International Journal of Sciences: Basic and Applied Research (IJSBAR)

ISSN 2307-4531
(Print & Online)

http://gssrr.org/index.php?journal=JournalOfBasicAndApplied

Intervention of Sustainability Report Disclosure toward the Effect of Good Corporate Governance on Financial Performance

Ni Nyoman Meita Jayantini[a]*, I Ketut Sujana[b]

[a,b]Department of Accounting Udayana University, Denpasar, Indonesia
[a]Email: meita94@yahoo.com

Abstract

This study aims to examine intervention of sustainability report disclosure toward the effect of good corporate governance on company's financial performance. The company's financial performance is well illustrated with a high level of profit achievement. By implementing good corporate governance, the company's financial performance will tend to increase. The company also needs to disclose the sustainability report. Sustainability report disclosure is a logical consequence of the implementation principles of Good Corporate Governance (GCG). The GCG in this study was measured by the size of the board of commissioners, the proportion of independent commissioners, and size of the audit committee; sustainability report disclosure was measured by SRDI; and financial performance was measured by the ratio of net profit margin. The population of this study was mining companies listed on the Indonesia Stock Exchange during the period 2013-2016. The sample determination method uses purposive sampling. The analysis technique used is path analysis. The results of this study indicate that the size of the board of commissioners has no effect on sustainability report disclosure and the company's financial performance, the proportion of independent commissioners and the size of the audit committee has a positive effect on sustainability report disclosure and the company's financial performance. Sustainability report disclosure does not mediate the effect of the size of the board of commissioners on the company's financial performance, but sustainability report disclosure mediates the effect of the proportion of independent commissioners and the size of audit committee on the company's financial performance.

Keywords: Size of the Board of Commissioners; Proportion of Independent Commissioners; Size of the Audit Committee; Sustainability Report; Company's Financial Performance.

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* Corresponding author.

1. Introduction

Financial performance is performance achievement that has been achieved by a company and contained in the company's financial report. The company's financial performance is used as a benchmark that can describe the condition of a company. In addition, financial performance can also show the efficiency and effectiveness of a company in achieving its objectives. The company's financial performance is well illustrated with a high level of profit achievement, so that it can attract investors to invest in the company. But before investors buy shares offered by the company, investors will first evaluate the company's financial performance in order to find out whether the company is good or not. Therefore, the company must strive to continuously improve its performance. The important objective of the establishment of a company is to improve the welfare of its owners and shareholders and maximize shareholder wealth through improving the performance of the company [1], so as to achieve these objectives shareholders submit the company's management tasks to professionals or managers. The shareholders (principals) hand over the management of their company to the manager (agent), thus causing a separation between the management of the company and ownership, and ultimately can cause different interests from both parties (principal and agent). The manager's job is to manage the company, so that managers will be more aware of internal information and company prospects than shareholders. Managers may not take the best actions for the interests of the owner because of differences in interests, so that they can trigger conflicts of interest between the agent and the principal [2]. Conflicts of interest between managers and shareholders can be minimized by implementing good corporate governance (GCG). In Indonesia, public companies are required to implement GCG, but in fact there are still companies that commit violations. One of the violations carried out by companies in Indonesia is the mining company PT Bumi Resources Tbk. Indonesia Corruption Watch (ICW) reported that PT Bumi Resources Tbk manipulated sales reports to the Directorate General of Taxes. ICW suspects that PT Bumi Resources Tbk has engineered reporting since 2003-2008, causing a state loss of US $ 620.49 million. This phenomenon indicates that corporate governance is still weak, so that the management of the company is less transparent and less professional. Weak corporate governance can cause the company's financial performance to decline, due to the decline in investor confidence in the company. As a result of the violations committed, the shares of PT Bumi Resources Tbk decreased in 2012 by 72.55% from Rp 2,150 on 30 December, 2011 to Rp 590 on 30 November, 2012, indicating that investor's credibility in PT Bumi Resources Tbk decreased. According to [3] states that companies that implement GCG, their performance will tend to increase. If the company implements good corporate governance, then this can minimize the opportunities for managers to take deviant actions (seeking profit for personal gain), so that decisions that harm the company will decrease and will ultimately improve the company's financial performance. Research on the effect of GCG on the company's financial performance has been done before, but the results of the study were still inconsistent, so this study was conducted to reexamine the effect of good corporate governance proxied by the size of the board of commissioners, the size of independent commissioners, and the size of audit committee on company's financial performance, by intensifying sustainability report disclosure as a mediating variable. Sustainability report disclosure is a logical consequence of the implementation of GCG principles. One of the principles of GCG states that companies need to pay attention to the interests of their stakeholders in accordance with existing rules and establish active cooperation with stakeholders for the long-term survival of the company [4]. The Sustainability report has several functions, such as; for the company, it functions as a measure of the achievement of work targets in the triple bottom line issue, while for investors, it serves as a means of control over the achievement of corporate performance as well as a medium for investors consideration in allocating financial resources, and for other stakeholders (media, government, consumers, academics and others) sustainability report serves as a benchmark to assess the company's commitment to sustainable development [5].

2. Theoretical review

Agency Theory. According to [6] agency relations will arise when there is delegation of authority by shareholders as the owner of the company to management. The agency relationship has the potential to cause a conflict of interest between the two parties, namely the shareholders (as principals) and management (as agents). This conflict of interest can occur because of the differences in the goals and interests of each party towards the company. According to [7], stated one way to minimize agency problems, namely Good Corporate Governance (GCG). GCG is used as a form of monitoring the company to minimize agency problems that occur between agents and principals, because if without adequate supervision and control by the company it will make the manager has the opportunity to take actions that only benefit himself without regard to the interests of the company owner.

Stakeholder Theory. Theory that describes to which company is responsible [8]. This theory assumes that the sustainability of a company cannot be separated from the role of stakeholders. The company cannot live without the support of stakeholders. Stakeholder theory states that all stakeholders have the right to obtain information about company activities that can influence their decision making. Companies must pay attention to stakeholders, because stakeholders can also influence the company. If the company ignores the stakeholders, then the company can reap protests and can eliminate the legitimacy of stakeholders, as a result the company is difficult to maintain its existence in competition with other companies.

Legitimacy Theory. Legitimacy theory is a theory that illustrates that a company will ensure that the company's operations run within the limits and norms that apply to society. The company needs to ensure that the operations carried out by the company are legal in the eyes of the community so that the company's operations can continue. This theory is often used by researchers to be able to examine the extent to which the implementation of corporate social and environmental responsibility is carried out in Indonesia. [9] Stated that the underlies of legitimacy theory is a social contract that occurs between a company and a community where the company operates and uses economic resources. A social contract is an expectation that the community has about the way the company runs its operations.

Good Corporate Governance (GCG). Good Corporate Governance (GCG) is a principle that is needed by the company to bridge the interests between agents and principals, so that corporate objectives can be achieved [7]. GCG is also a concept that takes into account the way the company is managed and run, including the relationships between organs in a company and the accountability between company managers and shareholders and other stakeholders. The board of commissioners, independent commissioners and audit committee are the oversight mechanism of GCG. According to [10] the board of commissioners is one of the company's organs that plays an important role in the company, especially in the implementation of GCG. The board of commissioners control the board of directors in carrying out their duties as best as possible for the benefit of the company and shareholders, ensuring the company always discloses its social responsibility in the sustainability report, and monitors the effectiveness of the GCG implementation carried out by the company. Independent commissioners are members of the board of commissioners who are appointed based on a GMS decision from an unaffiliated party with the main shareholders, members of the board of directors and or other members of the board of commissioners. According to [11], the audit committee is an additional organ needed in the implementation of the GCG principles. The audit committee is formed by the board of commissioners to conduct an examination or research deemed necessary to the implementation of the function of the board of directors in carrying out the management of the company and carrying out important tasks related to the financial reporting system. The audit committee is very important to be owned by the company to support the success of the board of commissioners.

Sustainability Report. [12] Stated that defines sustainability report as a report that contains information not only about financial performance, but also non financial information which consists of information on social and environmental activities that allow companies to grow sustainably. Sustainability report will be one of the media to describe the report of economic, environmental and social impact reporting.

Financial Performance Financial performance is an achievement achieved by the company and reflects the health conditions of the company within a certain period of time. So it can be said that financial performance is a measure of a company's performance achievement. With a clear performance measure, this can be used as a reference for making decisions by stakeholders based on company information. Financial performance is analyzed with financial analysis tools so that it can be known the good and bad financial condition and financial performance of a company within a certain time [13]. Net Profit Margin (NPM) is a profitability ratio that describes the company's ability to generate profits derived from the results of its operational activities. According to [14] NPM is net income divided by net sales. This ratio describes the amount of net income earned by the company at each sale made.

3. Research Hypothesis

3.1 The Effect of GCG on the Company's Financial Performance

H_{1a}: The size of the board of commissioners has a positive effect on the company's financial performance

H_{1b}: The proportion of independent commissioners has a positive effect on the company's financial performance

H_{1c}: The size of the audit committee has a positive effect on the company's financial performance

3.2 The Effect of GCG on Sustainability Report Disclosures

H_{2a}: The size of the board of commissioners has a positive effect on the sustainability report disclosure

H_{2b}: The proportion of independent commissioners has a positive effect on the sustainability report disclosure

H_{2c}: The size of the audit committee has a positive effect on the sustainability report disclosure.

3.3 The Effect of Sustainability Report Disclosures on Company's Financial Performance

H_3: Sustainability report disclosure has a positive effect on the company's financial performance.

3.4 Sustainability Report Disclosures Mediating the Effect of GCG on the Company's Financial Performance

H_{4a}: Sustainability report disclosure mediates the effect of the size of the board of commissioners on the company's financial performance

H_{4b}: Sustainability report disclosure mediates the effect of proportion of independent commissioner on the company's financial performance

H_{4c}: Sustainability report disclosure mediates the effect of the size of audit committee on the company's financial performance

4. Research methods

The population of this study was mining sector companies listed on the Stock Exchange during the period 2013-2016 totaling 43 companies, including coal sub sector, oil and gas sub-sector, other metals and minerals sub sector, and rock stone sub sector.

The sample was determined by purposive sampling method.

This study used secondary data in the form of annual reports, financial reports, and sustainability reports obtained through the Indonesia Stock Exchange and company websites.

This study consisted of 3 types of variables, namely; independent variables, dependent variables, and mediating variables.

Good corporate governance is an independent variable, proxied by the size of the board of commissioners [15], the proportion of independent commissioners [15], the size of the audit committee [16].

Financial performance is a dependent variable, proxied by the ratio of net profit margin. Sustainability report disclosure is a mediating variable, proxied by the sustainability report disclosure index [17].

5. Result and discussions

Testing data in this study used path analysis techniques. The results of the analysis of substructural 1 equation analysis (sustainability report disclosure as the dependent variable) are presented in table 1.

Table 1: Test Results of Substructural Equation Analysis 1

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	T	Sig.
1 (Constant)	0,508	0,090		5,610	0,000
Size of the Board of Commissioners (X_1)	0,002	0,006	0,019	0,261	0,796
Proportion of Independent Commissioners (X_2)	1,193	0,303	0,405	3,931	0,001
Size of the Audit Committee (X_3)	0,111	0,020	0,596	5,607	0,000

From table 1 above can be arranged substructure 1 equation as follows:

$Z = b1X_1 + b2X_2 + b3X_3 + e1$, $Z = 0.002X_1 + 1{,}193X_2 + 0{,}111X_3 + e1$

The results of the analysis of substructural equation analysis 2 (disclosure of financial performance as the dependent variable) are presented in table 2.

Table 2: Results of Testing of Substructural Equation Analysis 2

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	T	Sig.
1 (Constant)	-0,352	0,036		-9,922	0,000
Size of the Board of Commissioners (X_1)	0,002	0,002	0,048	0,936	0,358
Proportion of Independent Commissioners (X_2)	0,235	0,102	0,211	2,304	0,029
Size of the Audit Committee (X_3)	0,020	0,008	0,285	2,584	0,016
Sustainability Report Disclosure (Z)	0,202	0,051	0,535	3,971	0,000

From table 2 above can be arranged substructural equation 2 as follows:

$Y = b4X_1 + b5X_2 + b6X_3 + b7Z + e1$, $Y = 0.002X_1 + 0.235X_2 + 0.020X_3 + 0.202Z + e1$

The amount of direct effect and indirect effect between variables is presented in Table 3 below.

Table 3: Results of Direct Effect and Indirect Effect

Variable Effect	Direct Effect	Indirect Effect (through Sustainability Report Disclosures)
$X_1 \rightarrow Y$	-	-
$X_2 \rightarrow Y$	$P_4 = 0{,}211$	$P_3 \times P_7 = 0{,}217$
$X_3 \rightarrow Y$	$P_6 = 0{,}285$	$P_5 \times P_7 = 0{,}315$

5.1 Effect of Good Corporate Governance on Corporate Financial Performance

a) Effect of the Size of the Board of Commissioners on the Company's Financial Performance

Table 2 shows the significance value of the size of the board commissioners variable of 0.358 (0.358> 0.05) which means that H_{1a} is rejected. This means that the board size of commissioners has no effect on the company's financial performance. It is because the board of commissioners has not been effective in carrying out their duties, so they have not been able to uphold GCG within the company. Therefore, more and more personnel who become commissioners do not affect the company's financial performance. The results of this study are in line with the results of research from Tertius and Christiawan [18], Widiawati [19], Yulianingtyas and Andayani [20], Lukas and Basuki [21]. The results of this study do not support agency theory which explains that the board of commissioners is considered the highest internal control mechanism that plays an important role in monitoring and supervising management. If the function of the board of commissioners has been effective then the supervision system will be better, and ultimately can improve financial performance. Vice versa, if the function of the board of commissioners has not run effectively, the supervision system will be less than optimal, so it will not affect the company's performance.

b) Effect of the Proportion of Independent Commissioners on Corporate Financial Performance

Table 2 shows the significance value of the proportion of independent commissioners variable is 0.029 (0.029 < 0.05) which means that H_{1b} is accepted. This means that the proportion of independent commissioners has a positive effect on the company's financial performance. The existence of an independent commissioner will improve the quality of the supervisory function in the company, because independent commissioners come from outside the company and are not affiliated with the company. The greater the proportion of independent commissioners, the supervision of company management will increase, so that at the end it will have an impact on the company's increased financial performance. Independent commissioners can act as mediators in disputes between internal managers and control management policies and also provide advice to management [22]. The results of this study are in line with the results of research by [23], Widiawati [19]. The results of this study support the agency theory which explains that conflicts of interest between agents and principals can be reduced by proper supervision, namely the presence of independent commissioners will improve the quality of the supervisory function in the company.

c) Effect of the Size of Audit Committee on Corporate Financial Performance

Table 2 shows the significance value of the audit committee size variable is 0.016 (0.016 < 0.05) which means that H_{1c} is accepted. This means that the size of the audit committee has a positive effect on the company's financial performance. The audit committee functions to control the accounting process, so that the greater size of the audit committee, the level of supervision increases. If the level of supervision is increasing, then the manager will manage the company objectively, so that it will ultimately have an impact on the company's increased financial performance. The results of this study are in line with the results of research from Mulyasari and his colleagues [24], Yulianingtyas and Andayani [20], Anderson and his colleagues [25], Awan and Jamali [26].

5.2 The Effect of Good Corporate Governance on Sustainability Report Disclosures

a) Effect of the Size of Board of Commissioners on Sustainability Report Disclosures

Table 1 shows the significance value of the board size commissioners variable of 0.796 (0.796 > 0.05) which means that H_{2a} is rejected. It means that the size of the board of commissioners has no effect on the sustainability report disclosure. It is because the board of commissioners has not done its job well in monitoring and directing the management of the company, so that the more number of members of the board of commissioners in a company does not affect the disclosure of sustainability report. The results of this study are in line with the results of research conducted by Aziz [4], Aliniar and Wahyuni [27], Sukasih and Sugiyanto [28], which state that the size of the board of commissioners does not affect the sustainability report disclosure. The results of this study do not support agency theory which explains that the board of commissioners is considered the highest internal control mechanism. The board of commissioners is a supervisory mechanism of GCG that functions to monitor, provide direction, and guidance to the manager. The board of commissioners can provide strong enough influence to pressure management to disclose information about the performance of the economic, social and environmental aspects of the sustainability report. If the board of commissioners has not carried out their duties properly in monitoring and directing company managers, the greater size of the board of commissioners in a company does not affect the disclosure of sustainability reports.

b) Effect of the Proportion of Independent Commissioner on Sustainability Report Disclosures

Table 1 shows the significance value of the proportion of independent commissioners variable of 0.001 (0.001 < 0.05) which means that H_{2b} is received. This means that the proportion of independent commissioners has a positive effect on the sustainability report disclosure. The greater the proportion of independent commissioners, it will increase the level of supervision of managers in reporting information on economic, social and environmental aspects. So that, the information disclosed by companies in sustainability reports is increasingly widespread. The results of this study are in line with the results of research conducted by Djazilah and Kurnia [29], Aliniar and Wahyuni [27], Nurkhin [30], Makhdalena and his colleagues [31], Haniffa and Cooke [32]. The results of this study support the agency theory which explains that independent commissioners are the highest supervisory component in the company that can improve the supervisory function and disclosure of sustainability reports. The existence of independent commissioners is expected to be able to neutralize all policies and decisions made by the directors, so that decisions and policies can be objective, including the decision to disclose sustainability reports.

c) Effect of the Size of Audit Committee on Sustainability Report Disclosures

Table 2 shows the significance value of the variable the size of audit committee of 0,000 (0,000 <0,05) which means that H_{2c} is received. This means that the size of the audit committee has a positive effect on the sustainability report disclosure. The more audit committees the company has, the more effective the role of the audit committee in controlling and monitoring management. This has resulted in information that is disclosed by the company in the sustainability report. The results of this study are in line with the results of research from

Aniktia and Khafid [33], Siregar and Priantinah [34], Makhdalena and his colleagues [31]. Agency theory states that the audit committee has a role in overseeing and ensuring that the sustainability report's implementation and disclosure are going well [35]. Reference [36] States that if the audit committee's supervision is effective, then the level of disclosure including sustainability report disclosure can increase, and agency problems can also be minimized, so that information related to the social values required by investors can be fully disclosed.

5.3 Effect of Sustainability Report Disclosures on Company's Financial Performance

Table 2 shows the significance value of sustainability report disclosure variables of 0,000 (0,000 <0,05) which means that H_3 is accepted. This means that sustainability report disclosure has a positive effect on the company's financial performance. The broader information disclosed by the company in the sustainability report, the more support provided by stakeholders, because stakeholders believe that the company has been managed well and finally the company's financial performance has also increased. The results of this study are also in line with the results of research from Rizal and his colleagues [37], and Luthan and his colleagues [38], Lin and Amin [39], Amacha and Dastane [40], Dewi and Sudana [41], Apriyanti and Budiasih [42] which state that sustainability report disclosures have a positive effect on the company's financial performance. The results of this study support the legitimacy theory which explains that sustainability report disclosure can have a positive image impact on the company, so that the investors, the public, and other stakeholders will believe that the company has operated according to the prevailing frame or norm in the community, which resulting an increase in financial performance company. In addition, the results of this study also support stakeholder theory which explains that all stakeholders have the right to obtain information about company activities (including covering economic, social and environmental aspects) that can influence their decision making. When the company has disclosed information about economic, social and environmental aspects in the sustainability report, it can increase the support of stakeholders to the company and also improve the company's reputation, so that it can ultimately improve the company's financial performance.

5.4 Sustainability Report Disclosure Mediates the Effect of Good Corporate Governance on the Company's Financial Performance

a) Sustainability Report Disclosure Mediates the Effect of the Size of the Board of Commissioners on the Company's Financial Performance.

The results of statistical tests in Table 1 show the significance value of the size of commissioners board variable of 0.796 (0.796> 0.05) which means the size of board of commissioners variable does not affect the sustainability report disclosure (H_{2a} rejected). Statistical test results in Table 2 show the significance value of the size of board of commissioners variable is 0.358 (0.358 > 0.05), which means the size of board of commissioners variable does not affect the company's financial performance (H_{1a} rejected). This means that the sustainability report disclosure does not mediate the influence of the size of the board of commissioners on the company's financial performance (H_{4a} is rejected). In this study sustainability report disclosure does not mediate the influence of the size of the board of commissioners on the company's financial performance, because the size of the board of commissioners does not affect the disclosure of sustainability reports directly.

b) Sustainability Report Disclosures Mediate the Effect of the Proportion of Independent Commissioners on Company's Financial Performance

Table 3 shows the path coefficient value of the direct effect of the proportion of independent commissioners on the company's financial performance of 0.211 and the indirect coefficient of effect of the proportion of independent commissioners on the company's financial performance through sustainability report disclosure of 0.217. This shows that the indirect effect has a greater effect (P4 < P3xP7), so H_{4b} is received. If the independent variable directly affects the dependent variable, the independent variable also affects the mediating variable, and then the mediating variable also affects the dependent variable, then this condition is called partial mediation. This means that sustainability report disclosure mediates the effect of the proportion of independent commissioners on the company's financial performance. Agency theory which explains that an independent commissioner is the highest supervisory component in a company that can improve the supervisory function and disclosure of sustainability reports. If the information disclosed in the sustainability report by the company is wider, the company's financial performance will increase.

c) Sustainability Report Disclosure Mediates the Effect of the Size of Audit Committee on the Company's Financial Performance

Table 3 shows the path coefficient value of the direct effect of the audit committee's size on the company's financial performance of 0.285 and the indirect coefficient of effect of the audit committee's size on the company's financial performance through sustainability report disclosure of 0.315. This shows that the indirect effect has a greater effect (P6 < P5xP7), so H_{4c} is accepted. If the independent variable directly affects the dependent variable, the independent variable also affects the mediating variable, and then the mediating variable also affects the dependent variable, then this condition is called partial mediation. This means that sustainability report disclosure mediates the effect of the size of audit committee on the company's financial performance. The more audit committees the company has, the more effective the role of the audit committee in controlling and monitoring management. This has resulted in information that is disclosed by the company in the sustainability report. If the information disclosed in the sustainability report by the company is wider, the company's financial performance will increase. The stakeholders will believe that the company has been managed well because the company has been paying attention to economic, social and environmental issues that are disclosed in the sustainability report, and ultimately the company's financial performance has increased.

6. Conclusion and recommendation

Based on the results of testing and discussion, it can be concluded that: (1) The size of the board of commissioners does not affect the company's financial performance, (2) The proportion of independent commissioners has a positive effect on the company's financial performance, (3) The size of the audit committee has a positive effect on the company's financial performance , (4) The size of the board of commissioners does not affect on the sustainability report disclosure, (5) The proportion of independent commissioners has a positive effect on the sustainability report disclosure, (6) The size of the audit committee has a positive effect on sustainability report disclosure, (7) Sustainability report disclosure has a positive effect on company's financial performance, (8) Sustainability report disclosure does not mediate the effect of the size of the board of commissioners on the company's financial performance, (9) Sustainability report disclosure mediates the effect of the proportion of independent commissioners on the company's financial performance, (10) Sustainability report disclosure mediates the effect of the size of audit committee of the company's financial performance.Based on the conclusions of the study, the suggestions that can be submitted are as follows: (1) For the company, in appointing the board of commissioners should be carried out effectively, not only for regulatory compliance, so as not to be able to uphold GCG within the company, this can lead to the supervisory function is not effective, (2) Investors, before making investments in addition to paying attention to the company's financial performance, should pay attention to the company's sustainability report disclosures as well. If the company has revealed sustainability reports it means that the company has paid attention to social performance and environmental performance. Financial performance without being supported by social and environmental performance will not guarantee the sustainability and existence of a company.

7. Limitations

The limitations of this study are the sample of this study. It is still relatively small because only few companies that publish their sustainability reports. Therefore, it is suggested for other researchers who will conduct further research can increase the number of research samples. Because based on the rules of the Financial Services Authority No. 51 /POJK 03/2017 in article 10 paragraph 6 states that in 2019 sustainability report must be reported.

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