

The Impact of Good Corporate Governance on the Quality of Sustainability Reports

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ABSTRACT

This research aims to examine the effect of Good Corporate Governance (GCG) on the quality of Sustainability Reports (SR). The population for this study consists of energy companies listed on the Indonesia Stock Exchange (IDX) in 2023. The sample was determined using purposive sampling, resulting in a total of 143 companies. Legitimacy theory is used to explain the findings. Data analysis was performed using multiple linear regression. The results show that the proportion of independent commissioners, the frequency of audit committee meetings, and the proportion of managerial ownership positively affect the quality of SR. Conversely, the size of the board of directors negatively affects the quality of SR.

Keywords: Sustainability report quality; proportion of independent commissioner; audit committee meetings; proportion of managerial ownership; board size.

Pengaruh Good Corporate Governance Pada Kualitas Sustainability Report

ABSTRAK

Penelitian ini bertujuan untuk menguji pengaruh Good Corporate Governance (GCG) pada kualitas Sustainability Report (SR). Populasi dalam penelitian ini adalah perusahaan energi yang terdaftar di BEI pada tahun 2023. Penentuan sampel menggunakan purposive sampling dan diperoleh total sampel sebanyak 143. Penelitian ini menggunakan teori legitimasi dalam menjelaskan hasil temuan. Analisis data menggunakan regresi linear berganda. Hasil analisis menunjukkan variabel proporsi komisaris independen, pertemuan komite audit dan proporsi kepemilikan manajerial berpengaruh positif pada kualitas SR. Sedangkan variabel ukuran dewan direksi berpengaruh negatif pada kualitas SR.

Kata Kunci: Kualitas Sustainability Report; Proporsi Komisaris Independen; Pertemuan Komite Audit; Proporsi Kepemilikan Manajerial; Ukuran Dewan Direksi.

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INTRODUCTION

This research aims to determine the influence of Good Corporate Governance (GCG) on the quality of Sustainability Reports (SR) produced by energy sector companies listed on the Indonesia Stock Exchange (IDX) in 2023. A quality SR is defined as one that aligns with the Global Reporting Initiative (GRI) standards (Madona & Khafid, 2020). Given the energy sector's sensitivity to social and environmental issues, it is crucial for these companies to publish high-quality SRs to maintain public trust and gain legitimacy from stakeholders. Public trust in the energy sector is influenced by transparency, ethics, and accountability – key principles of GCG (Edelman, 2023).

Legitimacy theory has been employed in several studies analyzing the impact of GCG on SR quality, including those by e.g., (Aniktia *et al.*, 2015), (Lucia & Panggabean, 2018), (Dewi & Ramantha, 2021), (Ardiani *et al.*, 2022), (Razaq *et al.*, 2023). Legitimacy theory explains the social contract between a company and its community (Fuadah & Safitri, 2018). The discrepancy between a company's activities and the community's expectations is referred to as the legitimacy gap. This gap arises when there is a misalignment between what the company does and what the community perceives and expects (Adel *et al.*, 2019). In corporate sustainability, a legitimacy gap can occur due to insufficient information about the company's social, economic, and environmental activities, leading to negative perceptions that the company is indifferent to social and environmental issues (Fuadah & Safitri, 2018). Thus, disclosing detailed information about these activities is essential for improving public perception and gaining legitimacy.

Previous research has measured SR quality using the Sustainability Report Disclosure Index (SRDI), as seen in studies by e.g., (Aniktia *et al.*, 2015), (Ardiani *et al.*, 2022), (Dewi & Pitriasari, 2019), (Madona & Khafid, 2020). This method assigns a value to each disclosure, and the total value is divided by the expected total value of disclosures. However, not all disclosures in an SR are of high quality; some may be formalities or lack evidence and truthfulness. To enhance previous research, this study assesses SR quality using an evaluation score based on Ekaputri & Eriandani (2022), with modifications. These modifications account for the fact that elements like photos and graphics are supplementary and can be part of systematic manipulation to enhance reader impressions (GRI, 2002). This evaluation score aims to consider the breadth and nature of the disclosed information, whether qualitative or quantitative.

Good Corporate Governance (GCG) can regulate the relationships among stakeholders, managers, the government, and shareholders to control the company effectively (Nataliantari *et al.*, 2020). The principles of GCG are optimally implemented when the key organs in the company's management function effectively. Effective application of GCG principles by the company's management encourages transparent disclosure of information to the public, thereby enhancing the quality of the company's Sustainability Report (SR) (Aziz, 2014). The GCG proxies used as independent variables in this study include the proportion of independent commissioners, the frequency of audit committee meetings, the proportion of managerial ownership, and the size of the board of directors (Ardiani *et al.*, 2022; Madona & Khafid, 2020). The study also uses control variables such as company size, perception of environmental reputation, and company age.

The proportion of independent commissioners is the number of independent commissioners relative to the total number of board commissioners (Wahyudi, 2021). Independent commissioners enhance the monitoring of company activities and increase transparency, thereby improving the quality of SR (Adel *et al.*, 2019). However, previous studies have shown inconsistent results. Research by Dewi *et al.* (2019), Madona & Khafid (2020) and Saepudin *et al.* (2021) found a negative relationship between the proportion of independent commissioners and SR quality. In contrast, studies by Novitaningrum *et al.* (2017) Razaq *et al.* (2023) and Putri *et al.* (2022) showed a positive relationship.

Companies with a higher number of independent commissioners are more motivated to disclose information about their sustainability efforts to the public. Independent commissioners bring new perspectives and ideas related to SR, enhancing their understanding and oversight of SR quality (Dewi & Pitriasari, 2019). Increased disclosure of information in the SR can help the company gain legitimacy from the public (Rudyanto & Siregar, 2018).

H₁: The proportion of independent commissioners positively influences the quality of SR.

Audit committee meetings refer to the gatherings held by the audit committee over the course of a year (Ardiani *et al.*, 2022). According to research by Lucia *et al.* (2018) and Wahyudi, (2021), these meetings negatively impact the quality of Sustainability Reports (SR) produced by companies. Conversely, studies by Aniktia *et al.* (2015), Ardiani *et al.* (2022), Dewi *et al.* (2021) and Ruhana *et al.* (2021) indicate that audit committee meetings positively influence SR quality.

Audit committee meetings are crucial for ensuring the completeness, timeliness, and integrity of sustainability reports (Buallay & Al-Ajmi, 2020). An increasing frequency of meetings can enhance coordination among members, thus improving oversight of management performance and optimizing the effectiveness of SR preparation (Ruhana & Hidayah, 2020).

H₂: Audit committee meetings positively influence the quality of SR.

The proportion of managerial ownership refers to the shares owned by management compared to the total shares outstanding (Setyawan *et al.*, 2018). Research by Ardiani *et al.* (2022), Razaq *et al.* (2023) and Saepudin *et al.* (2021) shows that the proportion of managerial ownership positively affects SR quality. Similarly, studies by Novitaningrum & Amboningtyas (2017), Madona & Khafid (2020) and Tijjani *et al.* (2023) also demonstrate a positive influence of managerial ownership on SR quality.

Managerial share ownership can increase management's motivation to disclose the company's activities, as managers who own shares tend to be more attentive to sustainability issues (Nurhalisa & Hernawati, 2023). Enhanced information disclosure leads to higher quality SRs, helping the company gain legitimacy from the public (Madona & Khafid, 2020).

H₃: The proportion of managerial ownership positively influences the quality of SR.

The board of directors is responsible for formulating policies essential for the company's operational activities (Dewi *et al.*, 2021). Research by Kalbuana *et al.*, (2022), Kilic (2019), Lucia & Panggabean (2018), and Wahyudi (2021) suggests that the size of the board of directors negatively affects SR quality. In contrast,

studies by Correa *et al.* (2020), Razaq *et al.* (2023), Trisnawati *et al.* (2022) and Dewi *et al.* (2021) show a positive influence of board size on SR quality.

A larger board of directors can prevent decision-making from being dominated by a single party, which can help produce SRs that meet stakeholder expectations and enhance the company's accountability (Ardiani *et al.*, 2022). More members on the board provide diverse perspectives, leading to more comprehensive and thorough considerations in preparing SRs (Trisnawati *et al.*, 2022).

H₄: The size of the board of directors positively influences the quality of SR.

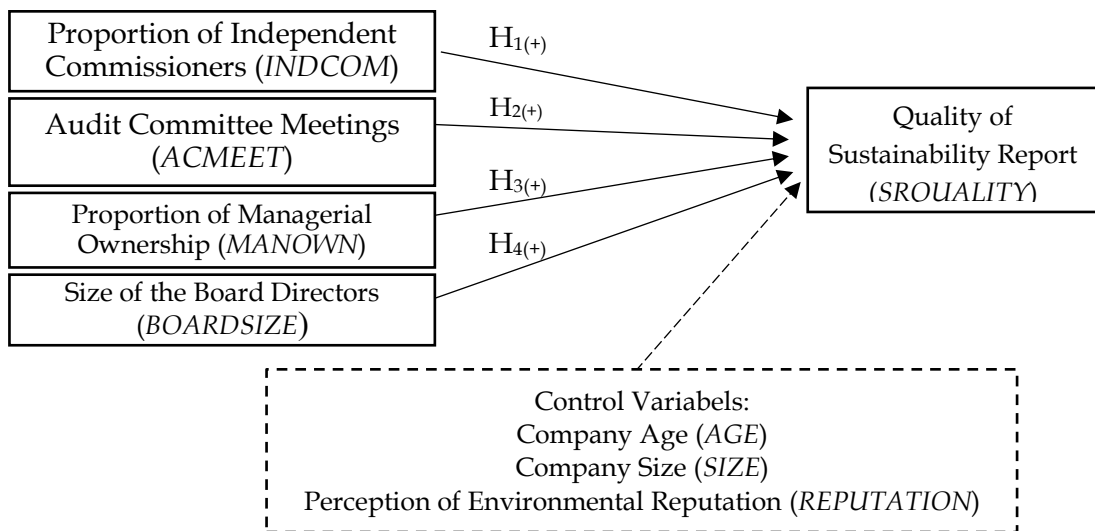


Figure 1. Research Model

Source: Research Data, 2021

RESEARCH METHODS

The population of this study comprises energy sector companies listed on the Indonesia Stock Exchange (IDX) in 2023. The secondary data utilized includes sustainability reports and annual reports. The research sample was selected using a purposive sampling method, focusing on energy companies listed on the IDX in 2023 that publish both sustainability and annual reports on either the IDX or the company's official website. A total of 40 companies satisfied these criteria.

The dependent variable, the quality of the sustainability report (SRQUALITY), is measured using an assessment score. This study employs sustainability indicator items from the GRI Standards 2021. Each sustainability indicator disclosed by the companies, based on the GRI Standards 2021, is evaluated using an assessment score adapted from the research by Ekaputri and Eriandani (2022), with some modifications. These modifications were necessary because photos or graphics, while complementary to written information, can often manipulate reader impressions. The assessment score was also adjusted to include limits for both brief and comprehensive disclosures.

Table 1. Assessment Scores

Assessment Scores	Description
0	No disclosure
1	Disclosure of sustainability indicators with a brief explanation (1-5 sentences)
2	Disclosure of sustainability indicators with a complete explanation (more than 5 sentences)
3	Disclosure of sustainability indicators with a brief explanation (1-5 sentences) accompanied by quantitative data
4	Disclosure of sustainability indicators with a complete explanation (more than 5 sentences) accompanied by quantitative data
5	Disclosure of sustainability indicators with a complete explanation (more than 5 sentences) accompanied by quantitative data, including costs incurred and photos/graphics (optional)

Source: Research Data, 2024

The quality of the SR is calculated using the natural logarithm of the total score to reduce excessive data fluctuations. The formula for calculating the SR quality in this study is as follows:

$$SRQUALITY = \ln(\text{Total Score}) \dots \dots \dots (1)$$

The independent variables consist of the proportion of independent commissioners, audit committee meetings, the proportion of managerial ownership, and the size of the board of directors. The proportion of independent commissioners (INDCOM) is measured using the following formula: (Nuraeni & Darsono, 2020):

$$INDCOM = \frac{\text{number of independent commissioners}}{\text{total number of commissioners}} \dots \dots \dots (2)$$

Audit committee meetings (ACMEET) are measured by the number of audit committee meetings held in one year (Ardiani *et al.*, 2022).

Managerial ownership proportion (MANOWN) is calculated using the following formula (Aniktia *et al.*, 2015):

$$MANOWN = \frac{\text{number of shares owned by management}}{\text{total number of outstanding shares}} \dots \dots \dots (3)$$

Board size (BOARDSIZE) is measured based on the number of board members (Correa *et al.*, 2020).

Control variables consist of company age (AGE), company size (SIZE), and environmental reputation perception (REPUTATION). Company age is measured using the following formula (Sandy & Ardiana, 2023):

$$AGE = \text{year of observation} - \text{year the company was founded} \dots \dots \dots (4)$$

Company size (SIZE) is measured using the natural logarithm of total assets (Kalbuana *et al.*, 2022).

$$SIZE = \ln(\text{Total Assets}) \dots \dots \dots (5)$$

Environmental reputation perception is measured by assigning a score of 1 to companies indexed in SRI-Kehati, and a score of 0 to those not indexed in SRI-Kehati (Sandy & Ardiana, 2023).

The research sample consists of energy companies listed on the Indonesia Stock Exchange (IDX) in 2023, totaling 143 observations based on specified criteria. Data collection involved downloading annual and sustainability reports from the

IDX website and company websites. Data analysis was conducted using multiple linear regression with the model equation:

$$SRQUALITY = \beta_0 + \beta_1 INDCOM_{i,t} + \beta_2 ACMEET_{i,t} + \beta_3 MANOWN_{i,t} + \beta_4 BOARDSIZE_{i,t} + \beta_5 AGE_{i,t} + \beta_6 SIZE_{i,t} + \beta_7 REPUTATION_{i,t} + \varepsilon_{i,t} \dots \dots \dots (6)$$

Keterangan:

<i>SRQUALITY</i>	= Sustainability report quality
β_0	= Constant
$\beta_1, \beta_2, \beta_3, \beta_4$	= Regression coefficients of independent and control variables
<i>INDCOM_{i,t}</i>	= Proportion of independent commissioners
<i>ACMEET_{i,t}</i>	= Audit committee meetings
<i>MANOWN_{i,t}</i>	= Proportion of managerial ownership
<i>BOARDSIZE_{i,t}</i>	= Board size
<i>AGE_{i,t}</i>	= Company age
<i>SIZE_{i,t}</i>	= Company size
<i>REPUTATION_{i,t}</i>	= Perception of environmental reputation
$\varepsilon_{i,t}$	= Residuals

RESULTS AND DISCUSSION

Descriptive statistical tests aim to determine the highest and lowest values of sustainability report (SR) quality, as well as other variables, among the sampled companies. These test results provide an illustration of the research data's characteristics. Descriptive statistics present the minimum and maximum values, mean (average), and standard deviation.

The company with the lowest SR quality score, 3.04, is PT. Rig Tenders Indonesia Tbk. Conversely, the highest SR quality score, 5.05, is attributed to PT. Perusahaan Gas Negara Tbk. The average SR quality score among the sampled companies is 4.21, with a standard deviation of 0.37.

Table 2. Descriptive Statistics

	Number of Observations	Minimum Value	Maximum Value	Mean Value	Value Standard Deviation
SRQUALITY	143	3.04	5.05	4.21	0.37
INDCOM	143	0.16	0.75	0.41	0.10
ACMEET	143	0.00	60.00	12.58	13.09
MANOWN	143	0.00	0.76	0.04	0.13
BOARDSIZE	143	2.00	11.00	5.03	2.02
AGE	143	6.00	57.00	31.75	13.32
SIZE	143	25.88	32.75	29.98	1.37
REPUTATION	143	0.00	1.00	0.09	0.29

Source: Research Data, 2024

Normality test using the Jarque-Bera (JB) test. Normality is detected by comparing the JB value with the Chi-Square table. If JB value < Chi-Square table value, then the residuals of the regression model are normally distributed (Hamid, 2020:89). The test results indicate JB value < Chi-Square table value (6.02733 < 171.906799). It is concluded that the regression model is normally distributed.

Table 3. Normality Test Results

N	143
Jarque-Bera	6.02733
Probability	0.049111

Source: Research Data, 2024

Autocorrelation test using the Correlogram of Residuals Test. There is no autocorrelation issue if all probability values of each observation are not significant at the 5% level (probability > 0.05). The test results indicate no autocorrelation symptoms because the probability values of all observations are > 0.05.

Table 4. Multicollinearity Test Results

Variable	Centered VIF
INDCOM	1.071
ACMEET	2.608
MANOWN	1.127
BOARDSIZE	1.573
AGE	1.363
SIZE	1.851
REPUTATION	2.506

Source: Research Data, 2024

The Variance Inflation Factor (VIF) values are used as a reference for decision-making in multicollinearity tests. There is no multicollinearity issue if the VIF value is < 10. The test results show the VIF values as follows: proportion of independent commissioners = 1.071, audit committee meetings = 2.608, managerial ownership proportion = 1.127, board size = 1.573, company age = 1.363, company size = 1.851, and environmental reputation perception = 2.506. All VIF values for variables are < 10, indicating no multicollinearity issue.

Table 5. Heteroskedasticity Test Results

F-Statistic	1.4742	Prob. F	0.0705
Obs*R-squared	44.1294	Prob. Chi-Square	0.0933
Scaled explained SS	47.2601	Prob. Chi-Square	0.0514

Source: Research Data, 2024

Heteroskedasticity test used is the White Test. There is no heteroskedasticity issue if Obs*R-squared has a Chi-Square probability value > 0.05. The test results indicate no heteroskedasticity symptoms because the Chi-Square probability value is 0.0933 > 0.05.

The influence of independent variables and control variables on SR quality in this study was analyzed using multiple linear regression. Below is the regression equation based on Table 2.

$$SRQUALITY = -0.398 + 0.739INDCOM + 0.016ACMEET + 0.054MANOWN - 0.004BOARDSIZE + 0.005AGE + 0.133SIZE - 0.558REPUTATION + \varepsilon$$

Table 6. Multiple Linear Regression Analysis Results

Variable	Coefficients	Std. Error	t-Statistic	Prob.
(Constant)	-0.398	0.625	-0.637	0.524
INDCOM	0.739	0.216	3.416	0.000
ACMEET	0.016	0.002	6.010	0.000
MANOWN	0.054	0.170	0.318	0.750
BOARDSIZE	-0.004	0.013	-0.335	0.738
AGE	0.005	0.001	2.935	0.003
SIZE	0.133	0.021	6.099	0.000
REPUTATION	-0.558	0.117	-4.762	0.000
Adjusted R ²				0.5017
Prob(F-statistic)				0.0000

Source: Research Data, 2024

The coefficient of determination was tested in this study, revealing an Adjusted R-Squared value of 0.5017. This indicates that 50.17% of the variation in sustainability report (SR) quality is influenced by the proportion of independent commissioners, audit committee meetings, managerial ownership proportion, board size, company age, company size, and environmental reputation perception. The remaining 49.83% is influenced by other variables outside the scope of this study.

The combined effect of independent and control variables on SR quality was assessed using an F-test, which yielded a significance value of 0.000, well below the threshold of 0.05. Thus, it is concluded that the proportion of independent commissioners, audit committee meetings, managerial ownership proportion, and board size, along with control variables such as company age, company size, and environmental reputation perception, collectively have a significant impact on SR quality.

The t-test results (Table 2) provide further insights. The proportion of independent commissioners, as an independent variable, has a positive coefficient with a significance level of 0.0008, indicating a positive and significant relationship with SR quality at a 99% confidence level, thereby supporting H1. Audit committee meetings also exhibit a positive coefficient with a significance level of 0.0000, underscoring a positive and significant influence on SR quality at a 99% confidence level, supporting H2.

Conversely, the managerial ownership proportion shows a positive coefficient with a significance level of 0.750, which, although positive, is not significant at the 90%, 95%, or 99% confidence levels, leading to the acceptance of H3 but without statistical significance. The variable of board size displays a negative coefficient with a significance level of 0.7380, indicating a negative but not significant influence on SR quality, thus rejecting H4.

Additionally, Table 2 reveals that the control variables company size and company age have positive effects on SR quality, whereas environmental reputation perception has a negative effect, all at a 99% confidence level.

The first hypothesis test confirms that the proportion of independent commissioners has a positive and significant impact on SR quality. A higher

number of independent commissioners enhances the quality of sustainability reports. This finding aligns with the studies by Novitaningrum & Amboningtyas (2017) and Putri *et al.* (2022). An increased proportion of independent commissioners motivates companies to disclose more comprehensive information about their sustainability practices to the public. Independent commissioners bring diverse perspectives and fresh insights into sustainability reporting, which enhances their understanding and oversight of SR quality (Dewi & Pitriasari, 2019).

According to legitimacy theory, companies seek to gain legitimacy from stakeholders by adopting actions and policies that align with stakeholder expectations (Ardiani *et al.*, 2022). A greater number of independent commissioners helps stakeholders perceive the company's commitment to sustainability, thereby enhancing the company's legitimacy. A larger proportion of independent commissioners ensures diversity and independence in decision-making processes, strengthening the internal oversight of sustainability practices. Their presence also enhances transparency and accountability, prompting the company to provide more accurate and comprehensive information in sustainability reports (Putri *et al.*, 2022). Improved transparency and accountability elevate the company's disclosure practices, leading to higher quality sustainability reports. Ultimately, better SR quality aids the company in gaining public legitimacy (Rudyanto & Siregar, 2018).

The second hypothesis test indicates that audit committee meetings positively and significantly influence SR quality. This finding is supported by the studies of Ardiani *et al.* (2022) and Aniktia *et al.* (2015). Audit committee meetings are crucial for effective oversight. During these meetings, members exchange ideas and perspectives, which enhances their understanding and improves their supervisory capabilities. More frequent audit committee meetings improve coordination among members, thereby increasing the pressure on management to enhance report quality. As the quality of these reports improves, the disclosures in the company's sustainability reports also become more robust (Aniktia *et al.*, 2015).

Audit committee meetings play a crucial role in ensuring the completeness and timeliness of reports and maintaining the integrity of sustainability reports (Buallay & Al-Ajmi, 2020). Increased meeting frequency enhances coordination among members, which maximizes oversight of management performance and ultimately optimizes the effectiveness of sustainability reporting (Ruhana & Hidayah, 2020).

Frequent audit committee meetings can be viewed as a strategic move by the company to enhance its legitimacy by demonstrating a serious commitment to overseeing sustainability aspects (Ardiani *et al.*, 2022). This commitment encourages management to provide more comprehensive sustainability report disclosures. Improved disclosure completeness helps the company gain legitimacy from stakeholders.

The third hypothesis test indicates that the proportion of managerial ownership has a positive but not significant effect on SR quality. This finding is consistent with the studies by Novitaningrum & Amboningtyas (2017) and Madona & Khafid (2020). According to legitimacy theory, companies adopt policies and actions perceived as legitimate by society to maintain or enhance their

legitimacy. Morck (1988) explains the convergence of interest hypothesis, which posits that when managers own shares in the company, their interests align with those of the owners. This alignment encourages managers to consider the long-term implications of their decisions and reassess sustainability issues to uphold the company's reputation. Managerial share ownership can motivate management to disclose company activities more thoroughly because managers with shares are more attentive to sustainability issues relevant to the company (Novitaningrum & Amboningtyas, 2017) (Nurhalisa & Hernawati, 2023). Enhanced disclosure practices improve SR quality, aiding the company in gaining legitimacy from the public (Madona & Khafid, 2020).

The proportion of managerial ownership has an insignificant effect on SR quality because the data distribution for this variable ranges from 0% to 76%, with a mean value of only 4.3%. This indicates that, on average, managers in the sample companies own just 4.3% of the shares, a very small percentage compared to the total shares held by other shareholders. This finding aligns with Nuraeni & Darsono (2020), who suggest that the insignificant impact of managerial ownership is due to the low share ownership by managers in the sample companies, with some companies having no managerial ownership at all.

The fourth hypothesis test reveals that board size has a negative but not significant effect on SR quality, indicating that larger boards are associated with a decline in SR quality. Similar results were found in the studies by Lucia & Panggabean (2018) and Wahyudi (2021). However, this contrasts with the findings of Dewi & Ramantha (2021) and Razaq *et al.* (2023), which show a positive influence of board size on SR quality. These discrepancies may be due to differences in SR quality measurement methods and the types of companies studied. Previous studies used the SDRI for measuring SR quality, while this research employs a modified scoring method. Additionally, earlier research included all companies listed on the IDX and non-financial companies listed on the Nigeria Exchange Group, whereas this study focuses specifically on energy sector companies.

The average number of directors in a company is five, in compliance with OJK Regulation No. 33/POJK.04/2014, which stipulates a minimum of two directors. Despite this, companies with larger boards do not produce higher-quality SRs. Larger boards can hinder the execution of directors' duties due to differing opinions, views, and working styles among members, complicating decision-making in preparing sustainability reports. This decline in directors' performance ultimately affects SR quality. This finding supports Yermack (1996) assertion that larger boards reduce directors' monitoring ability and complicate coordination, communication, and decision-making. A larger board size may lead to less attention to SR disclosure quality, diminishing the board's effectiveness in fulfilling its responsibilities (Ardiani *et al.*, 2022). Consequently, the decreased effectiveness of the board of directors can negatively impact the quality of SRs, making it more challenging for the company to gain legitimacy from the public.

CONCLUSION

A larger proportion of independent commissioners within a company's structure can enhance corporate transparency, leading to more comprehensive and higher-

quality disclosures in sustainability reports. Audit committee meetings can improve management effectiveness through the oversight of the audit committee, thereby enhancing SR disclosure practices. The proportion of managerial ownership has a positive but not significant impact on SR quality, which is attributed to the low level of managerial ownership that hinders managers' ability to improve report quality. Meanwhile, the board size has a negative but not significant effect on SR quality. A larger board size can reduce effectiveness and trigger conflicts that disrupt coordination in performing the board's duties.

This study has limitations, particularly in the selection of energy companies, which is restricted to the year 2023. Energy companies were chosen due to their major contribution to carbon emissions and the high incidence of workplace accidents in this sector. However, companies impacting social, economic, and environmental conditions are not limited to energy companies alone; other sectors, such as manufacturing, also have significant effects on these aspects. Therefore, future research should consider a combination of several sectors identified to impact social and environmental aspects and extend the timeframe for the selection of companies beyond a single period. Additionally, future studies are advised to use GRI 11: Oil & Gas Sector and GRI 12: Coal Sector standards to choose relevant and suitable topics for measuring the SR quality of companies in the energy sector.

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