

Can Profitability Moderate the Board of Directors and Audit Committee's on Environmental Disclosure?

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Audit Committee, Board of Directors, Profitability, Environmental Disclosure, and Sustainability Report.

Abstract

This study aims to analyze and obtain empirical evidence regarding the influence of audit committees and boards of directors on environmental disclosure with profitability as a moderating variable. The population consists of companies in the automotive, transportation, and mining sectors listed on the Indonesia Stock Exchange during the period 2021-2024, totaling 111 companies. The sampling method used was purposive sampling, which resulted in 50 companies with a total of 169 units of analysis over four years. WarpPLS 7.0 was used for testing in this study. The results prove that the audit committee has a positive effect on environmental disclosure. The board of directors has no effect on environmental disclosure. Profitability has a significant negative effect in moderating the board of directors on environmental disclosure. The suggestion that can be given is that companies can report environmental disclosure in sustainability reports in more detail and comprehensively based on 32 GRI standards criteria. Further research can add company sectors and other variables outside this research model.

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INTRODUCTION

In an effort to address global challenges in sustainability reporting, the Indonesian Institute of Accountants (IAI) has identified key factors that lead to success in achieving more comprehensive sustainability reporting in Indonesia. One of these key factors is strong regulations from regulators. Ghozali & Chariri (2014), state that the general objective of financial reporting is to provide useful financial information to support economic decision-making. Adequate and accountable disclosure is essential to achieve this objective. Non-financial information is currently gaining widespread public attention. Social and environmental aspects are issues of interest to the wider community. Law number. 40 of 2007 about Limited Liability Companies stipulates that companies conducting business activities in the field of and/or related to natural resources are required to implement social and environmental responsibilities. In addition, financial reports must also include reports on the implementation of social and environmental responsibilities.

Financial Services Authority Regulation Number 51/POJK.03/2017 concerning the implementation of sustainable finance for financial services institutions, issuers, and public companies regulates companies to conduct sustainability reporting. Changes in natural conditions and various impacts of human activities on nature have begun to attract public attention. Recently, the government also released a new regulation, namely the Circular Letter of the Financial Services Authority of the Republic of Indonesia Number 16/SEOJK.04/2021 concerning the form and content of annual reports of issuers or public companies. This regulation requires companies to conduct sustainability reporting that includes economic, social, and environmental aspects starting in 2021.

The Global Reporting Initiative (GRI) is a non-governmental organization that issues regulations for compiling non-financial reports, whether in annual reports, separate reports, or reports on the company's official website, for countries that do not yet have specific regulations on non-financial reports. The GRI sustainability reporting guidelines cover disclosures on economic, environmental, and social aspects. GRI Standards are the latest reference for companies wishing to report on sustainability. GRI Standards contain 32 environmental disclosure items, each of which explains material disclosure, energy, water and effluent, biodiversity, emissions, waste, environmental compliance, and supplier environmental assessment.

The mining industry, which supports the economies of many countries, including Indonesia, finds itself in a paradoxical position. This industry contributes significantly to state revenue, foreign exchange, and employment. However, its operations are synonymous with massive environmental impacts, such as landscape destruction, water and soil pollution from waste, and loss of biodiversity. The Intergovernmental Panel on Climate Change (IPCC) in 2023 found that current global warming is largely caused by human activities, such as the burning of fossil fuels and land use change. The burning of fossil fuels for energy not only increases greenhouse gas emissions but also exacerbates global warming and climate change.

CNBC (2023) revealed that pollution in Jakarta is increasing. This is due to motor vehicle activity. This situation shows that business activities related to the automotive industry have a negative impact on health and the environment. Motor vehicle growth continues to increase by 5.7% per year for motorcycles and 6.38% per year for passenger cars. The biggest contributor to air pollution today is motor vehicles (Kominfo, 2023).

Reducing emissions at the source (motor vehicles) can reduce air pollution, but this can have an impact on the country's economy and pose a risk to the sustainability of the automotive industry. The government continues to strive to reduce air pollution with short-term plans such as conducting motor vehicle emissions tests and encouraging the use of public transportation (Kompas, 2024).

In addition to motor vehicles, aircraft also contribute significantly to air pollution. This phenomenon should make companies engaged in transportation more concerned about the environmental impact of their business activities. Purwantini et al (2019), found that environmental reporting by 35 companies was still quite low, at only around 22.5%. Therefore, this study is important to provide test results that are relevant to current conditions. Given the time difference, different conditions can also be anticipated and accommodated in this study.

Good corporate governance certainly plays an important role in achieving a company's success and is expected to provide supervision and control that can add value to the company (Ariningtika & Kiswara, 2013). Rifandi (2017), states that companies with high profit margins show growth for the future. To meet information needs, it is necessary to disclose information that is relevant to the needs/interests of users, namely the disclosure of sustainability reports. The implementation of good governance certainly depends on an independent board of commissioners, an audit committee, and a board of directors. These factors can influence companies in disclosing environmental reports in sustainability reports.

The audit committee within a company serves as a crucial internal control mechanism, not only verifying data but also emphasizing the importance of environmental accountability to top management, thereby promoting greater transparency as part of a comprehensive corporate governance strategy (Almahrog et al., 2022). Bataineh et al (2023) stating that there is no influence between the audit committee and environmental disclosure, but Tumwebaze et al (2022) and Jibril et al (2024) proving that audit committees have a positive influence on environmental disclosure. This is because audit committees encourage companies to comply with applicable regulations in relation to environmental disclosure.

Research on profitability in relation to environmental disclosure conducted by Nuskiya et al (2021) and Balogh et al (2022) shows that profitability significantly affects environmental disclosure, while Chandok & Singh (2017) & Wichianrak et al (2022) explains that profitability has a negative effect on environmental disclosure. Mohamed Adnan et al (2023) found that profitability does not affect environmental disclosure. Research on institutional ownership and profitability on environmental disclosure shows some differences in results. The inconsistency of these results indicates that the variables of institutional ownership and board of directors deserve further study.

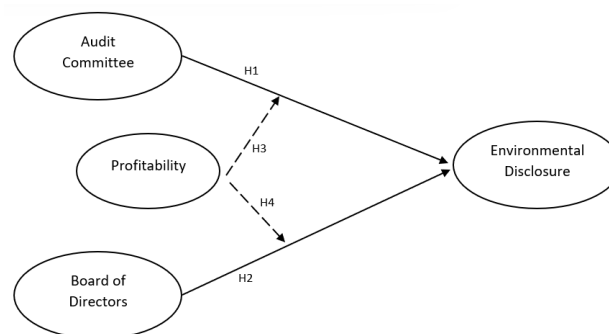
Ghozali & Chariri (2014) explains that theory is a logical reason, but statements of belief, whether in the form of explanations, estimates, or prescriptions, are hypotheses. In this study, the underlying theories are stakeholder theory and legitimacy theory. Freeman et al (2010) explains that stakeholder theory focuses on managers who carry out tasks and have a direct relationship with the company's business practices. The assumption of stakeholder theory is based on the idea that as companies grow, they connect with and attract the attention of the community. Therefore, companies need to demonstrate their accountability and responsibility to the wider community and not just to shareholders. Dowling & Pfeffer (1975) states that the

theory of legitimacy changes perceptions, diverts attention, and alters expectations to reduce external pressure. Legitimacy within a company provides the view that the company continues to strive to ensure that its activities are carried out in accordance with the norms that apply in society (Tumwebaze et al., 2022). Legitimacy can also be described as the trust that society places in a company and something that a company seeks to achieve from society, which will be useful as a potential resource for the company in sustaining its business processes. This theory aims to explain how companies continue to strive to provide assurance in conducting their business activities, integrating with the framework and norms of society in that environment (Pratiwi & Sumaryati, 2014). This concept shows that a company must also respond positively and show concern for the community in order to gain legitimacy from the general public, one way being through environmental disclosure via sustainability reports.

The stakeholder theory perspective explains that companies are not only responsible to shareholders but also to all stakeholders, where the pressure to meet the expectations of these diverse groups requires strong governance mechanisms. Audit committees and boards of directors serve as manifestations of the company's commitment to this accountability. Meanwhile, legitimacy theory emphasizes that companies must continuously strive to obtain, maintain, and improve social legitimacy in order to continue operating. High profitability, in this framework, is not only a measure of economic performance, but also a critical resource and "legitimacy capital". This study was conducted by adding profitability as a moderating variable. Profitability indicates a company's efforts to gain public trust in relation to its activities. Moderating variables are usually introduced when there is an unexpectedly weak or inconsistent relationship between the predictor and the criterion variable (Baron & Kenny, 1986). Using profitability as a moderating variable is expected to strengthen the influence of independent variables on dependent variables in this research model.

RESEARCH FRAMEWORK AND HYPOTHESIS

Figure 1. is a visualization of the conceptual relationship tested in this study. This framework illustrates the hypothesized relationship model, in which the audit committee and board of directors are examined as independent variables that directly influence environmental disclosure. Furthermore, this framework shows the hypothesized role of profitability as a moderating variable, which is expected to strengthen the influence of both governance mechanisms.



Source: Data processed

Figure 1. Research Framework

Bapepam Circular Letter No. SE-03/PM/2000 on audit committees explains that audit committees must create a climate of discipline and control that can reduce the opportunity for irregularities in company management. The audit committee will certainly supervise and provide input to the board of commissioners through meetings or agendas organized by the company. Meetings are held for effective coordination when supervising reports and implementing corporate governance. The frequency of annual audit committee meetings is a measure of its diligence. A higher frequency of meetings puts pressure on managers to provide additional information (Umar et al., 2023). In this context, the audit committee ensures that environmental disclosure is adequate and accountable to meet the information needs of stakeholders. Stakeholder theory can certainly explain how the audit committee relates to environmental disclosure. In carrying out its duties and responsibilities, the audit committee seeks to obtain and maintain social legitimacy. The audit committee encourages environmental disclosure as part of its legitimacy strategy to meet the expectations of stakeholders, including regulators and investors. Companies need to maintain social legitimacy by demonstrating their commitment to the environment. Previous studies reviewing the influence of audit committees on environmental disclosure have been conducted. Arif et al (2020), Maulia & Yanto (2020), Rahmadani et al (2021), Jibril et al (2024), which states that audit committees have a positive influence on environmental disclosure. These explanations and empirical evidence support the notion that audit committees influence environmental disclosure.

H₁: The audit committee influences environmental disclosure.

The board of directors is a membership formed by authorized stakeholders who are responsible for the operational activities of the relevant company. Hasanah et al. (2015) explains that governance is a set of rules that apply within a company and demonstrates the relationship between managers and shareholders. The board of directors is fully responsible for ensuring the long-term sustainability of the company and supervising the management within the company. The board of directors is responsible for balancing the interests of various stakeholders (investors, communities, regulators). Stakeholders naturally want management to report environmental disclosures in accordance with applicable regulations, so the board of directors will make environmental disclosures and fulfill its responsibilities to the company's owners in accordance with stakeholder theory. Research by Giannarakis et al (2020), Jamil et al (2020), Krisyadi & Elleen (2020), Ong & Djajadikerta (2020), Khairreddine et al (2020), Kumari et al (2022), Al-Absy (2024) supports this framework, which proves that the board of directors has a positive influence on environmental disclosure. Based on the explanations and empirical evidence stated above, it can be assumed that the board of directors influences environmental disclosure as described in sustainability reports.

H₂: The board of directors influences environmental disclosure.

Stakeholder theory explains the relationship between audit committees and environmental disclosure in a company. Environmental disclosure is a manifestation of the audit committee's sense of responsibility to shareholders as owners of the company and the wider community in general. Profitability is expected to strengthen the influence of audit committees to consistently enforce a climate of discipline towards regulations and carry out their duties in terms of good reporting through environmental disclosure. Nuskiya et al (2021),

Wahyuningrum et al (2022), Wichianrak et al (2022) found that profitability has a significant effect on environmental disclosure. The results of research conducted by Arif et al (2020), Rahmadani et al (2021) and Jibril et al (2024) also supports this framework because it shows that audit committees have a significant influence on environmental disclosure. Therefore, based on the above explanation and existing empirical evidence, it can be assumed that profitability can strengthen the influence of audit committees on environmental disclosure.

H₃: Profitability strengthens the audit committee's influence on environmental disclosure.

Stakeholder theory can explain how the board of directors relates to stakeholders regarding environmental disclosure. The board of directors is responsible for balancing the interests of various stakeholders (investors, regulators, communities). Good reporting will certainly include environmental disclosure, which is a form of the board of directors responsibility to shareholders as owners of the company and the wider community in general. High-profit companies will certainly encourage stakeholders to demand environmental accountability. In order to comply "OJK Regulation No. 51/POJK.03/2017 concerning the implementation of sustainable finance for financial services institutions, issuers, and public companies and Circular Letter of the Financial Services Authority of the Republic of Indonesia No. 16/SEOJK.04/2021 concerning the form and content of annual reports of issuers or public companies" the board of directors is closely involved in the disclosure of sustainability reports. Research conducted by Monteiro et al. (2021) shows that the board of directors has a significant influence on environmental disclosure. Previous studies that also support this framework are Nuskiya et al (2021), Wichianrak et al (2022), Ahmed et al (2022) which explains that profitability has a significant influence on environmental disclosure. Therefore, based on this explanation and empirical evidence, it can be assumed that profitability can moderate the board of directors' approach to environmental disclosure in sustainability reports.

H₄: Profitability strengthens the board of directors' influence on environmental disclosure.

METHOD

This study limits its research subjects to automotive, transportation, and mining companies listed on the Indonesia Stock Exchange from 2021 to 2024. Based on the number of variables or factors that may influence environmental disclosure, this study focuses on the audit committee and board of directors as independent variables. The operationalization of the dependent variables, namely environmental disclosure, was measured using content analysis based on the number of indicators from the Global Reporting Initiative (GRI) Standards disclosed by the company. The independent variables, audit committee and board of directors, were proxied using the number of meetings held by the audit committee and the number of board of directors meetings in one year of the reporting period. Meanwhile, the profitability variable is proxied by Return on Assets (ROA), which is calculated from net income divided by total assets. Profitability in this study is used as a moderating variable. The sample selection was conducted by selecting companies that presented this data. This study also adds another factor as a moderating variable, namely profitability. The addition of a moderating variable is expected to have a significant impact on this study. The research model, company

sector, and actual year of research certainly provide different results, making it more relevant to current conditions and useful for adding knowledge about the influence of variables in the research model on environmental disclosure as described in sustainability reports. The measurement of the research variables used is described in Table 1. The data analysis technique used for this research model is PLS regression analysis with moderating variables using the WarpPLS 7.0 application.

Table 1. Variable Measurements

Variable	Measurements	Source
Environmental Disclosure	$\sum$ Items disclosed in accordance with GRI Standards/Number of environmental items must be disclosed	Nuskiya et al (2021)
Audit Committee	$\sum$ Audit committee meetings within one year	Jibril et al (2024)
Board of Directors	$\sum$ Board of directors meeting within one year	Liu et al (2023)
Profitabilitas	ROA = Net profit/ total assets	Wichianrak et al (2022)

Source: Data processed (2025)

The significance level used is 5%. Linearity testing was conducted to determine the algorithm used in the inner model of the WarpPLS 7.0 software. Meanwhile, the algorithm used in the outer model of the WarpPLS 7.0 software was determined based on the algorithm capable of producing the lowest p-value compared to other algorithms. Because the measurement model is formative, the evaluation of the measurement model (outer model) used weight significance testing and multicollinearity testing. Meanwhile, the structural model (inner model) evaluation uses the predictive relevance (Q^2) test and coefficient of determination (R^2) test. Model fit and quality indices tests are also conducted before hypothesis testing.

RESULT AND DISCUSSION

The evaluation of the measurement model/outer model shows that the significance value of the weight has p-value of $0.001 < 0.05$, and the multicollinearity test shows a VIF value of $0.000 < 2.5$, so the construct measurement is declared feasible. Evaluation of the structural model/inner model shows a predictive relevance (Q^2) value of $0.258 > 0$, so this research model has good predictive validity. The results of the coefficient of determination (R^2) test show a value of 0.304, which means that the dependent variable can be explained by the independent variable by 30.4%.

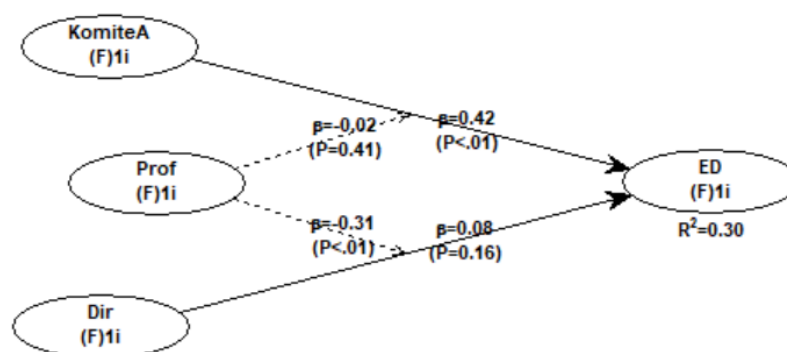
Table 2. Model fit and quality indices

Indicator	Value	Requirements	Conclusion
Average Path Coefficient (APC)	0.207; $P = 0.001$	$P < 0.05$	Accepted
Average R-squared (ARS)	0.304; $P < 0.001$	$P < 0.05$	Accepted

<i>Average full collinearity VIF</i> (AFVIF)	2.489	Accepted if ≤ 5 , ideally ≤ 3.3	Ideal
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Source: Data processed, WarpPLS 7.0

Based on the test results shown in Table 2, the results indicate that an APC value of $0.001 < 0.05$ and an ARS value of $< 0.001 < 0.05$, as well as an AFVIF value of $2.489 \leq 3.3$, which means that the research model is ideal.



Source: Data processed, WarpPLS 7.0

Figure 2. Valid Model

The results of statistical analysis show that audit committees have a positive and significant influence on environmental disclosure, as indicated by a beta coefficient value of 0.42 and a p-value < 0.01 . These findings indicate that any increase in the effectiveness of audit committees in creating a climate of discipline will be followed by an increase in the quality and quantity of corporate environmental disclosure. From a stakeholder theory perspective, these results are consistent with the argument that companies form strong audit committees in response to pressure and expectations from various stakeholders, including investors, regulators, and communities, who are increasingly concerned about environmental performance. Environmental disclosure serves as a mechanism to meet their demands and build harmonious relationships. Legitimacy theory also explains this relationship, namely that broader environmental disclosure, facilitated by the audit committee, is a strategic strategy for companies to obtain, maintain, or restore their social legitimacy. Companies seek to show the public that they operate responsibly and in accordance with prevailing social norms, thereby ensuring their long-term operational sustainability. The results of this study are in line with Arif et al (2020), Maulia & Yanto (2020), Rahmadani et al (2021), Jibril et al (2024) which states that audit committees have a positive influence on environmental disclosure.

The results of the analysis showing that the board of directors does not have a significant effect on environmental disclosure ($\beta = 0.08$; p-value = $0.16 > 0.05$) are an interesting finding, especially in a context where environmental disclosure has become a regulatory requirement. From a stakeholder theory perspective, this finding indicates that the board of directors does not significantly influence environmental disclosure. The board of directors views compliance with environmental regulations as a cost of compliance, rather than a

strategic opportunity to build relationships with stakeholders. As a result, its decisions are minimalist, only fulfilling what is required by law without any additional initiatives that can be influenced by the board of directors. Meanwhile, legitimacy theory explains that with the existence of coercive regulations, environmental disclosure has shifted from being a “strategic choice” to gain legitimacy to “a license to operate.” In this situation, companies feel that their legitimacy is sufficient simply by complying with the rules, so that the board of directors is no longer reflected in environmental disclosure practices. The finding that the intensity of board meetings, measured by the number of meetings in a year, has no significant effect on environmental disclosure indicates that the quantity of meetings does not necessarily translate into quality oversight and strategic commitment to environmental issues. This may be because board meetings are still dominated by discussions of financial and short-term strategic issues, thereby sidelining in-depth discussions on environmental responsibility and sustainability. The results of the study are in line with Umar et al (2023) which states that the board of directors has no influence on environmental disclosure.

The results show that profitability cannot moderate the influence of the audit committee on environmental disclosure ($\beta = -0.02$; $p\text{-value} = 0.41 > 0.05$), indicating that the level of profitability neither strengthens nor weakens the role of the audit committee in promoting environmental disclosure. Reviewed from stakeholder theory, this finding confirms that the audit committee's commitment to meeting stakeholder expectations through environmental disclosure is principled and inherent in good governance, rather than a function of the company's short-term financial capabilities. The audit committee, measured by the intensity of its meetings throughout the year, has consistently performed its supervisory role, with the high frequency of meetings reflecting a commitment to ensuring corporate accountability, including in terms of environmental disclosure. In this case, the performance of the audit committee does not depend on the company's high profits, as its duties are driven more by regulatory obligations and professional integrity than by the availability of financial resources. The pressure for legitimacy from stakeholders to be environmentally responsible has been internalized as a governance obligation, regardless of profitability conditions (Li et al., 2023). Therefore, the effectiveness of audit committees in promoting consistent implementation of this practice, whereby even companies with low profitability feel obliged to disclose their environmental performance to avoid the threat of delegitimization, means that profitability variation is no longer a significant moderating factor in this relationship. The results of the study are supported by Mohamed Adnan et al (2023) which states that profitability does not affect environmental disclosure.

The results show that profitability significantly weakens the influence of the board of directors on environmental disclosure, as indicated by an interaction coefficient value of -0.313 with a $p\text{-value} < 0.001$. This finding reveals that in companies with high profitability, there is actually a decline in the contribution of the board of directors in promoting environmental transparency. This study used a sample of companies whose business activities have an impact on environmental damage. The higher the company's profit, more reluctant the board of directors is to disclose environmental information because it interprets the impact of environmental damage as being greater. From a stakeholder theory perspective, this condition can also be explained through the phenomenon of managerial opportunism, whereby when financial performance is strong, management and the board feel that they have met the main expectations of stakeholders (i.e.,

shareholders) and therefore allocate less attention and resources to meeting the demands of other stakeholders, including the community and environmentalists (Helfaya & Moussa, 2017). The legitimacy theory in this study explains that highly profitable companies will rely on “profitability” legitimacy derived from their financial success. They feel that no longer need to strengthen their legitimacy through substantial environmental disclosure, because their legitimacy is already considered sufficient by their ability to generate profits (profit-legitimacy trade-off). This study is in line with the findings Cho & Patten (2007) whereas the boards of directors of highly profitable companies tend to adopt a symbolic or minimalist approach to environmental disclosure, because they believe that financial success is a strong enough shield against social pressure.

CONCLUSION

Based on the results and discussion of the study, it can be concluded that the audit committee has a significant positive effect on environmental disclosure. The board of directors has no significant effect on environmental disclosure. Profitability is unable to moderate the audit committee's effect on environmental disclosure, but profitability is able to moderate the board of directors' effect on environmental disclosure in a significantly negative manner. The existence of regulations requiring the establishment of audit committees has proven effective in promoting environmental accountability. However, the insignificant role of the board of directors, which can be further weakened by profitability, indicates a narrow compliance mindset, whereby the board of directors may view environmental disclosure as merely a cost burden rather than a strategic investment in corporate legitimacy.

The findings of this study are limited to environmental disclosures made by companies in the automotive, transportation, and mining sectors listed on the Indonesia Stock Exchange (IDX) during 2021-2024, so that further research can expand the sector. The measurement of this study is also limited to the variables of audit committee, board of directors, and profitability, so that further research can add other variables outside this research model.

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