AAJ ACCOUNTING ANALYSIS JOURNAL

Accounting Analysis Journal

https://journal.unnes.ac.id/sju/index.php/aaj

The Effect of Corporate Political Engagement on Environment, Social, & Governance (ESG) Disclosure

Verna Budi Amanda [1]✉ and Ainun Na'im [2]

[1,2]Faculty of Economics and Business, Universitas Gadjah Mada, Indonesia

ARTICLE INFO

Article History:
Submitted February 26th, 2024
Revised May 20th, 2024
Accepted September 29th, 2024
Published October 24th, 2024

Keywords:
Corporate Political Engagement, ESG Disclosure, Ownership Structure, Earnings Quality

ABSTRACT

Purpose : The research investigates the relationship between corporate political engagement and ESG disclosure moderated by the ownership structure and mediated by earnings quality. The sample for this study consists of companies that sponsor, build, and operate steam power plants in Indonesia.
Method : Sample consists of 22 companies sponsoring, constructing, and operating steam power plants in Indonesia particularly during the period 2019-2021. In testing for the direct effect, moderation effect, and mediation effect, the researchers use multiple regression analysis, moderated regression analysis, and path analysis.
Findings : The results of the statistical test show evidence that corporate political engagement has a negative relationship with ESG disclosure and the ownership structure is capable of weakening the negative relationship between corporate political engagement and ESG disclosure. However, earnings quality is unable to mediate the relationship between corporate political engagement and ESG disclosure.
Novelty : The research has several original factors. First, this research utilizes ownership structure as a moderation variable and earnings quality as a mediation variable. Second, this research analyzes the relationship between corporate political engagement and all the ESG components, aiming for more comprehensive results compared to previous studies.

INTRODUCTION

Extreme climate change has a significant impact on the global economy, including a reduction in global GDP by up to 7.2%, decreased corporate revenues and profits, and increased inflation (Javadi & Masum, 2021; Kahn et al., 2019; Wade & Jennings, 2016). One of the main causes of climate change is the rise in carbon gas emission (European Commision, 2023), with energy companies being the largest contributors to carbon emissions and thus significantly driving climate change (Environmental Protection Agency, 2023). Due to the substantial negative impacts, more companies are beginning to pay attention to the environmental and social effects which is caused by their operational activities. This is proven by the growing interest in disclosing Environmental, Social, and Governance (ESG) factors in corporate reports over the past few years.

ESG disclosure has been proven to enhance corporate reputation and financial performance by increasing competitive advantage (H. Chen et al., 2022; Chouaibi et al., 2022; Duque et al., 2021; Nekhili, 2021). Companies with excellence ESG performance are also believed to be more resilient to climate change risk due to the flexibility contingency within their operations, which allowed them to have better crisis management (Chouaibi et al., 2022). However, despite the importance and benefits of ESG disclosure, many companies do not prioritize ESG disclosure as one of their corporate reports, particularly those who engage in political activities (Dicko et al., 2020).

In simple terms, corporate political engagement is an interaction between the business sector and the regulators (Yazid & Angelica, 2021). This interaction can involve lobbying to strengthen the relationship between companies and policymakers, advocating opinions to influence specific regulations, partnering with coalitions to shape government agendas, and providing campaigns through political action committees (PAC) to support specific candidates. The interaction between companies and the government is one form of legitimacy-seeking action that can assist the government. However, when corporate political engagement is conducted in a non-transparent way,

* E-mail: vernabudiamanda@mail.ugm.ac.id
Address: Jln. Sosio Humaniora No. 1, Bulaksumur, Yogyakarta, Indonesia

DOI 10.15294/aaj.v13i2.1898 p-ISSN 2252-6765 e-ISSN 2502-6216

it can create a situation where a company is able to influence public policies so they align with its own interests, particularly in the context of this research, we refer to policies related to ESG disclosure in corporate reports.

The purpose of this research is to analyze how corporate political engagement can influence management decisions to disclose voluntary information such as environment, social, & governance (ESG) in company reports. Previous studies have demonstrated the benefits that political connections can provide to companies, including easier access to funding, improved financial performance, and granting privileges to companies such as access to legislative processes (H. Chen et al., 2022; Chouaibi et al., 2022; Duque et al., 2021; Hölzer et al., 2022; Nekhili, 2021). However, there is still limited research presenting evidence on how the political connections of a company can affect management decisions related to the disclosure of voluntary information, such as ESG. This research is expected to fill the literature gap in this regard.

This research offers several novelties. First, based on previous studies, there is still a scarcity of research examining the influence of corporate political engagement on ESG disclosure. Most studies only investigate the impact of corporate political engagement on individual ESG components, such as environmental disclosure, corporate social responsibility (CSR), and governance practices. Examples of such studies include those conducted by Al-Hadi et al. 2018, Cheng et al. 2017 and Muttakin et al., 2018. Research focusing on each ESG component results in less comprehensive findings. Therefore, the researcher aims to fill this research gap by taking a more holistic approach. Second, this research utilizes ownership structure as a moderating variable and earnings quality as a mediating variable.

This research used Resource Dependence Theory as a main theory. According to the resource dependence theory, every company must have access to external resources to continue to survive and grow (Dicko et al., 2020). Therefore, to overcome this, companies must rely on their social connections. Companies involved in politics can leverage their political connections to gain access to key external resources, enabling them to continue to survive and grow (Dicko et al., 2020). In Indonesia, political connections play a crucial role in the sustainability of a company, as exemplified by power plant (PLTU) companies in the country. The level of corruption and bribery cases within these companies is notably high, as evidenced by two factors. First, according to the Transparency in Corporate Reporting (TRAC) research in 2019, 51 out of 95 power plant development companies lacked any corruption prevention systems. Additionally, recent corruption and bribery cases have implicated numerous public officials in Indonesia. For instance, the corruption case involving the Riau-1 power plant ensnared former Minister of Social Affairs Idrus Marham, former Member of Parliament Eni Maulani Saragih, and Johanes Kotjo in the procurement of the Riau-1 power plant project under the Power Supply Business Plan (or RUPTL) 2016-2025. Another case involves bribery related to the permits of PT. Cirebon Energi Prasarana (PLTU 2), which implicated the former Regent of Cirebon Sunjaya Purwadisastra. The prevalence of high corruption and bribery is attributed to individuals and companies, especially private ones, not being part of networks that enjoy privileges in winning business competitions. For companies with political connections, leveraging these connections can provide a competitive advantage in business competitions (Yazid & Angelica, 2021). Therefore, political connections represent one of the most important social networks that can help companies survive and thrive.

In contrast to companies involved in politics, those not engaged in political activities must participate in various activities such as voluntary disclosures (such as ESG) to enhance their legitimacy and reputations. This enables them to attract external stakeholders for funding, ensuring their ability to survive in the market (Dicko et al., 2020). This argument is supported by research conducted by Boubakri et al. (2012), which shows that politically connected companies have a lower cost of equity compared to companies not connected with politics. This allows them to have easier access to financial resources, reducing the urgency to disclose ESG in corporate reports. This is in contrast to companies not connected with politics, which require ESG disclosure to attract external interest for investment. Additionally, according to Dicko et al. 2020, ESG disclosure is typically done by companies facing high litigation risks, whereas politically connected companies often have lower litigation risks. This argument is supported by Jia et al. 2019, indicating that politically connected companies often receive favoritism from the high courts. They have access to bureaucratic systems that can influence overall court decisions, making it easier for them to resolve business conflicts (Jia et al., 2019). Based on these considerations, the first hypothesis proposed in this study is as follows.

H_1: Corporate political engagement has a negative impact on ESG disclosure

Ownership structure is a key indicator that can describe a company's identity and contribute to institutional perspectives, influencing a company's motives in disclosing information (Eng & Mak, 2003). Additionally, the ownership structure significantly affects corporate decision-making, making it a catalyst in this study (Amosh, 2022). This study uses foreign ownership and domestic ownership, as moderating variables. According to Amosh (2022), foreign ownership can enhance corporate governance and maximize stakeholder value by encouraging companies to respond to their demands and aspirations, including the level of corporate disclosure regarding sustainability, such as ESG disclosure. Fahad & Nidheesh (2020) suggest that due to geographical differences, foreign investors tend to increase demands for corporate disclosure. They expect a higher level of disclosure from domestic companies because of their international market experience. Foreign investors are highly aware of the importance of businesses being socially responsible in the current environmental context.

Furthermore, according to Khan et al. (2013), when a company is allowed to be owned by the general public, public accountability becomes crucial for the company. Therefore, such companies tend to disclose more comprehensive additional information due to the transparency and accountability issues arising from the involvement of numerous stakeholders. Based on these arguments, the researcher suggests that the levels of foreign ownership and domestic ownership in a company can influence the extent of ESG disclosure in corporate reports, including for politically connected companies. Thus, the next hypotheses proposed in this study are:

H_{2a}: Foreign ownership weakens the negative relationship between corporate political engagement and ESG disclosure

H_{2b}: Domestic ownership weakens the negative relationship between corporate political engagement and ESG disclosure

This study also uses earnings quality as a mediating variable. According to Hölzer et al. (2022), policy uncertainty resulting from political decisions can impact each company, and one of the consequences is the practice of income shifting by companies, to align reported profits with their desired figures (Ozili, 2020). As a result, this practice can worsen the earnings quality of the company. Harymawan & Nowland (2016) state that two situations can influence the impact of corporate political connections on earnings quality. The first situation is when the government plays an effective role, and the second situation is the level of political stability. When companies benefit from their political connections, it can reduce the company's responsiveness to market pressure, thereby reducing earnings quality. Similar to Harymawan & Nowland (2016), Chaney et al. (2011) provide two reasons why companies involved in politics have poor earnings quality. First, insiders in politically connected companies can hide or delay the disclosure of the benefits received by the company to deceive investors. Second, the protection provided by political connections makes companies less concerned about earnings quality. In conclusion, there is a negative relationship between companies involved in politics and earnings quality. The higher (lower) the political connections of the company, the lower (higher) the earnings quality of the company.

According to Francis *et al.* (2008), there is a positive relationship between earnings quality and voluntary disclosure. Francis *et al.* (2008) states that companies with high (low) earnings quality tend to disclose more (less) additional information, such as ESG, because investors would perceived the information as more (less) credible. The information which is announced by companies with low earnings quality is based on the low quality information, therefore rational markets may consider that the information disclosed by the company is not credible. Hence, it can be concluded that there is a positive relationship between earnings quality and ESG disclosure, where companies with good (poor) earnings quality tend to disclose more (less) ESG information in corporate reports.

The political connections held by a company offer various benefits, such as lower cost of debt (Tee & Kasipillai, 2022), equity (Boubakri et al., 2012), ease of obtaining credit loans (Leuz & Oberholzer-Gee, 2006), collaboration opportunities with the government (Bunkanwanicha & Wiwattanakantang, 2009), and government bailouts (Faccio et al., 2006). Because political connections can bring many advantages to a company, the company may no longer feel the need to disclose ESG information to enhance its reputation and attract investor interest for capital investment. Consequently, indirectly, the company may no longer find it necessary to be more responsive to the market and enhance its earnings quality (Harymawan & Nowland, 2016; Tee & Kasipillai, 2022).

Based on the arguments presented earlier, it can be concluded that earnings quality has the potential to mediate the influence of corporate political engagement on ESG disclosure. Therefore, the final hypotheses proposed in this study are:

H_{3a}: Corporate political engagement has a negative relationship with earnings quality

H_{3b}: Earnings quality has a positive relationship with ESG disclosure

H_{3c}: Earnings quality mediates the relationship between corporate political engagement and ESG disclosure

RESEARCH METHODS

The population for this study refers to the report published by TI Indonesia, titled "Corporate Political Engagement Index 2021: Assessment of Corporate Political Engagement in Steam Power Plants (PLTU) in Indonesia." TI Indonesia has identified at least 90 companies sponsoring, constructing, and operating PLTU in Indonesia, both domestically and internationally. This includes companies sponsoring, constructing, and operating steam power plants in Indonesia. The selection of PLTU is based on the TI Indonesia report, indicating that many PLTU companies exhibit non-transparent political activities (Yazid & Angelica, 2021). TI Indonesia assesses corporate political engagement in 5 dimensions with each dimension has several criteria that must be fulfilled by the company (see Table 1 for details). The assessment is done by analyzing documents that can be publicly obtained, such as annual report, sustainability report, corporate good governance guidance, corporate ethical guidance, and anti-corruption policy which are published in the period of 2018-2020. After analyzing those documents, TI Indonesia provides the opportunity for company to give feedback on the assessment results. The results range from 0-10, with 0 meaning the corporate highly engages in political activity but has the lowest political activity disclosure and vice versa. The results from the 5 dimensions have been included in TI Indonesia report and these score will be used by the researcher. However, for the research's needs, the researcher has established criteria for selecting a sample using purposive sampling. These criteria include companies regularly publishing their financial reports during the study period (2019 to 2021) and having ESG scores listed on Bloomberg. Hence, the analysis unit used in this research is the organizational level. Operational definitions for each variable uses in the research are presented in table 1.

The data use in this research are secondary data in the form of annual report. The researcher uses annual reports which can be obtained from the stock exchange websites of each respective country or the companies' websites. For ESG data, researchers utilize the Bloomberg database. For corporate political engagement data, the researcher uses data provided by TI Indonesia. TI Indonesia has provided a score range from 0-10 for each company in their report mentioned above along with the method they used for scoring. Last, for ownership structure, the researcher examines a percentage for both foreign ownership and domestic ownership in each company's annual report.

The testing of H_1 in this study was conducted using the multiple linear regression method. Equation 1 below represents the regression model used to test the first model of this study, which was the influence of corporate political engagement (PCON) on ESG disclosure (ESG)

$$ESG_{i,t} = \beta_0+\beta_1PCON+\beta_2F\_PERF_{i,t}+\beta_3SIZE_{i,t}+\beta_4LEV_{i,t}+\beta_5LIQ_{i,t} \quad \ldots\ldots 1$$

The testing of H_{2a} and H_{2b} in this study was conducted using the moderated regression analysis method. Equations 2 and 3 below are the regression model equations used to test H_2 in this study, which was the influence of corporate political engagement (PCON) on ESG disclosure (ESG) moderated by foreign ownership (FOREIGN_OWN) and domestic ownership (DOM_OWN).

$$ESG_{i,t} = \beta_0+\beta_1PCON+\beta_2FOREIGN\_OWN+\beta_3PCON*FOREIGN\_OWN+\beta_4F\_PERF_{i,t}+\beta_5SIZE_{i,t}+ \beta_6LEV_{i,t}+\beta_7LIQ_{i,t} \quad \ldots\ldots 2$$

$$ESG_{i,t} = \beta_0+\beta_1PCON+\beta_2DOM\_OWN+\beta_3PCON*DOM\_OWN+\beta_4F\_PERF_{i,t}+\beta_5SIZE_{i,t}+ \beta_6LEV_{i,t}+\beta_7LIQ_{i,t} \quad \ldots\ldots 3$$

The testing of $H_{3a,}$ $H_{3b,}$ and H_{3c} in this study was conducted using the path analysis method. Equations 4, 5, and 6 below are the regression model equations used to test the mediating effect of earnings quality (E_QUALITY).

$$EQUALITY_{i,t} = \beta_0+\beta 2PCON_{i,t}+\beta_3F\_PERF_{i,t}+\beta_4SIZE_{i,t}+\beta_5LEV_{i,t}+\beta_6LIQ_{i,t} \quad \ldots\ldots 4$$

$$ESG_{i,t} = \beta_0+\beta_1E\_QUALITY_{i,t}+\beta_2F\_PERF_{i,t}+\beta_3SIZE_{i,t}+\beta_4LEV_{i,t}+\beta_5LIQ_{i,t} \quad \ldots\ldots 5$$

$$ESG_{i,t} =\beta_0+\beta 1PCON_{i,t}+\beta_2E\_QUALITY_{i,t}+\beta_3F\_PERF_{i,t}+\beta_4SIZE_{i,t}+\beta_5LEV_{i,t}+\beta_6LIQ_{i,t} \quad \ldots\ldots 6$$

RESULTS AND DISCUSSIONS

The sample in this study refers to the report published by TI Indonesia, titled "Corporate Political Engagement Index 2021: Assessment of Corporate Political Engagement in Steam Power Plant Companies in Indonesia." TI Indonesia has identified at least 90 companies sponsoring, constructing, and operating steam power plants (PLTU) in Indonesia. First, the researcher eliminated 45 companies that did not publish their financial reports during the research period. Second, the researcher excluded 23 companies that did not have ESG scores listed on Bloomberg. The final sample for this study consisted of 22 companies with a total of 66 items of observation data. Table 2 shows the results of the descriptive statistical tests for the 66 items of observation data. Political connection (PCON) had a minimum value of 0 because TI Indonesia measured the political engagement of PLTU companies on a scale of 0 - 10. Table 3 shows the results of hypothesis testing for H_1. The results of the H1 test indicated that corporate political engagement (PCON) had a significance value of $< \alpha$ (5%), which was 0.039 with a coefficient value of $\beta = -0.274$. Based on this, it could be concluded that H_1 was supported, meaning that corporate political engagement (PCON) had a negative and significant effect on ESG disclosure.

Table 4 shows the results of hypothesis testing for H_{2a} and H_{2b}. Based on Table 4, the significance values for both foreign ownership and domestic ownership were 0.000 and 0.042, respectively, which were $< \alpha$ (5%). This meant that both foreign ownership and domestic ownership could act as moderating variables. In conclusion: **1) Foreign ownership** (FOREIGN_OWN) had a significance value of 0.046 with a coefficient β of -0.491. Based on this, it could be concluded that Hypothesis H_{2a} has been accepted. This is consistent with the research conducted by Amosh (2022). In addition, the adj. R-square value in model 2 was 68.3%, indicating that 68.3% of the variation in the dependent variable was explained by the independent variable in Hypothesis H_{2a}. **2) Domestic ownership** (DOM_OWN) had a significance value of 0.000 with a coefficient β of -1.191. Based on this, it could be concluded that Hypothesis H_{2b} has been accepted. This is consistent with the research conducted by Amosh (2022) and Fuadah et al. (2022)social, and governance (ESG. In addition, the adj. R-square value in model 3 was 88.8%, indicating that

Table 1. Variable's Operational Definitions

Variables		Operational Definitions	Resources	Measurement
Dependent	ESG	ESG is how companies and investors integrate issues related to environmental, social, and governance (ESG). (Gillan et al., 2021)	Bloomberg	Average of 3 ESG's components, namely environmental, social, and governance. (Dicko et al., 2020)
Independent	Corporate Political Engagement	Corporate Political Engagement is an interaction between the business sector and government. (Transparency International, 2018)	Report published by TI Indonesia, titled "Corporate Political Engagement Index 2021: Assessment of Corporate Political Engagement in Steam Power Plants (PLTU) in Indonesia."	TI Indonesia measured corporate Political Engagement using five dimensions. These dimensions were: 1) Dimension1: Control Environment 2) Dimension 2: Political Donation 3) Dimension 3: Responsible Lobbying 4) Dimension 4: Revolving Door 5) Dimension 5: Transparency in Reporting
Moderation	Ownership Structure	This research use 2 type of ownership structure, namely foreign ownership and domestic ownership. Foreign ownership is a number of shares owned by foreign investors (V. Z. Chen et al., 2014). Whereas domestic ownership is described as a number of shares owned by a company's founder, domestic companies, and institutional investors (Choi et al., 2011, 2012).	Annual Report	Foreign ownership is measured by percentage of foreign ownership in each of company's annual report (Amosh, 2022). Whereas domestic ownership is measured by a percentage of domestic ownership in each company's annual report (V. Z. Chen et al., 2014)
Intervening	Earnings Quality	Earnings Quality refers to the relevance of profits in measuring a company's performance (Subramanyam & Wild, 2014). This research uses Penman (2001) approach to calculate earnings quality. If operating income no longer contains transitory items, it can be used to predict the company's future condition. To determine if operating income accurately reflects the company's performance is by comparing it with operating cash flows (Penman, 2001). The smaller the ratio reflects how well the company's earning quality is (Houqe & Islam, 2011; Penman, 2001).	Annual Report	Operating Cash Flow / Operating Income (Houqe & Islam, 2011; Penman, 2001)
Control	Financial Performance	Financial performace is a subjective measure of how well a company can use assets to generate revenues (Gallego-Álvarez & Pucheta-Martínez, 2020).	Annual report	Net Income / Total Assets (Gallego-Álvarez & Pucheta-Martínez, 2020)
	Firm Size	Firm size is the size of company which is measure by total revenue (Gallego-Álvarez & Pucheta-Martínez, 2020).	Annual report	Ln (Total Asset) (Gallego-Alvarez & Pucheta-Martinez, 2020)
	Leverage	Leverage is a subjective measure of how a company uses debt or borrowed capital to undertake an investment or project (Gallego-Álvarez & Pucheta-Martínez, 2020).	Annual report	Total Debt / Total Assets (Gallego-Alvarez & Pucheta-Martinez, 2020)
	Liquidity	Liquidity refers to the efficiency of an asset or security that can be converted into ready cash (Gallego-Álvarez & Pucheta-Martínez, 2020).	Annual report	Total Current Assets / Total Current Liabilitiy (Gallego-Alvarez & Pucheta-Martinez, 2020)

Table 2. Statistical Descriptive (all: 66 data observations)

Variabel	Minimum	Maximum	Mean	Std. Deviation
ESG	1.49	6.42	3.49	1.27
PCON	0.00	5.51	1.90	1.96
FOREIGN _OWN	0.00	50.00	19.19	14.77
DOM_OWN	0.00	96.43	74.94	23.96
E_QUALITY	-17.44	31.27	2.49	6.69
SIZE	10.17	30.79	16.93	4.66
F_PERF	0.00	1.37	0.50	0.32
LEV	0.03	3.11	0.66	0.48
LIQ	0.31	7.15	1.65	1.16

Source: Output SPSS 25, 2023

Note. **ESG** data was obtained from Bloomberg. **PCON** (political connection) was obtained from the Transparency International Indonesia report titled "Corporate Political Engagement Index 2021: Assessment of Political Engagement in Steam Power Plant Companies (PLTU)." **FOREIGN_OWN** (foreign ownership) is measured using the percentage of foreign ownership listed in each company's annual report. **DOM_OWN** (domestic ownership) is measured using the percentage of domestic ownership listed in each company's annual report. **E_QUALITY** (earnings quality) is measured using the ratio of cash flow from operations to net income (Penman, 2001). **F_PERF** (financial performance) is measured using the ROA ratio (Subramanyam & Wild, 2014). **SIZE** (company size) is measured using the formula Ln (total assets) (Gallego-Alvarez & Pucheta-Martinez, 2020). **LEV** (leverage) is measured using the ratio of total debt to total assets (Subramanyam & Wild, 2014). **LIQ** (liquidity) is measured using the ratio of current assets to current liabilities (Gallego-Alvarez & Pucheta-Martinez, 2020).

88.8% of the variation in the dependent variable was explained by the independent variable in hypothesis H_{2b}. This finding is supported by the graphic shown in Figure 1. Figure 1 illustrates the relationship between foreign ownership and domestic ownership as a moderate variable with political engagement as independent variable and ESG disclosure as a dependent variable. It can be seen that, foreign ownership and domestic ownership can weaken the negative relationship between political engagement and ESG disclosure.

Table 5 shows the results of hypothesis testing for H_{3a}, H_{3b}, and H_{3c}. Based on the table, it could be concluded that: **1) Direct Effect**: Corporate political engagement had a significant negative impact on ESG disclosure. This was consistent with the findings of Hung et al. (2018). **2) Indirect effect**, namely Corporate political engagement (PCON) had a significance value of 0.047 with a coefficient β of -0.392 on earnings quality (E_QUALITY). Based on this, it could be concluded that corporate political engagement (PCON) had a significant negative effect on earnings quality (E_QUALITY). This aligns with the research conducted by Abdul Wahab et al. (2020) and Chaney et al. (2011) and Harymawan & Nowland (2016); Earnings quality (E_QUALITY) had a significance value (a) of 0.014 with a coefficient β of -0.352 on ESG disclosure (ESG). Based on this, it could be concluded that earnings quality (E_QUALITY) had a significant negative effect on ESG disclosure (ESG). This result indicates that Hypothesis H3b has been rejected. However, even so, the test results are consistent with the research conducted by Francis et al. (2008). **3) Total effect** of the intervening variable, namely a) Corporate political engagement (PCON) had a significance value (a) of 0.261 with a coefficient β of 0.226 on ESG disclosure (ESG). Based on this, it could be concluded that there was no statistically significant effect between corporate political engagement (PCON) and ESG disclosure (ESG). b) Earnings quality (E_QUALITY) had a significance value of (a) 0.195 with a coefficient β of -0.258 on ESG disclosure (ESG). Based on this, it could be concluded that there was no statistically significant effect between corporate political engagement (PCON) and ESG disclosure (ESG). According to Baron & Kenny (1986), there are three conditions that must be met by a variable for it to be considered a mediator. In this study, one of these conditions could not be met. Therefore, considering this, it could be concluded that earnings quality could not act as a mediating/intervening variable in this study, so Hypothesis H_{3c} in this study was rejected.

Corporate Political Engagement & ESG

The first hypothesis, which posits that corporate political engagement has a significant negative effect on ESG disclosure, is statistically supported. This study aligns with the research conducted by Hung et al. (2018). According to Hung et al. (2018), there are two mechanisms that differentiate the level of voluntary disclosure between political-

Table 3. First Hypothesis testing

Environment, Social, & Governance (ESG)	Expected Result	*Standardized Coefficients Beta*	t	Sig.
PCON	-	-0.274	-2.107	0.039
SIZE		-0.092	-0.702	0.485
F_PERF		0.337	2.585	0.012
LEV		-0.183	-1.435	0.157
LIQ		0.296	-2.530	0.014
R^2 (overall)				0.4102

Source: Output SPSS 25, 2023

Table 4. The Result of *Moderated Regression Analysis (MRA)*

Variabel	Model 2		Model 3	
	Coef. **B**	Sig	Coef. **β**	Sig
PCON	**-0.182**	**0.044**	**-0.867**	**0.000**
FOREIGN_OWN	**-0.063**	0.000		
DOM_OWN			**-0.291**	0.042
SIZE	**-1.348**	0.000	0.429	0.217
F_PERF	**0.976**	0.124	-0.144	0.001
LEV	**-0.177**	0.655	0.043	0.145
LIQ	**-0.457**	0.866	-0.694	0.825
PCON*FOREIGN_OWN	**0.004**	**0.046**		
PCON*DOM_OWN			**0.024**	**0.000**

Source: Output SPSS 25, 2023

Notes. Testing the moderation variables uses a significance level of α = 5%. Model 2 tests the influence of the foreign ownership moderation variable, while model 3 tests influence of the domestic ownership moderation variable.

ly involved companies and those not involved in politics, which are the role of capital market incentives and the litigation risk. Capital market incentives have significant role in voluntary disclosure made by companies. This occurs due to the demand for transparency is often associated with the development of capital markets (Hung et al., 2018). Research conducted by Faccio et al. (2006) shows that companies which engaged with political activities often received a corporate bailout from government rather than from capital market therefore reduce the capital market incentives. The lower the capital market incentives, the lower the demand for transparency for companies, particulary in this research refers to ESG disclosure. As for the second role, according to (Hung et al., 2018), one of the benefits from voluntary disclosure is mitigating litigation risk which is very crucial for industries with high litigation risk. Politically engaged companies tend to have lower litigation risk. This argument is supported by research conducted by Jia et al. (2019). The research shows that politically engaged companies often receives favouritism in the court. Company's political connection enabling them to acces the byrocratic system which can affect the final decision, hence made the business confict easier to resolve (Jia et al., 2019). Additionally, according to reports published by Indonesia Corruption Watch (ICW) in 2021 titled "Public Examination of Riau-1 Power Plant Corruption Case" clearly described how the favouritism practic often occurred in Power Plant companies due to their high politic-business relation in Power Plant sector (Anandya et al., 2021). Based on those arguments, it can be concluded that low financial needs from capital market and low litigation risk lead politically engaged companies to not prioritize ESG disclosure (Hung et al., 2018).

The results of testing the first hypothesis align with resource dependence theory, which explains that every company must have access to resources to survive and thrive (Dicko et al., 2020). This necessitates companies relying on their social connections (Dicko et al., 2020). According to Dicko et al. (2020), companies engaged in

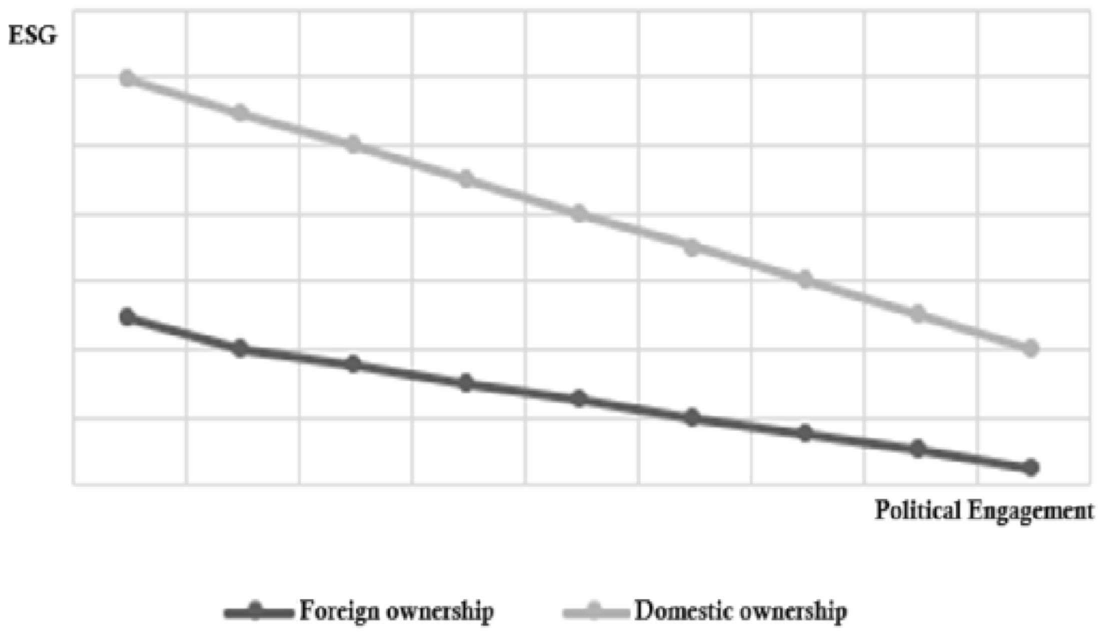

Figure 1. Moderating Effect of Ownership Structure & Political Engagement

Table 5. The Result of *Path Analysis*

Independen Variable	Dependen Variable	Coefficient Path	Direction	t	Sig.
Direct Relationship (Model 4)					
PCON	ESG	-0.274	Negative	-2.107	0.039
Indirect Relationship (Model 5)					
PCON	E_QUALITY	-0.392	Negative	-2.081	0.047
E_QUALITY	ESG	-0.352	Negative	-2.571	0.014
Total Effect (Model 6)					
PCON	ESG	0.226	Positive	1.151	0.261
E_QUALITY		-0.258	Negative	-1.332	0.195

Source: Output SPSS 25, 2023

Notes. All tests were conducted by including the control variables predetermined by the reseacher, and the testing was performed at a significance level of 5%.

politics can leverage their political connections to gain access to key external resources, enabling them to survive and grow. Therefore, politically engaged companies do not feel any urgency to engage in voluntary disclosure practices such as ESG (Dicko et al., 2020; Hung et al., 2018). Additionally, in Indonesia, political connections are often utilized to gain a competitive edge in business competition (Transparency International, 2018). Moreover, the electricity sector is particularly susceptible to conflicts of interest due to the presence of individuals holding active public office or who are affiliated with those in such positions (politically-exposed persons) who own power plant businesses (Transparency International, 2018).

Corporate Political Engagement, ESG, & Ownership Structure

The second hypothesis proposed in this study, which suggests that the ownership structure (foreign ownership & domestic ownership), can weaken the negative relationship between corporate political engagement and ESG disclosure, is statistically supported. This research aligns with the findings of Amosh (2022) and Fuadah et al. (2022). Amosh (2022) suggests that the foreign expertise made available by foreign ownership can enhance sustainability practices, such as ESG disclosure, particularly in emerging economies. Fuadah et al. (2022) add that ESG disclosure can also be used as a legitimacy strategy by management to attract capital inflows from foreign entities, as foreign investors often use ESG disclosure as an indicator to assess a company's sustainability. Therefore, the presence of foreign ownership can enhance ESG disclosure (Amosh, 2022; Fuadah et al., 2022), even when the company is politically connected. Similarly, domestic ownership can also enhance ESG disclosure in companies (Amosh, 2022; Khan et al., 2013). Domestic ownership refers to the number of shares owned by founders (including family and affiliated parties), domestic companies, institutional investors, and the general public (Choi et al., 2011, 2012). According to Khan et al. (2013), when a company is allowed to be publicly owned, public accountability becomes crucial for the company. Therefore, such companies tend to disclose more comprehensive information, due to the transparency and accountability issues arising from having numerous stakeholders (Khan et al., 2013). This finding is supported by the numerous company samples that have high political and ESG scores. ABB Ltd is an example, which, based on Transparency International Indonesia's analysis, has a political score of 4.97/10 and an ESG score of 6.42/10, the second-highest scores in this study's sample. Moreover, 86.11% of ABB Ltd's shares are owned domestically. This strengthens the research finding that the ownership structure can enhance ESG disclosure, regardless of the company's political engagement (Khan et al., 2013; Amosh, 2022; Fuadah et al., 2022).

Corporate Political Engagement, ESG, & Earnings Quality

Based on the research sample, out of 22 companies, only six have good earnings quality. This indicates that almost all the companies involved in politics have poor earnings quality. According to Francis et al. (2008), from an empirical perspective, poor earnings quality can have negative impacts on a company, such as high cost of capital and the possibility of legal claims. In contrast to companies not engaged in politics, those engaged in politics may not face the negative consequences of poor earnings quality (Chaney et al., 2011). This is because the creditors of companies engaged in politics often provide capital to the company regardless of its poor earnings quality (Chaney et al., 2011). Furthermore, its creditors may not impose penalties on the company due to political pressure, especially in the case of government-owned banks (Chaney et al., 2011). Therefore, one of the main reasons for the poor earnings quality of companies involved in politics is the absence of penalties being imposed on them (Chaney et al., 2011). In Indonesia, especially during the New Order era, political connections played a crucial role for companies (Yazid & Angelica, 2021). This argument is supported by Leuz & Oberholzer-Gee (2006), who found that companies with strong ties to President Soeharto tended to have poor earnings quality.

Companies with high earnings quality also tend to avoid voluntary disclosures, such as ESG. This argument is supported by Francis et al. (2008). Francis et al. (2008) used earnings quality as a proxy for information asymmetry between management and shareholder. Negative relationship between earnings quality and voluntary disclosure occurs when there are different information and interest between management and shareholder (Francis et al., 2008). When this situation occurs, shareholder tend to push the company to disclose voluntary disclosure (particulary ESG) (Francis et al., 2008). This is done because voluntary disclosure can mitigate information asymmetry in the market, therefore company with high information asymmetry tend to increase it's voluntary disclosure (Francis et al., 2008). In contrast with company's with low earnings quality, company's with high earnings quality indicates lower information asymmetery between management and shareholder (Francis et al., 2008). Therefore, the company tend to not report voluntary disclosure (Francis et al., 2008).

Even though there are both negative and positive relationships between corporate political engagement, earnings quality, and ESG disclosure, statistically, earnings quality cannot mediate the relationship between corporate political engagement and ESG disclosure. This is due to the conditions stated by Baron & Kenny (1986). According to Habib & Hossain (2013), non-financial characteristics such as managerial and strategic factors could be more dominant in influencing voluntary disclosure than financial characteristic. Political engagement could be interpreted as a characteristic or attribute that is attached to higher-level management or a corporation's strategic (Faccio et al., 2006). As mentioned above, ESG disclosure is influenced significantly by political engagement. This can be interpreted that strategic factors (such as political engagement) play a crucial role rather than earnings quality in deciding a corporation's voluntary disclosure (particularly in this research ESG disclosure). This argument is also supported by Chaney et al. (2011) which stated that corporations with high political engagement often receive a bailout regardless of their poor earnings quality. Based on these arguments, it can be concluded that ESG disclosure is influenced by political interest or reputation considerations related to political engagement, therefore earnings quality does not serve as a mediating variable.

CONCLUSIONS

This research has several research objectives. First, to analyze the relationship between corporate political engagement and ESG disclosure. The result shows that corporate political engagement has a significant negative impact on ESG disclosure, which align with the resource dependence theory that suggests companies must depend on their social connections, including political connections, to thrive and survive. Moreover in Indonesia, the electricity sector is particularly susceptible to conflicts of interest due to the presence of individuals holding active public office or who are affiliated with those in such positions (politically exposed persons) who own power plant businesses (Transparency International, 2018). The second research objective is to analyze the relationship between corporate political engagement and ESG disclosure with ownership structure as a moderate variable. Results show that foreign ownership and domestic ownership can weaken the negative relationship between corporate political engagement and ESG disclosure. These findings is supported by Amosh (2022) and Fuadah et al. (2022)social, and governance (ESG, which said that foreign investors often use ESG disclosure as an indicator to assess a company's sustainability. Therefore, the presence of foreign ownership can enhance ESG disclosure, even when the company is politically connected. Whereas for domestic ownership, according to Khan et al. (2013), when a company is allowed to be publicly owned, public accountability becomes crucial for the company. Therefore, such companies tend to disclose more comprehensive information, due to the transparency and accountability issues arising from having numerous stakeholders (Khan et al., 2013). The third research objective is to analyze the relationship between corporate political engagement and ESG disclosure with earnings quality as an intervening variable. Results show that earnings quality cannot mediate the influence of corporate political engagement on ESG disclosure. According to Habib & Hossain (2013), non-financial characteristics such as managerial and strategic factors (particularly political engagement in this research) could be more dominant in influencing voluntary disclosure than financial characteristics. Thus, political engagement has a direct influence to ESG disclosure through strategic factors without the necessity of earnings quality as a mediate variable.

This study has several limitations. First, the sample for this research consisted of steam power plant (PLTU) companies obtained from the Transparency International Indonesia's 2021 report titled "Corporate Political Engagement Index 2021: Assessment of Corporate Political Engagement in Steam Power Plants (PLTU)." This resulted in a relatively small sample size. Additionally, the researcher acknowledges that the steam power plant industry is heavily regulated. Therefore, future research could consider using industries with fewer regulations and conduct a comparative study between highly regulated and less regulated industries. Finally, since ESG disclosure is also influenced by the legal system of a country, future research may consider conducting a multi-country analysis by including legal system variables.

REFERENCES

Abdul Wahab, E. A., Jamaludin, M. F., Agustia, D., & Harymawan, I. (2020). Director Networks, Political Connections, and Earnings Quality in Malaysia. *Management and Organization Review*, *16*(3), 687–724. https://doi.org/10.1017/mor.2020.26

Al-Hadi, A., Al-Yahyaee, K. H., Hussain, S. M., & Taylor, G. (2018). Market risk disclosures, corporate governance structure and political connections: evidence from GCC firms. *Applied Economics Letters*, *25*(19), 1346–1350. https://doi.org/10.1080/13504851.2017.1420877

Amosh, H. Al. (2022). *Ownership structure and environmental , social and governance performance disclosure : the moderating role of the board independence*. *2*(1), 49–66. https://doi.org/10.1108/JBSED-07-2021-0094

Anandya, D., Ramadhana, K., & Easter, L. (2021). Eksaminasi Publik Kasus Korupsi PLTU Riau-1. *Indonesia Corruption Watch*. https://antikorupsi.org/id/article/eksaminasi-publik-kasus-korupsi-pltu-riau-1

Baron, R. M., & Kenny, D. A. (1986). The moderator-mediator variable distinction in social psychological research: Conceptual, strategic, and statistical considerations. *Journal of Personality and Social Psychology*, *51*(6), 1173–1182. https://doi.org/10.1037//0022-3514.51.6.1173

Boubakri, N., Guedhami, O., Mishra, D., & Saffar, W. (2012). Political connections and the cost of equity capital. *Journal of Corporate Finance*, *18*(3), 541–559. https://doi.org/10.1016/j.jcorpfin.2012.02.005

Bunkanwanicha, P., & Wiwattanakantang, Y. (2009). Big Business Owners in Politics. *The Review of Financial Studies*, *22*(6), 2133–2168. https://www.jstor.org/stable/30225712

Chaney, P. K., Faccio, M., & Parsley, D. (2011). The quality of accounting information in politically connected firms. *Journal of Accounting and Economics*, *51*(1–2), 58–76. https://doi.org/10.1016/j.jacceco.2010.07.003

Chen, H., Kuo, T., & Chen, J. (2022). Impacts on the ESG and financial performances of companies in the manufacturing industry based on the climate change related risks. *Journal of Cleaner Production*, *380*(P1), 134951. https://doi.org/10.1016/j.jclepro.2022.134951

Chen, V. Z., Li, J., Shapiro, D. M., & Zhang, X. (2014). Ownership structure and innovation: An emerging market perspective. *Asia Pacific Journal of Management*, *31*(1), 1–24. https://doi.org/10.1007/s10490-013-9357-5

Cheng, Z., Wang, F., Keung, C., & Bai, Y. (2017). Will Corporate Political Connection Influence the Environmental Information Disclosure Level? Based on the Panel Data of A-Shares from Listed Companies in Shanghai Stock Market. *Journal of Business Ethics*, *143*(1), 209–221. https://doi.org/10.1007/s10551-015-2776-0

Choi, S. B., Lee, S. H., & Williams, C. (2011). Ownership and firm innovation in a transition economy: Evidence from China. *Research Policy*, *40*(3), 441–452. https://doi.org/10.1016/j.respol.2011.01.004

Choi, S. B., Park, B. Il, & Hong, P. (2012). Does Ownership Structure Matter for Firm Technological Innovation Performance? The Case of Korean Firms. *Corporate Governance: An International Review*, *20*(3), 267–288. https://doi.org/10.1111/j.1467-8683.2012.00911.x

Chouaibi, S., Chouaibi, J., & Rossi, M. (2022). ESG and corporate financial performance: the mediating role of green innovation: UK common law versus Germany civil law. *EuroMed Journal of Business*, *17*(1), 46–71. https://doi.org/10.1108/EMJB-09-2020-0101

Dicko, S., Khemakhem, H., & Zogning, F. (2020). Political connections and voluntary disclosure: the case of Canadian listed companies. *Journal of Management and Governance*, *24*(2), 481–506. https://doi.org/10.1007/s10997-019-09471-3

Duque, E., Javier, G., & Caracuel, A. (2021). Environmental , Social and Governance (ESG) Scores and Financial Performance of Multilatinas : Moderating Effects of Geographic International Diversification and Financial Slack. *Journal of Business Ethics*, *168*(2), 315–334. https://doi.org/10.1007/s10551-019-04177-w

Environmental Protection Agency. (2023). *Climate Change Impacts on Energy*. Environmental Protection Agency United States. https://www.epa.gov/climateimpacts/climate-change-impacts-energy#:~:text=The Link Between Energy and,pose safety risks to people.

European Commision. (2023). *Causes of Climate Action*. European Commision. https://climate.ec.europa.eu/climate-change/causes-climate-change_en#:~:text=Burning fossil fuels%2C cutting down,greenhouse effect and global warming.

Faccio, M., Masulis, R. W., Mcconnell, J. J., Faccio, M., Masulis, R. W., & Mcconnell, J. J. (2006). *Political Connections and Corporate Bailouts Published by : Wiley for the American Finance Association Stable URL : https://www.jstor.org/stable/4123440 Political Connections and Corporate Bailouts*. *61*(6), 2597–2635.

Fahad, & Nidheesh. (2020). Determinants of CSR disclosure: an evidence from India. *Journal of Indian Business Research*, *13*(1), 110–133. https://doi.org/10.1108/JIBR-06-2018-0171

Francis, J., Nanda, D., & Olsson, P. (2008). Voluntary disclosure, earnings quality, and cost of capital. *Journal of Accounting Research*, *46*(1), 53–99. https://doi.org/10.1111/j.1475-679X.2008.00267.x

Fuadah, L. L., Mukhtaruddin, M., Andriana, I., & Arisman, A. (2022). *The Ownership Structure , and the Environmental , Social , and Governance (ESG) Disclosure , Firm Value and Firm Performance : The Audit Committee as Moderating Variable*.

Gallego-Álvarez, I., & Pucheta-Martínez, M. C. (2020). How cultural dimensions, legal systems, and industry affect environmental reporting? Empirical evidence from an international perspective. *Business Strategy and the Environment*, *29*(5), 2037–2057. https://doi.org/10.1002/bse.2486

Gillan, S. L., Koch, A., & Starks, L. T. (2021). Firms and social responsibility: A review of ESG and CSR research in corporate finance. *Journal of Corporate Finance*, *66*(September 2019), 101889. https://doi.org/10.1016/j.jcorpfin.2021.101889

Habib, A., & Hossain, M. (2013). CEO/CFO characteristics and financial reporting quality: A review. *Research in Accounting Regulation*, *25*(1), 88–100. https://doi.org/10.1016/j.racreg.2012.11.002

Harymawan, I., & Nowland, J. (2016). Political connections and earnings quality: How do connected firms respond to changes in political stability and government effectiveness? *International Journal of Accounting and Information Management*, *24*(4), 339–356. https://doi.org/10.1108/IJAIM-05-2016-0056

Hölzer, M., Loy, T., Zimmermann, J., & Hölzer, M. (2022). *Policy Uncertainty , Earnings Management and the Role of Political Connections*. 1–46.

Houqe, M. N., & Islam, T. F. (2011). Measuring earnings quality: Evidence from New Zealand. *Corporate Board: Role, Duties and Composition*, *7*(1), 24–32. https://doi.org/10.22495/cbv7i1art2

Hung, M., Kim, Y., & Li, S. (2018a). Political connections and voluntary disclosure: Evidence from around the world. *Journal of International Business Studies*, *49*(3), 272–302. https://doi.org/10.1057/s41267-017-0139-z

Hung, M., Kim, Y., & Li, S. (2018b). Political connections and voluntary disclosure: Evidence from around the world. *Journal of International Business Studies*, *49*(3), 272–302. https://doi.org/10.1057/s41267-017-0139-z

Javadi, S., & Masum, A. Al. (2021). The impact of climate change on the cost of bank loans. *Journal of Corporate Finance*, *69*(June), 102019. https://doi.org/10.1016/j.jcorpfin.2021.102019

Jia, N., Mao, X., & Yuan, R. (2019). Political connections and directors ' and officers ' liability insurance – Evidence from China. *Journal of Corporate Finance*, *58*(June), 353–372. https://doi.org/10.1016/j.jcorpfin.2019.06.001

Kahn, M. E., Mohaddes, K., Ng, R. N. C., Pesaran, M. H., Raissi, M., Yang, J.-C., Batini, N., Cashin, P., Dybczak, K., Eble, S., Garcia-Macia, D., Hallegatte, S., Hasna, Z., Hassler, J., Jajko, B., Jaumotte, F., Kpodar, R., Moses, A. L., Phillips, P., … Tol, R. (2019). Long-Term Macroeconomic Effects of Climate Change: A Cross-Country Analysis IMF Working Paper Fiscal Affairs Department Long-Term Macroeconomic Effects of Climate Change: A Cross-Country Analysis * We are grateful to. *IMF Working Paper*.

Khan, A., Muttakin, M. B., & Siddiqui, J. (2013). *Corporate Governance and Corporate Social Responsibility Disclosures : Evidence from an Emerging Economy*. 207–223. https://doi.org/10.1007/s10551-012-1336-0

Leuz, C., & Oberholzer-Gee, F. (2006). Political relationships, global financing, and corporate transparency: Evidence from Indonesia. *Journal of Financial Economics*, *81*(2), 411–439. https://doi.org/10.1016/j.jfineco.2005.06.006

Muttakin, M. B., Mihret, D. G., & Khan, A. (2018). Corporate political connection and corporate social responsibility disclosures: A neo-pluralist hypothesis and empirical evidence. *Accounting, Auditing and Accountability Journal*, *31*(2), 725–744. https://doi.org/10.1108/AAAJ-06-2015-2078

Nekhili, M. (2021). *The ESG – financial performance relationship : Does the type of employee board representation matter ? November 2019*, 134–161. https://doi.org/10.1111/corg.12345

Ozili, P. K. (2020). Financial reporting under economic policy uncertainty. *Journal of Financial Reporting and Accounting*, *19*(2), 325–338. https://doi.org/10.1108/JFRA-08-2020-0242

Penman, S. H. (2001). *Financial Statement Analysis & Security Valuation*. McGraw-Hill Book.

Subramanyam, K. R., & Wild, J. J. (2014). *Analisis Laporan Keuangan*. Salemba Empat.

Tee, C. M., & Kasipillai, J. (2022). Female directors' monitoring and earnings quality: the moderating effect of political connections and family ownership. *International Journal of Manpower*, *43*(5), 1085–1107. https://doi.org/10.1108/IJM-02-2021-0101

Transparency International. (2018). *Corporate Political Engagement Index 2018*. https://www.transparency.org.uk/corporate-political-engagement-index

Wade, K., & Jennings, M. (2016). The impact of climate change on the global economy. *Schroders*, *page 8*, 1–12. https://www.schroders.com/en/us/institutional/insights/economic-views3/the-impact-of-climate-change-on-the-global-economy/

Yazid, F., & Angelica, B. (2021). *Corporate Political Engagement Index 2021*. https://www.transparency.org.uk/publications/corporate-political-engagement-index-2015