating agency or supplier.

Previous research examining the impact of Environmental, Social and Governance (ESG) on company value still does not provide consistent evidence. Environmental, social, and governance (ESG) and firm value have a significant positive relationship, according to research by (Melinda & Wardhani, 2020); (Muhammad Naeem et al., 2021); (Yu & Xiao, 2022); (Kurniawan & Rokhim, 2023); and (Aydoğmuş et al., 2022). However, a study by (Landi & Sciarelli, 2019); (Duque-Grisales & Aguilera-Caracuel, 2021) ; and (Febrianty et al, 2023) showed that environmental, social, and governance (ESG) had a negative impact on firm value. Other studies, however, produced the opposite results.

The audit committee within the ESG (Environmental, Social, and Governance) framework is an important entity in the corporate structure that is responsible for monitoring financial reporting and non-financial factors related to environmental, social and corporate governance aspects. The importance of the audit committee in ESG is not only limited to monitoring, but also as a guardian of the company's reputation. By closely monitoring ESG aspects, they can help prevent potential risks and avoid negative impacts on the company's image. An effective audit committee in an ESG context must have a strong understanding of environmental, social and corporate governance issues. They need to monitor company compliance with environmental and social regulations, as well as ensure that corporate governance is carried out well and in accordance with high standards of ethics and integrity. Apart from monitoring and evaluating financial aspects, audit committees within the ESG framework also examine the company's performance in fulfilling environmental commitments, such as waste management, energy efficiency, or efforts to mitigate environmental impacts. They also pay attention to social issues such as diversity, equality, human rights, and community involvement.

The difference between this study (Samy El-Deeb et al., 2023) research from 2023 is that instead of using firm value as the dependent variable with Price Book Value (PBV) as are proxy that used. The present study aims to investigate the role of audit committee as a moderator of the relationship between ESG and firm value, which is different from the research conducted (Samy El-Deeb et al., 2023). The function of the audit committee will be further evaluated in this study from a number of perspectives, including expertise, tenure, gender, and the number of audit committees.

LITERATURE REVIEW AND HYPOTHESIS TESTING

Legitimacy Theory

Legitimacy Theory is a management and accounting conceptual framework that highlights the need for organizations to maintain "legitimacy" or social credibility in the eyes of the public. Companies are considered legitimate if society feels that the company is behaving ethically and morally. This idea highlights the importance of companies striving to ensure that their operations do not contradict established standards and making efforts to maintain a good public image. There is a difference between the values according to the company and the values that exist in society, therefore the company will feel threatened if this difference occurs (Legitimacy gap) (Shafirah et al., 2022). The legitimacy gap occurs because of a conflict that is not aligned between the company and society due to the insensitivity of the company's activities. In this way, legitimacy theory is able to encourage companies to maintain and strengthen their reputation through Environmental, Social, and Governance (ESG).

An organization demonstrates that it has considered environmental, social, and governance factors as part of its efforts to uphold credibility when it adopts ESG (Environmental, Social, and Governance). Companies that care about ESG factors prioritize environmental consequences, social contributions, and good governance. This enables them to meet the expectations of society and stakeholders towards ESG issues. As a result, ESG disclosures and the procedures that support them become part of companies' efforts to maintain and enhance their social legitimacy. ESG has become an important aspect of maintaining corporate legitimacy in the current economic climate. Companies that actively incorporate ESG principles into their operations can enhance their social credibility and stakeholder trust. Thus, legitimacy theory and ESG work together in companies' efforts to maintain their credibility in the eyes of society and achieve long-term success.

Stakeholder Theory

The idea of "stakeholder theory" acknowledges the significance of the different groups participating in or with an interest in a company's operations. According to this theory, businesses must consider and serve the needs of a variety of stakeholders, including the government, local communities, employees, customers, and the environment, in addition to their own shareholders. R. Edward Freeman first proposed this theory in 1984. According to this view, companies have a moral obligation to consider and meet the needs and interests of every people involved in their operational environment. By paying attention to these stakeholders, companies can build harmonious relationships, increase trust, and support the long-term sustainability of the company, thus creating long-term value for all parties involved.

In order to comprehend the company's operations, stakeholders require disclosures about corporate responsibility and sustainability. For instance, when a company fulfills its obligations to stakeholders regarding environmental, social, or governance matters, both the company's financial performance and firm value increase. When competing in the market, stakeholders believe that firms with higher ESG performance would fare better. Stakeholders will reward these organizations by increasing consumer demand, investor investment, and staff productivity, resulting in higher enterprise value. In this context, the audit committee is also in charge of ensuring that the firm complies with ESG-related norms and legislation and that stakeholders receive accurate and relevant information. The audit committee helps ensure that stakeholders' interests are represented in the company's business practices, which in turn strengthens the legitimacy and trust of the various stakeholders in the company.

Agency Theory

Agency theory is a framework that explains the relationship between owners and managers in a company where there is a conflict of interest. This theory highlights the agency problem among stakeholders that can potentially lead to actions that are not in accordance with the company's objectives. In this context, the audit committee has an essential role in resolving these agency conflicts. The audit committee has an essential role in overseeing the company's operations, ensuring compliance with regulations and standards, and assessing the quality of financial statements for the benefit of shareholders.

Audit committees are viewed as one of the control mechanisms in agency theory that assist in lessening the information asymmetry between shareholders and management. They are in charge of independently examining the internal procedures and financial statements of the business. These functions help ensure that the information submitted by management is an accurate representation of the company's financial performance and position, thus helping to minimize the risk of agency conflicts that may occur.

Environmental, Social and Governance (ESG)

The term "environmental, social, and governance" (ESG) refers to a concept that considers social, corporate governance, and environmental aspects in order to encourage ethical and sustainable business operations. (Tambun, 2021) state that ESG is a framework for investing that consists of three main components: corporate governance, social responsibility, and the environment. With the help of this framework, businesses can better understand and manage the risks related to these three areas, build relationships with stakeholders, and enhance their reputation. The corporation hopes to improve its reputation by disclosing its environmental, social, and corporate governance responsibilities (Safriani & Utomo, 2020).

Hypothesis Development

ESG Score on Firm Value

The acronym ESG stands for environmental, social, and governance, and it encompasses three key areas of assessment that are used to gauge how well a business is doing in terms of social responsibility, sustainable practices, and good governance. The term "ESG Score" is used in ESG disclosure. An evaluation of a company's ESG practices expressed as a numerical number is called an ESG Score.

Numerous factors, including social policies, corporate governance, and environmental practices, are evaluated in order to determine this score. The ESG Score and business value are positively correlated, according to both legitimacy theory and stakeholder theory. Stakeholder theory emphasizes how important it is for companies to consider the interests of parties other than shareholders. Businesses that prioritize governance, social, and environmental issues typically receive more support from a wider range of stakeholders, which can increase firm value. This argument is consistent with the result that organizations with better ESG ratings have higher value because they take into account the interests of many stakeholders and acquire wider support (Srivastava & Anand, 2023). According to Legitimacy Theory, it is critical for businesses to preserve their legitimacy in the eyes of society and stakeholders by matching existing expectations and conventions. Companies that proactively address environmental, social, and governance issues can boost their legitimacy in the eyes of society, which can result in a rise in firm value (Yudhanto & Simamora, 2023).

Overall, a high ESG score is closely related to an increase in firm value. Both theories, Stakeholder Theory and Legitimacy Theory, give a thorough grasp of how organizations that prioritize environmental, social, and governance concerns operate aspects can gain wider support from various stakeholders, which ultimately contributes to an increase in overall firm value. In line with previous research (Melinda & Wardhani, 2020); (Fung & Hsieh, 2004)(Muhammad Naeem et al., 2021); (Yu & Xiao, 2022); (Cho, 2022); (Aydoğmuş et al., 2022); (Aras & Hacioglu Kazak, 2022); and (Srivastava &

Anand, 2023) which reveal that there is a significant positive relationship between ESG Score and Firm Value, the first hypothesis assumed is:

H1: ESG Score has a positive effect on Firm Value

The Audit Committee's Moderating Role in the Relationship among ESG and Firm Value The audit committee is an independent body formed within the company to oversee the audit process, internal control system and financial reports. The main task of this committee is to ensure that the company carries out its operations with a high level of transparency, compliance and integrity. Audit committee members typically consist of individuals who have relevant expertise and knowledge in accounting, finance, law, or related industries.

The audit committee has a function with the task of implementing good mechanisms and governance within the company which is considered capable of maintaining the improvement and integrity of audit quality results (Normasyhuri et al., 2022). The audit committee is responsible as an implementer in ensuring that good corporate governance and mechanisms are implemented properly, which is believed to be able to maintain the improvement and integrity of the quality of audit results. One of the key roles of the audit committee is to oversee the preparation of the company's financial reports. They must ensure that financial reports are prepared correctly, in accordance with applicable accounting principles, and provide an accurate picture of the company's financial condition to stakeholders.

Overall, the audit committee has a very important role in maintaining the company's integrity, transparency and compliance with various industry standards, regulations and best practices. With careful oversight and comprehensive evaluation, audit committees help ensure that the company operates well and is trustworthy for all parties involved.

The study (Fuadah et al., 2022) claims that the relationship among firm value and environmental, social, and governance (ESG) is moderated by the audit committee. Next, the following presumption is made:

H2: Environmental, social, and governance (ESG) disclosure and corporate value are moderated by the audit committee.

METHODS

This research uses quantitative methods that utilize numeric data, and the collected data is analyzed using statistical formulations. This quantitative research is to measure the relationship between variables and help produce strong empirical evidence. The independent variable in this study is ESG with the dependent variable being firm value, and the control variables include firm size, leverage and audit committee as moderating variables.

This research encompasses all corporations listed on the Indonesia Stock Exchange (IDX) between 2018 and 2022 as its study population. Employing purposive sampling, the selection process is based on specific criteria: companies must have disclosed comprehensive financial reports on the Indonesia Stock Exchange, adopted Environmental, Social, and Governance (ESG) practices, and maintained an ESG score throughout the designated observation period.

This study's population consists of firms registered on the Indonesia Stock Exchange between 2017 and 2022. The sampling technique is using purposive sampling provided that the company has published a complete financial report on the Indonesia Stock Exchange and has implemented ESG, and has an ESG score. throughout the specified observation period.

The data processing method in this research uses multiple linear regression using the IBM SPSS Statistics 27 program. To examine and evaluate the link between an independent variable and a dependent variable, multiple linear regression is used. The purpose of this study's multiple linear regression is to determine the impact of ESG on firm value and if the audit committee can mitigate the association between ESG and firm value.

This study was conducted to see how companies that disclose the audit committee for 5 years of observation have a moderating relationship to ESG Score and firm value. The company value in this study uses the Price to Book Value (PBV) proxy as the measuring variable, the independent variable identified in this study is the ESG Score, and the moderating variable used is the audit committee seen from expertise, tenure, total and gender, and uses company size (Size) and Leverage (LEV) as control variables.

Table 1. Descriptive Statistic

Variables		Measurement	Source
Dependent Variable	**Firm Value**	Price to Book Value (PBV) = $\frac{\text{Price per Share}}{\text{Book Value per Share}}$	(Irsyahma & Nikmah 2016)
Independent Variable	**ESG Score**	ESG Score Index	ESGI Dataset
Control Variable	**Size**	Size = LN (T. Assets)	(Eddy Suranta, Fenny Marietza, Pratana Puspa

			Midiastuty, 2014)
	Leverage	Debt to Asset Ratio $= \frac{T.Debt}{T.Assets}$	(Suranta, 2023)
Moderating Variable	**Audit Committee**	Expertise (Proportion of members with education/experience in accounting or finance) Tenure (The average years of board service of audit committee members is calculated by dividing the total number of board years by the number of audit committee members.) Total Audit Committee Gender (The proportion of female audit committee members)	(Al-Matari, 2022)

RESULTS AND DISCUSSIONS

Descriptive Statistic

Table 2. Descriptive Statistics

	Minimum	*Maximum*	*Mean*	*Standard Deviation*
PBV	.127	44.857	3.196	6.351
ESG	15.090	63.250	33.627	10.122
EXP	.200	1.000	.680	.247
TNR	1.000	9.000	3.636	1.766
GDR	.000	1.000	.192	.183
TTL	3.000	7.000	3.36	.712
LEV	.028	2.459	.474	.259
SIZE	29.463	33.655	31.413	.864

Source: Secondary data (2023)

It can be seen in Table 2 that the PBV value ranges from 0.127 to 44.857, with the average

3.196 and standard deviation is 6.351. This shows that the PBV has variabilitas. In the context of independent variables, the table shows an overview of the variability of ESG scores, with the lowest score being 15.090 and the highest score being 63.250. The average value of the ESG score is 33,627 and the standard deviation is 10,122 which shows limited variance, indicating that the observation data used is stable.

Then, the audit committee as a moderating variable has 4 proxies that are used in this research. For the first proxy is Expertise (EXP) value ranging from 0.200 to 1, with an average value of 0.680 and a standard deviation of 0.247 this indicates that EXP does not vary. With an average value of 0.680, this also illustrates that most companies prefer audit committees that have background expertise in accounting and finance. Furthermore, in the tenure audit committee, with a minimum of 1 with a maximum of 9, this can explain that the average audit committee has served for at least one year and a maximum of 9 years on the audit committee. On the next audit committee, namely gender with an average value of 0.192 and a standard deviation of 0.822, this states that the data presented varies greatly. This also explains that on average there are fewer female-gendered audit committees in a company than male-gendered ones. Finally, the proxy used to view the audit committee of a company is the number. Here, at least a company has 3 audit committees and a maximum of 7 audit committees with an average company having 3 audit committees.

Hypothesis Test

First Hypothesis: The Influence of ESG on PBV

Table 3. EGS on PBV

Price to Book Value (Dependent Variable)	Unstandardized B	t	Sig.
(Constant)	12.060	2.758	.000
ESG	-.105	-2.141	.034
LEVERAGE	.789	.533	.594
SIZE	-1.627	-2.657	.009

R^2	Adjusted R Square	F	Sig.
.073	.057	4.363	.000[b]

Source: Secondary data with IBM SPSS Statistisc 27 (2023)

The first hypothesis aims to find out more about the influence of ESG performance on firm value as measured by Price to Book Value (PBV). Table 3 presents the test results that reveal a negative and statistically significant correlation among ESG and firm value. The Price to Book Value (PBV) measure shows a coefficient of -0.105 with a significance value of 0.034 (0.000 < 0.050). This shows that increasing ESG performance contributes negatively to firm value. Several previous studies stated that there is a significant relationship between ESG and company value. Meanwhile, the results of this research are in line with (Maulana et al., 2023)which states that there is no relationship between ESG and company value as measured by the PBV proxy. This is also in line with (Whelan et al., 2021) who found that 8% and 21& of the existing research results show that ESG can have a negative or insignificant effect on firm value.

The negative relationship between ESG performance and firm value can be caused by First, ESG initiatives often require substantial initial investment in sustainable practices, which impacts short-term profitability and assets, thus affecting book value (Maulana et al., 2023). Second, investor perceptions and preferences may also affect the relationship between ESG and P/B ratio. Investor preferences prioritize short-term financial gains over long-term sustainability measures. Some of these investors may prioritize short-term profitability over long-term sustainability, potentially seeing ESG investments as a diversion of resources from immediate financial gains, leading to lower P/B ratios for companies that focus on ESG initiatives. The negative relationship between ESG factors and P/B ratio may stem from the costs required for ESG initiatives to be positively reflected in the company's book value.

Second Hypothesis: Audit Committee moderation of ESG on PBV

Table 4. Audit Committee (Expertise) Moderation

Price to Book Value (Dependent Variable)	**Unstandardized B**	**t**	**Sig.**
(Constant)	18.364	3.128	.002
ESG	-.110	-2.217	.028
EXPERTISE	-1.871	-1.038	.301
LEV	.605	.407	.685
SIZE	-1.705	-2.764	.006

R^2	Adjusted R Square	F	Sig.
.080	.057	3.541	.008[b]

Price to Book Value (Dependent Variable)	**Unstandardized B**	**t**	**Sig.**
(Constant)	18.716	3.173	.002
ESG	-.133	-2.263	.025
EXPERTISE	-2.884	-1.271	.206
ESG X EXP	.035	.737	.462

LEV	.686	.459	.647
SIZE	-1.696	-2.745	.007

R^2	Adjusted R Square	F	Sig.
.083	.054	2.934	.015[b]

Table 5. Audit Committee (Tenure) Moderation

Price to Book Value (Dependent Variable)	Unstandardized B	t	Sig.
(Constant)	17.090	2.916	.004
ESG	-.106	-2.140	.034
TENURE	.068	.296	.767
LEV	.701	.463	.644
SIZE	-1.610	-2.613	.010

R^2	Adjusted R Square	F	Sig.
.074	.051	3.276	.013[b]

Price to Book Value (Dependent Variable)	Unstandardized B	t	Sig.
(Constant)	.200	0.96	.924
ESG	.044	2.693	.008
TENURE	-.141	-1.437	.153
ESG X TNR	.002	.997	.320
LEV	.307	.695	.488
SIZE	-.005	-.027	.979

R^2	Adjusted R Square	F	Sig.
.078	.048	2.627	.026[b]

Table 6. Audit Committee (Gender) Moderation

	Unstandardized	t	Sig.

Price to Book Value (Dependent Variable)	B		
(Constant)	19.902	3.002	.003
ESG	-.088	-1.746	.083
GENDER	-2.911	-1.019	.310
LEV	4.484	1.741	.084
SIZE	-1.642	-2.624	.010

R^2	Adjusted R Square	F	Sig.
.098	.076	4.315	.002[b]

Price to Book Value (Dependent Variable)	Unstandardized B	t	Sig.
(Constant)	18.025	2.858	.005
ESG	-.095	-1.211	.228
GENDER	-2.877	-.825	.411
ESG X GENDER	.011	.143	.887
LEV	1.045	.696	.487
SIZE	-1.514	-2.433	.016

R^2	Adjusted R Square	F	Sig.
.076	.047	2.675	.024[b]

Table 7. Audit Committee (Total Audit Committee) Moderation

Price to Book Value (Dependent Variable)	Unstandardized B	t	Sig.
(Constant)	16.572	2.749	.007
ESG	-.095	-2.047	.042
TOTAL	-.446	-.652	.515
LEV	.889	.608	.544
SIZE	-1.492	-2.297	.023

R^2	Adjusted R Square	F	Sig.
.072	.050	3.205	.015[b]

Price to Book Value (Dependent Variable)	Unstandardized B	t	Sig.
(Constant)	17.520	2.857	.005
ESG	-.042	-.601	.549
TOTAL	-.021	-.027	.979
ESG X TOTAL	.015	-1.026	.307
LEV	.902	.609	.543
SIZE	-1.537	-2.362	.019

R^2	Adjusted R Square	F	Sig.
.078	.050	2.775	.020[b]

Hypothesis 2 aims to test that the audit committee moderates the relationship between ESG performance and firm value. The test results are presented in Table 5,6,7 and 8. The test results show that all of the proxies used for audit committee have insignificant regression. That's mean audit committee can't moderate the relationship between ESG and Firm value. The result of this study's findings diverges from earlier research endeavors that declared the correlation between ESG and firm value effectively moderated by the audit committee. This may occur because external factors such as government regulations, consumer demands, and market changes are often more dominant in influencing the relationship between ESG and firm value than the role of the audit committee (Fuadah et al., 2022). Furthermore, audit committees' ignorance of the critical aspects of ESG and lack of tools to precisely measure the various dimensions of ESG may also limit their ability to moderate this relationship (Mohammad & Wasiuzzaman, 2021). Moreover, different interpretations of ESG importance by stakeholders and the lack of uniformity in ESG reporting practices could be an additional challenge, reducing the effectiveness of audit committees in moderating the linkage between ESG and firm value.

CONCLUSIONS

The goal of this research is to give empirical evidence on the link among environmental, social, and governance (ESG) and firm value as proxied by price to book value (PBV) in firms with the ESG Index and listed on the Indonesia Stock Exchange (IDX) between 2018 and 2022. Furthermore, the goal of this research is to determine if the audit committee (expertise, tenure, gender, and number) can control the relationship between environmental, social, and governance variables and firm value. The findings of this study's hypothesis testing reveal that (1) Environmental, social, and governance (ESG) have a negative influence on company value. This study supports previous research (Maulana et al., 2023), which found that environmental, social, and governance (ESG) factors had a negative impact on firm value. Then, the audit committee which is proxied through Expertise, Tenure, Gender and Number is hence unable to regulate the correlation between environmental, social, and governance (ESG) and firm value.

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