

Scope, Standards, and Signals: ESG Assurance and Profitability under Indonesia's Evolving Disclosure Regime

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ABSTRACT: This study investigates the impact of ESG (Environmental, Social, and Governance) assurance and disclosure quality on the financial performance of companies listed in the IDX ESG Leaders Index in Indonesia. Motivated by regulatory advances such as POJK 51/2017 and the adoption of SPK Indonesia aligned with IFRS S1 and S2, the research assesses whether comprehensive and credible ESG disclosures enhance Return on Equity (ROE) and reduce cost of capital. Using panel data for Q1 2024 and a balanced sample of 30 firms, the analysis examines ESG disclosure indicators Scope 1, 2, and 3 emissions, third party assurance, governance structures, and reference to global standards (GRI, ISSB) and their associations with ROE, excess returns, and cost of debt. Panel regression results show that firms with ESG assurance exhibit significantly higher ROE. Scope 3 emissions disclosure and alignment with ISSB also correlate with reduced financing costs. Robustness tests confirm the stability of results. The findings demonstrate that ESG assurance acts as a signal of credibility, mitigates greenwashing risk, and enhances market perception. Companies with strong ESG governance and transparent, standardized disclosures are more likely to attract investment and secure favorable financing terms. As Indonesia moves toward mandatory ESG assurance through SPK Indonesia, this research supports regulatory emphasis on verifiability and standard alignment. The study contributes localized empirical evidence from a leading Southeast Asian market and informs policy design, investor strategy, and corporate governance practices under evolving ESG disclosure standards.

Keywords: ESG Assurance, Scope 3 Disclosure, Financial Performance, SPK Indonesia, IDX ESG Leaders, IFRS S1/S2.



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INTRODUCTION

The introduction of the Financial Services Authority (OJK) Regulation No. 51/2017 (POJK 51/2017) marked a significant shift in the landscape of sustainability reporting within Indonesia, effectively mandating public companies to issue sustainability reports. This regulation has profound implications for Environmental, Social, and Governance (ESG) reporting practices in

Indonesia. It aims to integrate financial and non-financial aspects of companies' performances while compelling them to exhibit responsible business practices that align with sustainable development goals (Adhariani & Toit, 2020; Darsono, 2024). Businesses are increasingly recognizing that robust ESG reporting can enhance their public image, align with stakeholder expectations, and potentially lead to improved financial performance in the long run (Rini, 2024; Zahroh & Hersugondo, 2021).

Moreover, the Sustainable Financial Action Plan introduced by POJK 51/2017 plays an integral role in reshaping corporate governance practices. Companies are now encouraged to establish sustainability committees at the board level and link executive compensation to ESG performance, thereby fostering a culture of sustainability from the top down (Rini, 2024). The emphasis on transparency ensures that stakeholders notably investors can make informed decisions based on a company's adherence to ESG criteria. This shift is particularly crucial in Indonesia, where traditional risk management practices often overlook sustainability considerations, creating potential conflicts between economic growth and environmental stewardship (Hermawan & Handoyo, 2024).

The effect of international standards, such as International Financial Reporting Standards (IFRS) S1 and S2, extends to the global governance landscape, influencing ESG disclosure frameworks worldwide. These standards advocate for a consistent and transparent approach to reporting that companies must adopt to ensure comparability across jurisdictions (Zaid & Issa, 2023). The introduction of these standards aligns closely with growing pressures from global investors, urging companies to address financial risks and integrate a comprehensive view of their sustainability impacts (Ellili, 2022). Consequently, the IFRS guidelines contribute to narrowing the reporting gap seen in emerging markets and inspire local regulations, including those in Indonesia, to adopt similar frameworks that emphasize non financial performance as a pillar of corporate accountability (Adeneye et al., 2022).

Challenges exist in implementing ESG assurance in emerging markets like Indonesia, where infrastructures supporting sustainability reporting may still be in development. These challenges include a lack of reliable data, varying levels of regulatory enforcement, and a general absence of established practices for ESG assurance, leading to skepticism regarding the credibility of reported information (Narula et al., 2024). Furthermore, companies often struggle with cultural aspects that influence the interpretation and implementation of ESG guidelines, creating inconsistencies in how sustainability is perceived and reported (Hermawan & Handoyo, 2024).

In terms of investor decision making, the role of ESG assurance cannot be understated. Investors increasingly regard non financial metrics as integral components of corporate performance assessments, leading them to favor firms with high ESG ratings (Naseer et al., 2023). Companies that engage in thorough and credible ESG reporting are likely to gain access to capital and secure more favorable terms due to reduced perceived risk. The integration of ESG practices into investment strategies is becoming a crucial factor for investors, reflecting a significant evolution in how corporate value is evaluated (Indriani, 2024; Pirtea et al., 2021). This trend further signifies a shift towards sustainable investing, where stakeholder interests dictate essential elements of corporate governance and operational directives (Yunus & Nanda, 2024).

ESG indices, such as the Indonesia Stock Exchange ESG Leaders (IDXESGL), serve a pivotal role in shaping corporate behavior toward enhanced disclosure. By creating a benchmark for the performance of listed companies in ESG dimensions, these indices incentivize firms to improve their sustainability practices (Padilla-Rivera et al., 2024; Sumiati & Isnaini, 2024). Companies listed on such indices often face elevated scrutiny and competitive pressure to maintain high standards of ESG reporting, propelling them toward adopting more proactive approaches to sustainability (Sumiati & Isnaini, 2024). Compliance with ESG norms can enhance corporate attractiveness to investors and improve overall market performance (Y. Li et al., 2018).

Financial market reactions to ESG regulatory announcements in Indonesia have varied, with a notable trend towards positive reception when companies demonstrate adherence to the new frameworks (Darsono & Ma'la, 2024). Investors typically respond favorably to companies that enhance their sustainability reporting, as this alignment is perceived as a risk mitigation strategy, potentially leading to stronger long term returns (Darsono & Ma'la, 2024). Empirical studies suggest that announcements related to ESG standards often correlate with positive stock price movements, reflecting an optimistic outlook from market participants regarding the companies involved (Moussa & Elmarzouky, 2024). Moreover, as regulatory environments tighten globally, companies in Indonesia that align more closely with these expectations are likely to gain substantial competitive advantages, fostering resilience in their business operations (Alsayegh et al., 2020; Marie et al., 2024).

Overall, while significant strides have been made in framing the ESG landscape within Indonesia through regulations such as POJK 51/2017, ongoing challenges remain, particularly regarding data integrity and cultural alignment in reporting practices. Nevertheless, the impact of these regulations, coupled with international standards like IFRS S1 and S2, has set the stage for collaborative efforts where local and global entities converge towards heightened corporate responsibility and transparency.

METHOD

The methodology employed in this study is grounded in quantitative research techniques tailored for ESG finance research, particularly using a panel regression model. This method is ideal for analyzing datasets that span both cross sectional and time series dimensions, allowing for a more comprehensive understanding of the dynamics between ESG assurance, disclosure quality, and financial performance (Almeyda & Darmansya, 2019).

This study utilizes a balanced panel dataset comprising 30 firms listed on the IDX ESG Leaders Index during the first quarter of 2024 (January–March). The choice of a balanced panel ensures data consistency across entities and over the time frame, enhancing the robustness and accuracy of the results (Nicolò & Peña, 2024).

Independent Variables:

- *Scope 1, 2, and 3 emissions disclosure* (binary indicators based on reporting presence).
- *Assurance presence* (binary: 1 if an independent assurance statement is disclosed; 0 otherwise).

- *Existence of ESG committee* (binary: 1 if committee is in place; 0 otherwise).
- *Use of global standards* (binary: 1 if the report refers to GRI/ISSB frameworks).

These variables are derived from sustainability reports and assessed according to international frameworks, such as the GHG Protocol, which provides industry aligned definitions and measurement techniques for greenhouse gas emissions (Huralikoppi, 2024).

Dependent Variables:

- *Return on Equity (ROE)* – a standard measure of profitability.
- *Excess return* – calculated relative to sectoral or market benchmarks.
- *Cost of debt* – proxied by bond yield spreads or debt servicing ratios.

Control Variables:

- Firm size (logarithm of total assets)
- Financial leverage
- Revenue growth rate (quarter over quarter)
- Sector classification (dummy variables)

Primary data were extracted from corporate sustainability reports and financial statements issued in Q1 2024. Index data were sourced from the Indonesia Stock Exchange (IDX), while ESG Risk Ratings and controversy screenings were referenced from Sustainalytics.

Sustainalytics' ESG Risk Ratings are widely used in the investment community and incorporate both qualitative and quantitative metrics to gauge a firm's ESG exposure. While some studies affirm their relevance in identifying credit risks and investor concerns, others caution against over reliance due to variability in methodology and transparency (Bernardelli et al., 2022; Demers et al., 2021).

The panel regression analysis employs both Fixed Effects and Random Effects models to control for firm level heterogeneity and unobserved characteristics (Ponce & Wibowo, 2023; Amaliah et al., 2020). The model specification is as follows:

$$\text{ROE}_{it} = \alpha + \beta_1(\text{Assurance}_{it}) + \beta_2(\text{Scope3}_{it}) + \beta_3(\text{Standards}_{it}) + \beta_4(\text{ESGComm}_{it}) + \text{Controls}_{it} + \varepsilon_{it}$$

Model selection between FEM and REM is guided by the Hausman test. Robustness checks include event studies around index rebalancing dates to capture market responses to ESG disclosure changes.

This methodological framework aligns with emerging best practices in ESG finance research, emphasizing replicability, data transparency, and policy relevance.

RESULT AND DISCUSSION

This section presents the findings of the study, which are organized into descriptive statistics, regression outputs, and robustness diagnostics. These results assess the relationship between ESG assurance, Scope 3 disclosure, use of global reporting standards, and financial performance among IDX ESG Leaders for Q1 2024.

Descriptive Statistics

Among the 30 firms assessed, all disclosed Scope 1 and Scope 2 emissions in their sustainability reports. However, only 70% disclosed Scope 3 emissions. This finding is consistent with global evidence that Scope 3 disclosure remains a challenge, even among ESG leaders, due to methodological complexity and data collection barriers (Hettler & Graf-Vlachy, 2023).

Independent ESG assurance was reported by 40% of the sample, with greater prevalence in the financial sector. These numbers align with ASEAN wide trends, where third party assurance is still developing, with only about 30% of firms adopting such practices (Singhania & Chadha, 2023).

Additionally, 80% of firms maintained ESG committees. The presence of such structures has been associated with more comprehensive and consistent disclosure practices in previous studies (Gönenç & Krasnikova, 2022). On disclosure standards, 90% of the firms referenced the GRI framework, while 30% incorporated ISSB alignment, reflecting the transitional state of standard adoption across emerging markets (Verbeeten et al., 2016).

Table 1. ESG Disclosure Characteristics of IDXESGL Firms (Q1 2024)

Disclosure Element	Firms Reporting (%)
Scope 1 and 2 Emissions	100%
Scope 3 Emissions	70%
ESG Assurance	40%
ESG Committee Presence	80%
GRI Standard Referenced	90%
ISSB Standard Referenced	30%

Regression Analysis

Panel regression results reveal a positive and statistically significant relationship between ESG assurance and Return on Equity ($\beta = +2.1$, $p < 0.05$). This supports the assertion that transparent and independently verified ESG disclosures contribute to improved profitability (Bogdan et al., 2023).

Similarly, Scope 3 disclosure demonstrates a negative relationship with cost of debt ($p < 0.1$), suggesting that firms actively addressing indirect emissions may face lower financing costs due to increased investor confidence and risk mitigation (X. Li et al., 2023).

The use of ISSB standards correlates with stronger excess returns and valuation multiples, reinforcing the perception that adherence to globally recognized standards enhances investor appeal (Katafuchi et al., 2024).

Table 2. Regression Summary of Key ESG Factors and Financial Performance

Variable	ROE Coefficient	p value	Cost of Debt Coefficient	p value
ESG Assurance	+2.1	0.034	1.2	0.041
Scope 3 Disclosure	+1.6	0.073	0.9	0.087
ISSB Standard Used	+2.3	0.051	1.5	0.062
ESG Committee Presence	+1.1	0.116	0.6	0.153

Robustness Checks

Robustness was tested using several diagnostic tools:

- Multicollinearity: Variance Inflation Factors (VIF) were below 5 for all regressors, indicating no multicollinearity threats (Verbeeten et al., 2016).
- Heteroscedasticity: Breusch Pagan tests confirmed homoscedastic residuals.
- Autocorrelation: Durbin Watson statistics were within acceptable thresholds, suggesting independence of residuals (Christensen et al., 2021).

An additional robustness check used event study techniques around IDXESGL rebalancing announcements. Firms newly included in the index exhibited positive abnormal returns, suggesting that improved ESG disclosure quality and assurance are recognized and rewarded by the market.

Table 3. Robustness Diagnostics Summary

Test Type	Result
VIF (Multicollinearity)	All < 5
Breusch Pagan (Hetero.)	No heteroscedasticity detected
Durbin Watson	Values between 1.6 and 2.2
Event Study Effect	Positive abnormal returns noted

These findings affirm the empirical relationship between ESG disclosure quality and financial outcomes, especially under Indonesia's evolving regulatory and disclosure landscape.

ESG Assurance and Greenwashing Risk

The findings of this study affirm the growing significance of ESG assurance and comprehensive disclosure in enhancing corporate financial performance. The positive association between third party ESG assurance and Return on Equity (ROE) not only aligns with global evidence but also

underscores the strategic relevance of transparent ESG practices in emerging markets like Indonesia. This suggests that investors are no longer treating sustainability disclosures as supplementary, but instead as core components of due diligence and investment decision making.

One of the most critical contributions of ESG assurance is its role in mitigating greenwashing risk. Greenwashing, where companies overstate or misrepresent their sustainability credentials, undermines market integrity and investor trust. In the absence of formal verification, sustainability claims may be perceived as promotional rather than factual, thereby eroding confidence in corporate communications. Independent assurance helps bridge this credibility gap by offering a reliable validation mechanism for ESG claims. By relying on third party auditors or recognized assurance providers, firms demonstrate their commitment to accountability, transparency, and rigorous internal controls. This form of verification sends a strong market signal about a firm's commitment to sustainability, thereby reducing perceived risks and enhancing reputational standing (Tang & Demeritt, 2017). It also establishes a feedback mechanism within organizations, where disclosures are not only externally validated but internally improved through iterative quality control.

Investor Perceptions and ESG Governance

Investor sentiment is particularly responsive to the presence of strong ESG governance structures. The findings reinforce previous studies which show that institutional investors increasingly rely on indicators of governance quality such as ESG committees, transparent reporting lines, and board level oversight to guide investment decisions. These structures enhance organizational clarity, ensure responsibility for ESG implementation, and signal long term strategic planning capacity. Firms with established ESG governance mechanisms are not only seen as more resilient but are also preferred by investors for their perceived long term value generation (Kräussl et al., 2023; López-de-Silanes et al., 2024).

This investor preference translates into tangible financial benefits. The analysis reveals that companies disclosing Scope 3 emissions and aligning their ESG reports with recognized global standards such as ISSB exhibit lower cost of capital. These practices reflect operational transparency and strategic alignment with long term sustainability goals. They also reduce uncertainty regarding ESG related risks, leading investors to demand lower returns for capital provision. Investors interpret such disclosures as evidence of effective risk management, particularly in sectors that are exposed to environmental and supply chain disruptions. Furthermore, these practices help reduce volatility by limiting surprise factors, thereby improving capital access and strengthening stakeholder engagement.

Regulatory Implications and Policy Alignment

From a regulatory standpoint, these findings support the case for integrating financial performance linkages into ESG disclosure mandates. Frameworks like SPK Indonesia which align with IFRS S1/S2 can significantly influence corporate behavior by standardizing expectations and

emphasizing the financial implications of sustainability disclosures (Raimo et al., 2021; Sciarelli et al., 2021). By mandating structured disclosures and encouraging international comparability, these frameworks enhance investor confidence and promote accountability.

Requiring firms to disclose ESG metrics that directly correlate with performance encourages better governance, enhances data quality, and promotes responsible investment. It also enables regulatory bodies to set clearer compliance thresholds, facilitates benchmarking, and allows for more effective market surveillance. Policymakers can leverage these insights to create differentiated reporting tiers, provide assurance incentives, and link compliance with fiscal or regulatory rewards. Thus, regulation evolves from enforcement to facilitation, supporting the maturation of sustainable markets.

Mandatory Regimes and Corporate Strategy

Mandatory ESG disclosure regimes also appear to act as catalysts for strategic transformation. As regulations evolve, companies adapt by embedding ESG into their operational and strategic frameworks. This shift is evident in the growing prevalence of ESG committees, Scope 3 reporting, and assurance practices across IDX ESG Leaders. Regulatory pressure provides a foundation for consistent ESG integration, reducing reputational risks and enhancing cross sectoral comparability (Kulal et al., 2023).

Moreover, the obligation to disclose transforms ESG from a reactive reporting function into a proactive component of corporate planning. Companies invest in data systems, employee training, supplier engagement, and board level ESG capabilities. These adaptations not only improve disclosure quality but also drive substantive improvements in ESG performance. Consequently, ESG becomes part of broader value creation strategies, influencing innovation, resilience, and competitive advantage.

Furthermore, these regimes improve decision making for investors by establishing a baseline of comparability. Standardized metrics, as promoted by ISSB and GRI, facilitate more accurate assessments of firm performance and sustainability integrity. Consequently, investors can better differentiate between firms with genuine ESG commitments and those engaging in symbolic compliance. This transparency also facilitates the development of ESG linked investment instruments, enabling capital to flow toward more responsible firms and discouraging superficial adoption of ESG practices.

CONCLUSION

This study explores the relationship between ESG assurance, disclosure quality, and financial performance among IDX ESG Leaders in Indonesia. The findings reveal that companies with third party ESG assurance, Scope 3 disclosures often the most complex and informative indicators further differentiate firms by illustrating a comprehensive grasp of their environmental impact across the value chain. These associations emphasize the financial benefits of verifiable and transparent ESG practices.

ESG assurance emerged as a key credibility mechanism that mitigates the risk of greenwashing, enhances investor trust, and signals a firm's commitment to long term sustainability. Firms that engage independent assurance providers demonstrate superior governance and accountability, which translates into improved market reputation and financial attractiveness. Scope 3 disclosures often the most complex and informative emission indicators further differentiate firms by illustrating a comprehensive grasp of their environmental impact across the value chain.

The presence of ESG governance structures, such as board level sustainability committees, contributes to higher reporting quality and organizational alignment with sustainable goals. These internal mechanisms not only satisfy regulatory expectations but also meet investor demand for transparency and consistency in ESG performance.

This research also affirms the role of regulatory frameworks, particularly SPK Indonesia, in shaping corporate ESG strategy. As Indonesian regulators align local policies with IFRS S1 and S2, the emphasis on comparability and assurance is likely to increase. Mandated disclosures and assurance protocols create a more level playing field and enable investors to better assess the integrity of sustainability claims.

The key contribution of this study is its empirical validation of the link between ESG assurance and financial performance in an emerging market context. It supports global findings while offering localized insights into how regulatory alignment and investor expectations shape ESG behavior among Indonesian firms.

Future research could extend this analysis over a longer period, capturing the evolution of ESG practices post implementation of SPK Indonesia in 2027. Moreover, expanding the sample beyond IDXESGL firms would allow for a broader assessment of disclosure heterogeneity and its financial implications. Ultimately, as ESG continues to gain prominence, firms that prioritize data credibility, comprehensive reporting, and governance oversight will be better positioned to attract investment, manage risks, and contribute to sustainable economic growth.

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