

# The Research Status and Prospect of the Relationship between ESG Performance and Audit

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**Abstract.** In recent times, ESG has become an important aspect and indicator for evaluating the sustainable development, governance performance and social values of enterprises and organizations. In the field of audit, ESG has gained increasing importance, becoming an indispensable reference and influential factor. By thoroughly reviewing the relevant literature on the relationship between ESG and audit published on CNKI and WOS until September 2024, this paper aims to analyze the current research status, summarize the mutual effect and mechanism between these two domains. This study primarily focuses on two lines: firstly, it explores the impact of ESG performance on audit pricing, audit quality, and audit outcomes. Secondly, it studies how audit behavior and processes influence ESG performance. The findings suggest that favorable ESG performance generally leads to reduced audit pricing, enhanced audit quality, and increased likelihood of issuing positive audit reports. However, it is important to note that such conclusions are based on general discussions as some studies have reported contradictory results. Therefore, further exploration and discussion are needed for in-depth study in this area. Moreover, audits predominantly play a constructive role in promoting ESG performance. Based on these insights, this paper categorizes the mechanisms while discussing future research prospects with an aim to provide valuable references.

**Keywords:** audit relationship, ESG performance, Audit pricing, audit behavior

## 1. Instruction

The term ESG, which encompasses environmental, social, and corporate governance, has become a global initiative and phenomenon that is being advocated and prioritized by governments, international organizations, and financial institutions. Under the ESG framework, companies are mandated to disclose their relevant information pertaining to environmental protection, social responsibility, and corporate governance. This facilitates investors in comprehensively understanding the sustainable development potential of enterprises and urges businesses to place greater emphasis on social responsibility and long-term interests, while fostering their enduring growth. At the same time, the field of audit has gradually embraced and incorporated ESG, which then plays an increasingly pivotal role. This is because ESG factors enable auditors to gain a comprehensive understanding of corporate risks and performance, thereby facilitating a more accurate evaluation of the authenticity and accuracy of their financial statements. It is clear that the audit and ESG fields have a significant interplay. Exploring this relationship will enhance corporate comprehension of the significance of ESG, enable better implementation of this concept, and foster auditors' awareness and attention towards ESG, making it a crucial consideration in the auditing process. Moreover, it helps stakeholders in assessing ESG information for better understanding relevant companies, ultimately improving their investment decisions. Based on these premises, this paper aims to investigate the correlation between ESG performance and audit by conducting an advanced search resulting in 115 high-quality literature sources from 2022 to 2024 on CNKI and WOS platforms. Through induction and reorganization of interaction mechanisms between ESG and audit, two relationship chains are identified: (1) The influence mechanism of ESG on audit pricing, audit quality and audit outcomes; (2) The influence mechanism of audit behavior on ESG performance.

As a result, it is found that favorable ESG performance generally leads to a reduction in audit fees, enhancement of audit quality, and an increased likelihood of issuing positive audit reports. However, it should be noted that this conclusion is based on a broad discussion and some current studies have identified contradictory findings, indicating the need for further exploration and discourse in this field.

In another aspect, audits fundamentally play a constructive role in promoting ESG performance. Building upon this premise, this paper categorizes the influence relationships and mechanisms while also discussing future research prospects with the aim of providing valuable insights for this domain.

## 2. Literature Review

This paper aims to examine the impact of ESG on audit and audit behavior on ESG. For the former, this study will analyze the influence of ESG performance on audit pricing, audit quality, and audit outcomes individually. The majority of current research focuses on examining the correlation between audit pricing and ESG, indicating that higher ESG scores are associated with reduced audit costs. Nevertheless, little study has been done on how audit behavior impacts ESG performance or how ESG impacts audit quality and outcomes. It is important to note that in this paper, "ESG performance" refers to a comprehensive representation consists of ESG practices, rating results, as well as subjective and proactive engagement.

### 2.1. The impact of ESG performance on auditing

#### 2.1.1 The impact of ESG performance on audit pricing

The negative impact of ESG performance on audit pricing has been well established. Currently, the key dimensions for measuring corporate ESG performance primarily include ESG rating, ESG rating divergence, and overall ESG performance. Relevant literature suggests that corporate ESG performance primarily influences audit fees and pricing through three mediating effects: business risk, information risk, and audit risk.

Jia and Xia (2024) argue that favorable ESG performance is often reflected in the proactive identification and effective management of environmental, social, and corporate governance risks, signifying the company's exceptional risk management capabilities within its internal operations. Such performance enhances the focus, efficiency, and robustness of the audit process, thereby facilitating a reduction in audit fees.

Additionally, better ESG performance leads to reduced agency costs by fostering greater engagement with stakeholders, enhancing the disclosure of ESG information, and ensuring higher quality earnings. This ultimately enhances corporate information transparency and reduces information asymmetry, thereby decreasing auditor workload and risk perception (Song et al., 2023). According to the research conducted by Zheng et al., the ESG ratings of enterprises are publicly available, and current media tends to report negative or even exaggerated news. Consequently, auditors face increased professional risks and reputation risks when dealing with enterprises having diverse ESG ratings, leading to an adjustment in audit pricing as a form of risk compensation (Zheng et al., 2024). Notably, the impact is more pronounced for firms operating in heavily polluting industries, firms located in regions with low marketability, or when audits are conducted by industry-expert auditors.

Furthermore, Jia and Xia argue that better ESG performance generally indicates that the enterprises' proactive identification and timely control of environmental, social, and corporate governance risks, showing that the company excels in risk management within its internal operations. Such performance facilitates a more focused, efficient, and robust audit process (Zheng et al., 2024), thereby contributing to reduced audit fees.

However, it is important to note that while mainstream research has generally acknowledged a negative correlation between ESG performance and audit pricing, there are still studies finding that Higher ESG disclosure ratings are linked to higher audit fees, and companies that disclose ESG information typically have higher audit fees than those that do not (Wang et al., 2023). The reason behind this is that when confronted with companies boasting high disclosure scores, in order to guarantee the accuracy and consistency of financial statements and ESG data, auditors typically increase their communication and data analysis activities, which raises fees. Higher disclosure ratings

can also be a sign of opportunistic tactics like "greenwashing," which raises the risk and expense of audits.

These two disparate outcomes arise from divergent research perspectives and considerations. The notion that there exists an inverse correlation between ESG performance and audit pricing is primarily grounded in the company's standpoint, as it acknowledges that enterprises with higher ESG ratings tend to exhibit greater information transparency, thereby alleviating audit pressure. Conversely, the perspective positing a positive association between ESG rating and audit pricing centers around auditors' vantage point, wherein their professional skepticism is heightened to a larger extent. Consequently, as the ESG score increases, auditors are compelled raise their professional skepticism, consequently increasing audit costs. Both perspectives are reasonable, future research should strive towards combining these two considerations to yield more compelling conclusions.

### **2.1.2 The impact of ESG performance on audit quality**

In the Dictionary of Finance and Economics, Shengming defines audit quality as the level of audit work and the quality of audit effect. DeAngelo defined audit quality as the probability that an auditor will identify and report a breach in the corporate management. This paper is going to summarize audit quality as the effectiveness, reliability of the audit process and its results, and the adherence to auditing standards. Notably, due to unquantifiable nature of the audit quality, alternative indicators such as surplus management, audit fees, scale of accounting firms, and audit opinions are commonly used for measuring it. There exists a positive correlation between ESG performance and audit quality. The underlying mechanism primarily involves factors such as audit costs and earnings management to serve as mediating effects while financing constraints as regulating effect.

The extent and magnitude of surplus management can serve as indicators of audit quality. Asthana and Boone found that abnormal audit costs, whether positive or negative, tend to undermine the independence of an auditor, thereby compromising the controllable emergency surplus management of firms and diminishing audit quality (Asthana et al., 2012). Simultaneously, if a listed company exhibits poor ESG performance, it will have a stronger motivation of audit opinions shopping as a form of "economic rent" paid to auditors, resulting in positive abnormal audit costs. Similarly, as perceived by auditors, companies with poor ESG performance and ratings are more likely to face the risk of material misstatement, which may raise their willingness to propose higher audit fees in response (Wu et al., 2023).

Additionally, companies with better ESG performance will encounter fewer financing constraints and reduced incentives for revenue management, thereby mitigating financial risk and illegal risk, therefore leading to a significant reduction in operational risk, granting auditors' higher flexibility when developing audit plans. They can choose a more concise and efficient audit process, while effectively identifying and addressing the risk of significant error reporting, thereby improving overall audit efficiency and quality (Zhang et al., 2024).

### **2.1.3 The impact of ESG performance on audit outcomes**

In this paper, the audit outcomes primarily refer to the disclosure of audit opinion results. ESG performance predominantly influences the audit outcomes and presentation of opinions through the audit risks and operational risks.

The mediating effects of ESG on the audit risk path include information asymmetry and audit supervision pressure. According to Tang et al., their analysis of sample data from listed companies between 2010 and 2020 reveals a negative correlation between the ESG rating of listed companies and the likelihood of receiving a negative audit report (Tang et al., 2023). When an enterprise demonstrates favorable ESG performance, it usually signifies a superior information advantage and governance advantage, leading to increased willingness for management to minimize the concealment and selective disclosure of negative information (Li et al., 2024). Consequently, enterprises enhance favorable information generation and disclosure behavior, thereby improving information transparency, reducing information asymmetry, and ultimately exerting a positive influence on auditors' decision-making process regarding audit reports. To another respect, audit opinions are

influenced by industry dynamics and government regulations. A high ESG rating for an enterprise result in relatively diminished external supervision pressure as well as reduced external pressure, reputation risks, and auditing costs (Li et al., 2023), which collectively contribute to lowering the likelihood of issuing non-standard unqualified audit opinions.

In the mechanism of ESG affecting business risk, there are three main mediating effects: stakeholder relationship, financial support, and compliance management. Drawing from stakeholder theory, a favorable ESG performance by an enterprise typically indicates a more proactive response to stakeholders' demands and interests. These fosters trust and support from stakeholders, thereby enhancing the market competitiveness and business stability of the enterprise (Li et al., 2024). Simultaneously, enterprises with superior ESG performance embody heightened corporate innovation awareness, social responsibility, and green innovation potential. They are also more likely to possess a favorable reputation, thus attracts additional investment sources, even advantageous financial subsidies, tax policies, and credit support. This ultimately reduces business risks while improving financial backing. Furthermore, it reinforces enterprises' comprehension of government policies and their adherence to them while minimizing instances of non-compliance (Tang et al., 2023). Such performance diminishes the potential space for management in manipulating financial statements while reducing risk factors identifiable by auditors under modern risk-oriented auditing practices. As a result, this helps to reduce the amount of information required by auditors in the disclosure of key audit matters, and accordingly increases the likelihood of positive audit reports being issued.

The former studies concentrate on dissolving various factors in the mechanism of how ESG performance affects audit outcomes. However, enterprises with better ESG performance are more likely to receive unmodified audit reports. A higher ESG score generally indicates a company's proactive stance towards environmental and social responsibility, which is a crucial consideration for auditors when issuing their opinions. Consequently, their overall evaluation of the company tends to improve, thereby reducing the likelihood of revising audit opinions (Wang et al., 2023).

## 2.2. The impact of auditing on ESG performance

The prevailing consensus is that audit practices typically exert a favorable influence on ESG across various dimensions. However, some studies indicate that auditing activities and the issuance of audit reports may increase the likelihood of corporate “greenwashing.” This paper separates ESG performance into distinct components, analyzing the mechanisms by which auditing impacts corporate practices in environmental performance, social responsibility, and corporate governance.

In terms of environmental performance, given that corporate environmental disclosures often exhibit selective disclosure, subjective assumptions, and informational distortion, the role of certified public accountants (CPAs) has become increasingly critical under legal and audit requirements. Auditors, adhering to principles of assurance, evaluation, supervision, and independence, employ methods such as sampling, data review, document verification, and internal control assessment to verify the authenticity of disclosed environmental information, thereby effectively encouraging companies to improve their environmental practices (Song et al., 2024). Additionally, the more CPAs leverage their expertise to identify issues within corporate disclosures, the more effectively they can enhance the quality of environmental information disclosures.

In terms of social responsibility, the most notable impact of audit activities lies in improving the efficiency of information transmission, enhancing transparency, and reducing information asymmetry between corporations and external parties. Given the extensive nature of social responsibility disclosures, some companies may conceal unfavorable information or cut corners in their reporting. Auditing plays a key role in uncovering critical, concealed information and in preventing companies from evading social responsibility, thereby providing stakeholders with the necessary information. High-quality CPA audits encourage companies to convey more reliable information to the market and stakeholders, which enhances the efficiency of corporate communication, provides investors with more effective insights to evaluate corporate social performance, and mitigates information asymmetry. Furthermore, the supervisory pressure inherent in audit practices incentivizes companies

to address deficiencies in their social responsibility disclosures and improve disclosure quality to avoid receiving adverse audit opinions.

In terms of corporate governance, audit functions exert an external governance effect that reduces agency costs and enhances governance efficiency. Specifically, risk-oriented audits of internal control systems help companies identify previously unnoticed deficiencies, providing guidance for improvement and thus enhancing oversight and reducing internal supervision costs. Numerous studies also focus on the impact of state audits on corporate ESG performance, indicating that government audits possess higher levels of authority, objectivity, impartiality, and independence, as well as a deterrent effect against corporate misconduct. Government audits thus serve a crucial role in exposing, preventing, and mitigating risks, increasing corporate attention to ESG practices (Chen et al., 2024). This, in turn, fosters self-regulation, legal compliance, and enhances the overall efficacy of corporate governance.

However, not all research findings in this field support a positive correlation between audit behavior and ESG performance. Some studies have indicated that the occurrence of "greenwashing" tends to increase when a company receives a comment letter on its financial report (Liao et al., 2023). This perspective is particularly insightful. According to the crisis management hypothesis, when companies receive comment letters—especially if these letters contain information potentially damaging to corporate reputation—the heightened scrutiny from investors, media, and the public raises financial pressure and increases the likelihood of reputational harm. This often compels companies to engage in "greenwashing" practices when disclosing their ESG information.

On the other hand, some argue that the issuance of comment letters also increases the risk of exposing greenwashing behaviors, significantly raising the costs of such practices and potentially discouraging companies from attempting to mislead through ESG disclosures. The impact of financial report comment letters on corporate ESG disclosure practices thus remains an area for further exploration.

### 3. Conclusions

Overall, ESG performance and audit activities exhibit a mutually reinforcing influence, fostering positive oversight effects on one another. In mainstream perspectives, strong ESG performance tends to reduce audit fees, improve audit quality, and yield favorable audit outcomes. Simultaneously, audit activities encourage companies to commit more earnestly to ESG principles, ultimately resulting in higher ESG performance and ratings. However, some studies suggest that high ESG ratings may increase audit fees, while financial report comment letters from auditors may exert financial pressure on companies, thus raising the likelihood of misconduct or "greenwashing" in ESG reports. These varied viewpoints, each with merit, indicate a need for broader datasets and theoretical foundations to deepen analysis.

This paper posits that variations in company characteristics likely lead to diverse choices and behavioral outcomes; future studies could focus on differentiating between sectors and types of firms. By commencing with an examination of the inherent nature and behavioral logic of enterprises, and subsequently integrating specific data to scrutinize the correlation between ESG and audit, it is plausible that the level of divergence in research findings can be effectively mitigated.

As the world faces increasingly frequent extreme climate events, resource scarcity, slowed economic growth, and persistent income inequality, there is growing consensus that corporations must pursue low-carbon transitions, fulfill social responsibilities, and achieve sustainable, high-quality growth. Understanding the mechanisms and interactions between ESG performance and audit practices can guide companies toward better development pathways and offer valuable insights for audit policy formulation. Today, corporations are encouraged to more rigorously adopt ESG principles, comply with industry regulations and social policies, enhance the transparency of information disclosures, and foster positive relationships with stakeholders. Likewise, the audit

profession should consider more extensively incorporating ESG factors into audit standards to strengthen oversight and assessment of environmental, social, and corporate governance dimensions.

Notably, much of the current research has focused on specific cases within certain industries, such as the greater impact of ESG ratings on audit pricing in strong polluting industries, whereas audit influence on ESG performance appears more pronounced in non-polluting sectors. The underlying logic and causes of these distinctions remain insufficiently explored. The future research could thus prioritize examining the correlation between ESG and audit in both severe polluting and non-polluting industries to provide a comprehensive comparison. Additionally, further research might explore differences in ESG improvements across companies of varying sizes, thereby examining the actual effects of audit intervention on ESG performance. Such insights are anticipated to advance the integration of ESG and audit research, fostering continued development in this area.

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