
THE EFFECT OF ENVIRONMENTAL AND SOCIAL PERFORMANCE ON EARNINGS MANAGEMENT IN THE SRI-KEHATI INDEX



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Abstract

The rapid development of the business world encourages business actors to carry out various strategies, including earnings management, to present good financial reports. Earnings management is a strategy to show positive financial information that contradicts actual conditions. On this basis, companies carry out earnings management to achieve the company's profit target in the future. This study is focused on proving the effect of environmental and social performance on earnings management with the population used, namely SRI-KEHATI Index companies listed on the IDX in 2020-2023. This research is a quantitative study with a sampling method, namely purposive sampling, so that a sample of 11 companies with 4 years of observation is obtained. The data used in this study are secondary data obtained through financial reports and company sustainability reports. Data analysis in this study used Partial Least Squares (PLS). The results showed that environmental performance has a significant effect on earnings management. Meanwhile, social performance does not affect earnings management.

Keywords: Environmental Performance, Social Performance, ESG, Earnings Management

INTRODUCTION

The rapid development of the business world increasingly encourages business actors always to improve their business performance to survive in fierce competition. On this basis, companies always present positive financial reports to show good business performance to stakeholders. One of the information reported in the financial statements is profit. Information related to profit can reflect management's performance in managing company resources and estimating the company's potential in the future (Nabiilah & Fahira, 2024). However, in some conditions, earnings-related information tends to be unable to reflect the company's potential in the future, so it encourages management to carry out various strategies, such as earnings management to produce financial reports according to the set target (Andriani & Arsjah, 2022).

Earnings management is a strategy to present positive financial information contrary to actual conditions (Almubarak et al., 2023). Earnings management is carried out to achieve profit targets (Soeprajitno et al., 2024). However, earnings management practices can lead to a loss of trust gained from investors through a decreased quality of information related to corporate profits (Suryananingtyas et al., 2024). Several phenomena related to earnings management have emerged yearly (Sabila & Susilowati, 2024). One of the earnings management phenomena that has occurred recently is in SRI-KEHATI index companies such as PT Wijaya Karya Persero Tbk and PT Semen Indonesia.

Allegations of earnings management practices at PT Wijaya Karya Persero Tbk are based on financial statements that are stated to be consistently profitable, even though cash flow has never been positive. In 2022, consolidated net income increased, but the company experienced a loss of IDR 59.6 billion (Murwani, 2023). Not only that, allegations of earnings management practices also occurred at PT Semen Indonesia, where the company allegedly polished the numbers in the 2022 financial statements so that they did not make quantitative sense where a drastic decrease in revenue was found, namely 30% or IDR 41.474 trillion without a clear cause (Pratama, 2024).

Several factors can influence earnings management, including ESG (Andriani & Arsjah, 2022). Companies utilize ESG as a medium to hide earnings management practices from stakeholders (Kolsi et al., 2023). Not only that, companies that do not pay careful

attention to financial and ESG issues in terms of reporting encourage greenwashing (Velte, 2021). Meanwhile, another opinion states that ESG can motivate companies to behave honestly when preparing financial reports (Andriani & Arsjah, 2022). In this case, sustainability performance, such as ESG, encourages companies to focus on profits and environmental and social aspects. Environmental performance relates to the impact of company operations on nature. In contrast, social performance relates to the company's ability always to establish good and long-term relationships with labor, customers, and society. On this basis, the company discloses its sustainability performance through a sustainability report separately or incorporated into the annual report, which refers to the established standards, namely the Global Initiative Reporting (GRI).

Based on the background and previous problems, the authors are interested in researching “The Effect of Environmental and Social Performance on Earnings Management.” This study aims to prove the effect of environmental and social performance on earnings management. In this study, earnings management is measured using the Modified Jones Model. In contrast, environmental and social performance is measured through the company's total environmental and social performance disclosure compared to the total disclosure according to the standard.

REVIEW OF LITERATURE

Earnings Management

Earnings management is a strategy to influence earnings so that reported earnings follow the company's future profit achievement goals (Scott, 2015, p. 445). Not only that, earnings management can also be interpreted as management actions in increasing or decreasing the profit of a unit, which is the responsibility of company management (Maryati et al., 2022). In this case, earnings management practices hurt the decline in the quality of corporate earnings and the loss of trust the company gains from investors and stakeholders (Suryananingtyas et al., 2024). In other words, these actions can damage the credibility of financial statements so that they mislead stakeholders in the decision-making process (Soeprajitno et al., 2024).

Environmental Performance

The environment is an aspect that plays a vital role in maintaining the existence of a company in the future. Therefore, companies constantly strive to protect the environment from the negative impacts of their operational activities. On this basis, environmental performance is a form of corporate responsibility in disclosing its activities as a response to the environment. Environmental performance can be measured by revealing information related to environmental aspects in the company's annual report (Abbas et al., 2020). In this case, ecological elements consist of the impact of company operations on nature, such as air, land, water, and the entire ecosystem (Seker & Sengür, 2021).

Social Performance

Social performance is a form of corporate responsibility to stakeholders by disclosing information related to social aspects. If the company wants to gain the trust of stakeholders, then the company must fulfill its social responsibilities. This is because the company's social responsibility is a significant contribution to the company's future survival (Acar & Coskun, 2023). In this case, social performance is related to work quality, job satisfaction, human rights, community involvement, and product responsibility (Ricapito, 2024).

SRI-KEHATI Index

The Sustainable and Responsible Investment (SRI)-KEHATI stock index is a green index published in collaboration between the KEHATI Foundation and the Indonesia Stock Exchange. In this case, the SRI-KEHATI index comprises 25 companies from various sectors listed on the Indonesia Stock Exchange. SRI-KEHATI indexed companies are selected based on standards, namely companies that apply Sustainable and Responsible Investment (SRI) and ESG principles. On this basis, SRI-KEHATI index companies can be interpreted as companies with more concern for the environment and society to encourage accountability in financial reporting (Tjun et al., 2024).

RESEARCH METHOD

This research is a quantitative approach. The quantitative method is a study approach based on the positivism philosophy (Sugiyono, 2022, p. 16). The population in this study were SRI-KEHATI Index companies listed on the IDX in 2020-2023. The sampling technique in this study used a purposive sampling method so that 11 companies were

obtained with 4 years of observation. The type of data used in this study is secondary data obtained from each company's financial statements and sustainability reports. The data analysis technique used in this research is Partial Least Square (PLS).

RESULTS AND DISCUSSION

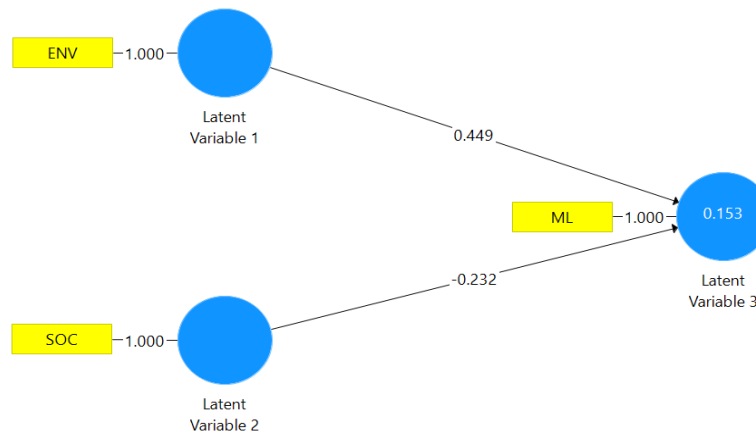


Figure 1.
Measurement Model Scheme (Outer Model)
Source: Secondary Data Processed, 2025

Convergent Validity can be interpreted as the loading factor value of the latent variable on its indicators. An indicator is good if it correlates > 0.6 with its construct. The Convergent Validity value can also be seen through the Average Variance Extracted (AVE) of each construct in the model. The results are declared valid if the AVE > 0.5.

Table 1.
Loading Factor Value

Variable	Loading Factor Value	Description
Environmental Performance	1,000	Valid
Social Performance	1,000	Valid
Earnings Management	1,000	Valid

Source: Secondary Data Processed, 2025

Table 2.
Average Variance Extracted (AVE)

Variable	AVE	Description
Environmental Performance	1,000	Valid

Social Performance	1,000	Valid
Earnings Management	1,000	Valid

Source: Secondary Data Processed, 2025

Based on Table 1 and Table 2, the loading factor value of each indicator is > 0.6 , which means that each indicator has a good relationship with each variable. Not only that, the Average Variance Extracted (AVE) value also has a value of > 0.5 , so all indicators and variables used in this study are valid. Therefore, the test results are valid by the Convergent Validity criteria.

Furthermore, in discriminant validity, constructs with good discriminant validity can be known through the cross-loading factor. In this case, the loading value of the intended construct must be greater than other constructs. Another way to measure discriminant validity is with the Fornell and Larcker method.

Table 3
Cross-Loading Value

Variable	ENV	SOC	EM
Environmental Performance	1,000	0,494	0,335
Social Performance	0,494	1,000	-0,010
Earnings Management	0,335	-0,010	1,000

Source: Secondary Data Processed, 2025

Table 4
Fornell and Larcker

Variable	ENV	SOC	EM
Environmental Performance	1,000		
Social Performance	0,494	1,000	
Earnings Management	0,335	-0,010	1,000

Source: Secondary Data Processed, 2025

Based on Table 3, each indicator has a more excellent cross-loading value than the cross-loading of indicators with other indicators. The most considerable cross-loading value is obtained from each indicator according to its variable, which is 1.000. Also, based on Table 4, the Fornell and Larcker values are obtained at 1.000 each, which means that all indicators used are valid and meet the discriminant validity criteria.

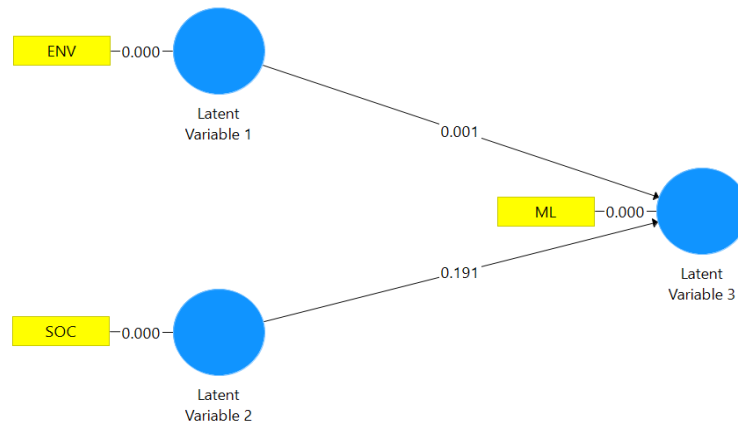


Figure 2.
Measurement Model Scheme (Inner Model)
Source: Secondary Data Processed, 2025

Based on Figure 2, the highest path coefficient value is obtained from the effect of social performance on earnings management, which is 0.191. Meanwhile, the lowest path coefficient value is obtained from the impact of environmental performance on earnings management, which is 0.001.

Table 5
R-Square Value

Variable	R-Square
Earnings Management	0,153

Source: Secondary Data Processed, 2025

The R-square value is the coefficient of determination on the dependent latent variable. The R-Square value is said to be strong if it has a value of 0.67, it is said to be moderate if it has a value of 0.33, and is considered weak if it has a value of 0.19. Table 5 shows that the R-Square value is 0.153 or 15.3%, which means that this research model is considered weak because it is <0.19. This indicates that environmental and social performance affects earnings management by 15.3%.

Table 6
Hypothesis Test Result

Variable	Original Sample (O)	Sample Mean (M)	STDEV	T Statistic	P Value
Environmental Performance -> Earnings Management	0,449	0,448	0,130	3,464	0,001
Social Performance -> Earnings Management	-0,232	-0,243	0,177	1,311	0,191

Source: Secondary Data Processed, 2025

H1: Environmental performance affects earnings management

The test results on the first hypothesis show that environmental performance significantly affects earnings management. The P-value of $0.001 < 0.05$ evidences this. These results are based on the criteria set out in the hypothesis test, so that it can be concluded that the first hypothesis is accepted.

H2: Social performance affects earnings management

The test results on the second hypothesis show that social performance has no significant effect on earnings management. The P-value of $0.191 > 0.05$ evidences this. These results are not based on the criteria set out in the hypothesis test, so it can be concluded that the second hypothesis is rejected.

The Effect of Environmental Performance on Earnings Management

The results of the tests that have been carried out show that environmental performance has a significant effect on earnings management. The higher the value of environmental performance, the more a company tends to engage in earnings management practices through increasing corporate profits (Asmara & Widiastuty, 2023). On this basis, companies involved in earnings management practices tend to have good environmental performance and implement sustainability to avoid unwanted stakeholder supervision. Almubarak et al. (2023) explain that company management utilizes environmental performance to cover up deviant actions in financial reporting, such as earnings management through its sustainability performance. In other words, companies use ecological performance to maintain the trust gained from stakeholders where the company wants stakeholders to continue to believe that the company has provided honest and transparent financial and non-financial information.

The Effect of Social Performance on Earnings Management

Based on the tests that have been carried out, the results show that social performance has no significant effect on earnings management. This is because disclosures related to social performance are considered normal to be published by companies, encouraging management not to use social performance to cover and maintain the company's reputation from deviant financial reporting practices such as earnings management. Not only that, social performance that has been considered normal to be published by the company causes it not to be an issue that attracts the attention of stakeholders, so social performance is not used as a medium to maintain a stable relationship with stakeholders in the long term (Citrajaya & Ghozali, 2020). Therefore, management does not consider social performance when practicing earnings management.

CONCLUSION

Based on the results of previous research, it can be concluded that environmental performance significantly affects earnings management. This is not without reason, but companies utilize ecological performance to avoid unwanted supervision from stakeholders and hide earnings management practices carried out through good sustainability performance. On the other hand, social performance does not affect earnings management. This is because disclosures related to social performance are considered normal so that they do not become an issue that can attract the attention of stakeholders, encouraging company management not to consider social performance when companies practice earnings management.

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