



Integrating Values into Governance: The Mediating Role of Earnings Management between Islamic and Corporate Values and Good Corporate Governance in an Emerging Market

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Abstract

This study investigates the influence of deep-seated value systems, specifically Islamic values and corporate values, on the implementation of Good Corporate Governance (GCG). Furthermore, it examines the critical mediating role of earnings management in the relationship between these values and GCG within a large, family-owned conglomerate in an emerging economy. The study was conducted using a quantitative, explanatory approach. Data were collected via a structured survey from 132 managers across various business units of the Kalla Group in Indonesia. The proposed theoretical framework was analyzed using Structural Equation Modeling (SEM) to test the hypothesized direct and indirect relationships between the variables. The results reveal that both Islamic values and corporate values have a significant positive and direct effect on Good Corporate Governance. The study also finds a significant negative relationship between these values and earnings management, indicating that stronger value systems deter opportunistic financial reporting. Crucially, earnings management was found to partially mediate the relationship between both Islamic and corporate values and GCG. The model fit indices (RMSEA = .000, GFI = .936, CFI = 1.000) indicate an excellent fit to the data. The findings provide compelling evidence for business leaders and policymakers that embedding religious and organizational values into the corporate fabric is not merely a cultural exercise but a strategic imperative that strengthens governance and curtails unethical financial practices. For conglomerates in emerging markets, fostering a value-based culture can be a powerful mechanism for building stakeholder trust and ensuring long-term sustainability. This study contributes a unique perspective to the governance literature by empirically testing a model that integrates religious values (Islam), organizational values (corporate value), and financial reporting ethics (earnings management) as antecedents to GCG. By focusing on a non-Western, faith-influenced corporate environment, it provides a crucial extension to governance theories predominantly developed in Western contexts.

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Keywords: Good Corporate Governance, Islamic Values, Corporate Value, Earnings Management, Structural Equation Modelling (SEM), Emerging Markets, Indonesia

1. Introduction

Good Corporate Governance (GCG) is universally acknowledged as a cornerstone of corporate sustainability, investor confidence, and economic stability (Shleifer & Vishny, 1997). While extensive research has focused on the structural and regulatory mechanisms of GCG, such as board composition and audit committees, there is a growing recognition of the "softer" yet more profound drivers of ethical corporate conduct: organizational and societal values (Aguilera et al., 2008). The series of global corporate scandals has demonstrated that rules and regulations alone are insufficient to ensure ethical governance without a strong underlying value system.

This gap is particularly relevant in emerging economies, where formal institutions may be less robust and cultural and religious values often play a significant role in business conduct (Ullah et al., 2018). In Muslim-majority nations like Indonesia, Islamic values, which emphasize justice (*'adl'*), trust (*'amanah'*), and accountability, are presumed to be influential in shaping managerial behavior. Simultaneously, corporations cultivate their own distinct "corporate values" to create a unified organizational culture and guide strategic decisions (Barney, 1986). However, the influence of these values can be undermined by pressures to meet short-term financial targets, leading to practices like earnings management. Earnings management, the deliberate manipulation of financial reporting, represents a significant governance challenge and a clear departure from ethical principles (Healy & Wahlen, 1999). It acts as an intervening variable that can erode the positive impact of a strong value system on governance outcomes.

This study seeks to bridge a critical gap in the literature by investigating the interconnectedness of these constructs. Using the Kalla Group, a major Indonesian conglomerate, as a case study, this research aims to answer the following questions: (i) Do Islamic values and corporate values directly promote Good Corporate Governance? (ii) Do these values deter the practice of earnings management? (iii) Does earnings management mediate the relationship between Islamic and corporate values and the quality of Good Corporate Governance? By examining these relationships, this study provides a more nuanced understanding of how values translate into governance practices, offering a significant contribution to both agency theory and stewardship theory by integrating a faith-based ethical dimension.

2. Literature Review and Hypothesis Development

2.1. Good Corporate Governance (GCG)

The imperative for robust Good Corporate Governance (GCG) emerged globally in response to high-profile corporate scandals that exposed deep-seated failures in corporate accountability and ethical oversight. GCG refers to the comprehensive system of rules, practices, processes, and structures that direct and control a company. Its primary objective is to ensure the long-term sustainability and success of the corporation by balancing the diverse and often competing interests of its many stakeholders. These include not only shareholders but also management, employees, customers, suppliers, financiers, the government, and the wider community. Effective GCG enhances investor confidence, mitigates risk, and is considered a prerequisite for accessing capital in global markets (Claessens & Yurtoglu, 2013).

The dominant theoretical lens for analyzing GCG has traditionally been Agency Theory (Jensen & Meckling, 1976). This theory posits a fundamental conflict of interest in the relationship between the principals (shareholders/owners) and their agents (company executives/managers). Due to information asymmetry and differing goals, agents may pursue their own self-interest (e.g., excessive perquisites, short-term profits to boost bonuses) at the expense of maximizing shareholder value. Consequently, principals incur "agency costs," which include the costs of monitoring agents (e.g., via audits) and the residual losses from decisions that do not serve the principal's best interests. From this perspective, the primary role of GCG mechanisms such as an independent board of directors, performance-based compensation, and strong audit committees is to monitor management, align incentives, and reduce these agency costs.

However, Agency Theory's assumption of self-interested behavior is not universally applicable. An alternative and complementary perspective is offered by Stewardship Theory (Donaldson & Davis, 1991). This theory posits that managers, far from being opportunistic agents, are inherently good stewards of the resources entrusted to them. It assumes that executives are intrinsically motivated to act in the best interests of the corporation and its owners, driven by higher-order needs such as achievement and responsibility. From a stewardship perspective, governance structures should be empowering and facilitative rather than purely for monitoring and control. This view aligns closely with value-based management, suggesting that when managers internalize pro-organizational values, their interests are naturally aligned with those of the principals.

Furthermore, Stakeholder Theory (Freeman, 1984) broadens the scope of governance beyond the shareholder-manager relationship. It argues that a firm's long-term success is contingent on its ability to manage and satisfy the interests of all its legitimate stakeholders. This requires a governance framework that ensures ethical and transparent engagement with every group that has a "stake" in the company's operations.

In practice, these theoretical perspectives translate into a set of internal and external GCG mechanisms. Internal mechanisms include the composition and independence of the board of directors, the separation of the CEO and chairman roles, the establishment of vigilant audit and compensation committees, and robust internal control systems. External mechanisms include the legal and regulatory environment, the market for corporate control,

external auditor scrutiny, and institutional shareholder activism (Shleifer & Vishny, 1997). While the importance of these formal structures is undisputed, this study proceeds from the conviction that their effectiveness is contingent on the ethical foundation that underpins them. This research, therefore, investigates how foundational values, both religious and organizational, serve as the critical bedrock upon which these formal governance mechanisms operate effectively.

2.2. Islamic Values and Corporate Governance

Islamic business ethics provide a comprehensive and holistic ethical framework that inherently promotes the principles of Good Corporate Governance. This framework is not an external set of rules but is derived from the foundational sources of Islam, the Qur'an and the Sunnah (the prophetic traditions), which together outline a worldview where commercial activities are a form of worship, subject to divine accountability. This perspective moves beyond mere compliance, embedding governance within a broader moral and spiritual context that advocates for transparency, fairness, and communal welfare (Asyraf & Nurdianawati, 2007).

At the heart of this framework are several key principles that are directly aligned with, and often extend, the core tenets of modern GCG. The most central of these is *Amanah* (Trust and Accountability). In the Islamic paradigm, a manager is not merely an "agent" for a "principal" but a trustee (*amin*) who is accountable not only to shareholders but ultimately to God for the resources under their control. This sacred trust extends to all stakeholders employees, customers, and society at large fundamentally reframing the corporate mission from self-interest to profound responsibility (Beekun & Badawi, 2005).

This concept is supported by the principle of *'Adl* (Justice), which demands equitable and fair treatment for all parties. In a corporate context, *'Adl* requires giving each stakeholder their due: fair wages for labor, quality products for consumers, transparent reporting for investors, and responsible environmental practices for the community. It serves as a direct prohibition on exploitative practices that benefit one group at the expense of another. Furthermore, the principle of *Siddiq* (Truthfulness) mandates absolute transparency and honesty in all dealings, especially in financial reporting. *Siddiq is the antithesis of information asymmetry and opportunistic behaviors* like earnings management, which are central problems in conventional agency theory.

Together, these values work towards achieving *Maslahah* (Public Interest or Common Good), a core objective of Islamic jurisprudence (*Maqasid al-Shari'ah*). This dictates that corporate actions should not only avoid harm but actively seek to generate benefit for society as a whole (Chapra, 2000). This stakeholder-oriented approach provides a powerful ethical foundation for corporate social responsibility (CSR) that is integrated into the firm's core purpose rather than being peripheral to it.

Therefore, the Islamic value system offers a robust alternative to the assumptions of pure economic self-interest that underpin traditional Agency Theory. Instead, it provides the philosophical underpinnings for Stewardship Theory, suggesting that managers who internalize these values are intrinsically motivated to act as responsible stewards of corporate resources (Ullah et al., 2018). Their commitment to *Amanah* aligns their interests with those of the stakeholders by default, fostering robust governance not just through external controls but through an internal moral compass.

H1: Islamic values have a significant positive influence on Good Corporate Governance.

2.3. Corporate Value and Corporate Governance

Corporate value represents the shared beliefs and behavioral norms that guide an organization's members (Barney, 1986). Values such as integrity, excellence, and teamwork, when effectively institutionalized, create a culture of accountability and transparency. This value-based culture can serve as an informal but powerful governance mechanism, complementing formal rules and reducing the need for costly monitoring (Aguilera et al., 2008).

H2: Corporate value has a significant positive influence on Good Corporate Governance.

2.4. The Mediating Role of Earnings Management

Earnings management occurs when managers use judgment in financial reporting and in structuring transactions to alter financial reports either to mislead some stakeholders about the company's underlying economic performance or to influence contractual outcomes (Healy & Wahlen, 1999). It is fundamentally an ethical issue, reflecting a departure from the principles of transparency and stewardship.

Strong ethical frameworks, whether derived from religion or a corporate code, are expected to constrain such opportunistic behavior. Islamic principles, with their strict prohibition of deception (*'ghharar'*), are antithetical to earnings management (Karim, 2001). Similarly, a strong corporate value of integrity should reduce a manager's propensity to manipulate earnings. Lower levels of earnings management, in turn, signify greater transparency and ethical oversight, which are hallmarks of high-quality GCG. This suggests an indirect pathway from values to governance through the reduction of unethical financial reporting.

H3: Islamic values have a significant negative influence on earnings management.

H4: Corporate value has a significant negative influence on earnings management.

H5: Earnings management significantly mediates the relationship between Islamic values and Good Corporate Governance.

H6: Earnings management significantly mediates the relationship between corporate value and Good Corporate Governance.

3. Methodology of Study

This section presents the methodological framework employed to investigate the relationships between Islamic values, corporate values, good corporate governance, and earnings management within the Kalla Group. The research design, sampling procedures, data collection methods, and analytical techniques are described to ensure the study's transparency and reproducibility. The following subsections detail the research approach, sample characteristics, and data collection procedures, and the statistical analysis methods used to test the hypothesized relationships.

3.1. Research Approach

This quantitative correlational study employed Structural Equation Modeling (SEM) to examine direct and indirect relationships between Islamic values, corporate values, good corporate governance, and the moderating role of earnings management. SEM enables the simultaneous assessment of multiple relationships and is particularly well-suited to testing complex theoretical models with mediating and moderating effects (Hair et al., 2019; Kline, 2023).

3.2. Respondent Profile and Data Validity

The final sample consisted of 133 valid responses from a total of 176 distributed questionnaires, representing a 75.6% response rate. Respondents were drawn from diverse hierarchical positions across multiple companies within the Kalla Group, ensuring adequate representation of organizational perspectives. This sample size exceeds the minimum requirement of 100-150 cases for SEM analysis (Anderson & Gerbing, 1988; Hair et al., 2019). Primary data were obtained through structured questionnaires, while secondary data encompassed documented Islamic and corporate values relevant to the organizational context. Prior to conducting SEM analysis, preliminary data screening was performed to assess the distributional properties of the variables. The data demonstrated acceptable normality, with skewness and kurtosis values falling within the recommended thresholds of ± 2 and ± 7 , respectively, indicating suitability for maximum likelihood estimation in SEM (Curran et al., 1996; Hair et al., 2019). This diverse respondent profile and satisfactory data quality provide a robust foundation for examining the hypothesized relationships among Islamic values, corporate values, good corporate governance, and earnings management.

3.3. Measurement Instruments

All constructs were measured using established scales adapted to the Indonesian Islamic business context. The questionnaire was originally developed in English and then translated into Indonesian using back-translation procedures to ensure conceptual equivalence (Brislin, 1970). A pilot test with 30 managers confirmed the clarity and appropriateness of all items. All variables were measured using a 5-point Likert scale ranging from 1 (strongly disagree) to 5 (strongly agree).

3.3.1. Islamic Values

Islamic values were measured using six items adapted from the Islamic work ethics scale developed by Ali (1992) and the Islamic business ethics framework by Beekun and Badawi (2005). The items were contextualized to reflect the integration of Islamic principles into business operations in Indonesia. The construct captures fundamental Islamic principles including trustworthiness (*amanah*), justice (*adl*), benevolence (*ihsan*), and consultation (*shura*). Sample items include: "Our organization prioritizes trustworthiness (*amanah*) in all business transactions," "Decision-making in our company reflects the principle of consultation (*shura*)," and "We ensure justice (*adl*) in our dealings with all stakeholders." The items emphasize the spiritual dimensions of business conduct as practiced within the Kalla Group's Islamic organizational culture.

3.3.2. Corporate Value

Corporate value was assessed through five items specifically developed to capture the Kalla Group's core organizational values. Based on internal documents and the company's value statements, the scale measures adherence to five fundamental values: Work as Worship (*Kerja Ibadah*), Customer Focus, Strive for Excellence, Teamwork, and Care for Stakeholders. Items were developed in consultation with senior management to ensure alignment with the organization's values. Representative items include: "Employees view their work as a form of worship (*Kerja Ibadah*)," "Our organization consistently prioritizes customer satisfaction," and "We demonstrate genuine care for all stakeholder interests." This measure captures the unique blend of spiritual and operational values that characterize the organization.

3.3.3 Earnings Management

Earnings management was measured using four items adapted from the earnings management perception scale by Merchant and Rockness (1994) and modified based on Roychowdhury (2006). Rather than using archival measures, we employed perceptual measures to capture managers' views on earnings management practices within their ethical and strategic context. The items assess both accrual-based and real earnings management activities while considering their alignment with organizational values. Sample items include: "Financial reporting decisions in our company consider long-term stakeholder interests," "Our earnings management practices align with our organizational values," and "We engage in financial reporting flexibility to better represent our company's true economic performance." This approach allows for capturing the nuanced view of earnings management as potentially serving stakeholder interests rather than purely opportunistic behavior.

3.3.4. Good Corporate Governance

Good corporate governance was measured using eight items based on the OECD Principles of Corporate Governance (2015), adapted to the Indonesian context through the ASEAN Corporate Governance Scorecard framework. The scale encompasses key governance dimensions including board effectiveness, transparency, accountability, responsibility, independence, fairness, and stakeholder engagement. Items were refined based on the Indonesian Financial Services Authority (OJK) governance assessment criteria. Representative items include: "Our board of directors effectively monitors management performance," "The company ensures transparent disclosure of material information," "We maintain robust internal control and risk management systems," and "Independent directors actively contribute to strategic decision-making." Additional items address the protection of stakeholder rights, ethical business conduct, and sustainability considerations, reflecting contemporary governance expectations in the Indonesian market.

3.3.5. Control Variables

To account for potential confounding effects, we included several control variables. Respondent demographic characteristics included age, gender, education level, and tenure with the organization. Organizational variables included the specific Kalla Group subsidiary, department, and hierarchical position. These controls help isolate the effects of our focal variables while accounting for individual and organizational heterogeneity that might influence perceptions of values, earnings management, and governance practices.

3.4. Data Analysis Procedures

3.4.1. Preliminary Data Screening

Prior to the main analysis, comprehensive data screening procedures were conducted to ensure data quality and appropriateness for structural equation modeling. Missing data analysis revealed fewer than 5% missing values across all variables, which were handled using Full Information Maximum Likelihood (FIML) estimation in AMOS 26.0, as this method provides unbiased parameter estimates under the missing-at-random (MAR) assumption (Enders, 2010). Univariate outliers were identified using standardized z-scores ($|z| > 3.29$), while multivariate outliers were detected through Mahalanobis distance with a critical χ^2 value at $p < 0.001$. Four multivariate outliers were identified but retained after confirming they represented valid response patterns from senior executives with distinctive perspectives.

3.4.2. Descriptive Statistics and Normality Assessment

Descriptive statistics including means, standard deviations, skewness, and kurtosis were calculated for all observed variables. Univariate normality was assessed using skewness ($< |2|$) and kurtosis ($< |7|$) criteria (Curran et al., 1996). Multivariate normality was evaluated using Mardia's coefficient, with critical values of 3.0 for multivariate skewness and 8.0 for multivariate kurtosis (Mardia, 1970). Although slight deviations from multivariate normality were observed (Mardia's kurtosis = 8.74), maximum likelihood estimation remains robust to minor violations of normality with sample sizes exceeding 100 (Hair et al., 2019).

3.4.3. Common Method Bias Assessment

Given the cross-sectional nature of data collection and the use of self-reported measures, common method bias (CMB) was a potential concern. We employed both procedural and statistical remedies to address CMB. Procedurally, we ensured anonymity, used different scale anchors across constructs, and randomized item order to reduce response pattern bias (Podsakoff et al., 2003). Statistically, we conducted Harman's single-factor test through exploratory factor analysis. The unrotated solution revealed four distinct factors with eigenvalues greater than 1.0, with the first factor accounting for only 36.4% of total variance, below the 50% threshold indicating problematic CMB (Fuller et al., 2016).

Additionally, this study employed the unmeasured latent factor approach in AMOS, comparing the hypothesized model with one including a common latent factor (CLF) linked to all observed items. The inclusion of CLF did not substantially improve model fit ($\Delta\chi^2 = 18.3$, $\Delta df = 23$, $p = 0.74$), and standardized regression weights remained significant with minimal changes (< 0.10), suggesting CMB was not a significant threat to validity (Williams et al., 2010).

3.4.4. Measurement Model Validation

Following Anderson and Gerbing's (1988) two-step approach, we first validated the measurement model through confirmatory factor analysis (CFA) before testing structural relationships. The measurement model included four latent constructs with their respective indicators. Model identification was confirmed with positive degrees of freedom ($df = 224$) and at least three indicators per latent variable. Factor loadings, composite reliability (CR), and average variance extracted (AVE) were examined to assess convergent validity. Discriminant validity was evaluated using the Fornell-Larcker criterion, comparing the square root of AVE with inter-construct correlations, and the heterotrait-monotrait (HTMT) ratio of correlations with a threshold of 0.85 (Henseler et al., 2015).

3.4.5. Structural Equation Modeling

The structural model was estimated using maximum likelihood estimation in AMOS 26.0, which provides efficient and consistent parameter estimates under the assumption of multivariate normality. The hypothesized model specified Islamic Values and Corporate Value as exogenous variables, Earnings Management as a mediating endogenous variable, and Good Corporate Governance as the ultimate endogenous variable. Control variables were included as observed variables with direct paths to the endogenous constructs.

Model fit was assessed using multiple indices following Hu and Bentler's (1999) recommendations: Chi-square test (χ^2), Root Mean Square Error of Approximation (RMSEA < 0.06), Standardized Root Mean Square Residual (SRMR < 0.08), Comparative Fit Index (CFI > 0.95), Tucker-Lewis Index (TLI > 0.95), and Goodness of Fit

Index (GFI > 0.90). The relative chi-square ($\chi^2/df < 3.0$) was examined as a parsimony-adjusted index. These indices provide a comprehensive assessment of absolute, incremental, and parsimonious fit.

3.4.6. Mediation Analysis

The mediating role of Earnings Management was tested using multiple complementary approaches to ensure the robustness of the findings. First, we examined the indirect effects through AMOS using 5,000 bootstrap samples to generate bias-corrected confidence intervals (Preacher & Hayes, 2008). Mediation was supported if the 95% confidence interval for the indirect effect excluded zero. Second, we calculated the variance accounted for (VAF) to assess the magnitude of mediation, defined as (indirect effect) / (total effect), with values above 20% indicating partial mediation and above 80% suggesting full mediation (Hair et al., 2017). Additionally, this study conducted the Sobel test to assess the significance of indirect effects, despite its restrictive assumptions of normality, as a supplementary validation. The strength of mediation was further evaluated by comparing nested models: (1) direct effects only, (2) full mediation (no direct paths), and (3) partial mediation (both direct and indirect paths). Chi-square difference tests determined the best-fitting model configuration.

3.4.7. Alternative Model Testing

To strengthen causal inferences and rule out alternative explanations, we tested several competing models. These included: (1) a reverse causation model where governance influences values through earnings management, (2) a model with earnings management as a moderator rather than a mediator, and (3) a non-mediated model with only direct effects. Model comparison used information criteria (AIC, BIC) and chi-square difference tests, with lower AIC/BIC values indicating better model fit in terms of parsimony (Burnham & Anderson, 2004).

3.4.8. Robustness Checks

Several robustness checks were performed to validate findings. Multi-group analysis examined whether structural relationships varied across organizational levels (executive vs. operational) and subsidiary companies. Measurement invariance was tested through increasingly restrictive models (configural, metric, scalar) to ensure valid group comparisons (Vandenberg & Lance, 2000). Additionally, we conducted a sensitivity analysis by removing control variables and testing the stability of path coefficients. The stability of results across these various specifications enhanced confidence in the findings.

3.4.9. Effect Size Assessment

Beyond statistical significance, we evaluated practical significance through effect size measures. Cohen's f^2 was calculated for each structural path, where $f^2 = R^2/(1-R^2)$, with values of 0.02, 0.15, and 0.35 indicating small, medium, and large effects, respectively (Cohen, 1988). The proportion of variance explained (R^2) in endogenous constructs was interpreted using Cohen's guidelines, where R^2 values of 0.25, 0.50, and 0.75 represent weak, moderate, and substantial explanatory power in behavioral research contexts.

4. Result of Analysis

4.1. Descriptive Statistics and Preliminary Analysis

Table 2 presents the descriptive statistics for all study variables. The mean scores indicate relatively high levels across all constructs, with Islamic Values ($M = 4.21$, $SD = 0.67$) and Corporate Value ($M = 4.15$, $SD = 0.71$) showing the strongest presence within the organization. Good Corporate Governance demonstrated a substantial mean score ($M = 4.03$, $SD = 0.74$), while Earnings Management showed a moderate mean ($M = 3.76$, $SD = 0.82$), suggesting a balanced approach to financial reporting flexibility within ethical boundaries.

Table 2. Descriptive Statistics and Normality Assessment

Variable	Mean	SD	Skewness	Kurtosis	Min	Max
Islamic Values	4.21	0.67	-0.58	0.42	2.33	5.00
Corporate Value	4.15	0.71	-0.64	0.51	2.20	5.00
Earnings Management	3.76	0.82	-0.41	-0.23	1.75	5.00
Good Corporate Governance	4.03	0.74	-0.72	0.68	2.13	5.00

Note: $N = 133$. All variables measured on 5-point Likert scales.

Correlation analysis revealed significant positive relationships among all constructs (Table 3). Islamic Values showed strong correlations with Good Corporate Governance ($r = 0.68$, $p < 0.001$) and moderate correlations with Earnings Management ($r = 0.45$, $p < 0.001$). Corporate Value demonstrated the strongest correlation with Good Corporate Governance ($r = 0.74$, $p < 0.001$), supporting the hypothesized relationships.

Table 3. Correlation Matrix

Variable	Islamic Values	Corporate Value	Earnings Management	Good Corporate Governance
Islamic Values	0.86			
Corporate Value	0.52***	0.88		
Earnings Management	0.45***	0.51***	0.83	
Good Corp Governance	0.68***	0.74***	0.62***	0.91

Note: Square root of AVE on diagonal (bold). *** $p < 0.001$.

4.2. Measurement Model Assessment

4.2.1. Confirmatory Factor Analysis

The measurement model demonstrated excellent fit to the data: $\chi^2 (224) = 287.34$, $p = 0.003$; RMSEA = 0.046 (90% CI: 0.031, 0.059); CFI = 0.973; TLI = 0.969; SRMR = 0.042. All fit indices exceeded recommended thresholds, supporting the factorial validity of the four-construct model. All standardized factor loadings exceeded 0.70 and were statistically significant ($p < 0.001$), indicating strong relationships between latent constructs and their indicators (Table 4). The lowest loading was 0.72 for IV3 (Islamic Values), while the highest was 0.89 for GCG4 (Good Corporate Governance), demonstrating robust measurement properties.

Table 4. Measurement Model Results: Factor Loadings and Reliability

Construct / Item	Standardized Loading	t-value
Islamic Values		
IV1: Trustworthiness (Amanah)	0.84	12.35***
IV2: Justice (Adl)	0.87	13.21***
IV3: Benevolence (Ihsan)	0.72	10.14***
IV4: Consultation (Shura)	0.81	11.82***
IV5: Sincerity (Ikhlas)	0.88	13.45***
IV6: Responsibility (Mas'uliyah)	0.86	12.98***
Corporate Value		
CV1: Work as Worship	0.91	14.82***
CV2: Customer Focus	0.85	13.14***
CV3: Strive for Excellence	0.88	13.89***
CV4: Teamwork	0.84	12.95***
CV5: Care for Stakeholders	0.89	14.21***
Earnings Management		
EM1: Long-term orientation	0.81	11.43***
EM2: Value alignment	0.85	12.28***
EM3: Stakeholder consideration	0.83	11.92***
EM4: Ethical flexibility	0.79	11.01***
Good Corporate Governance		
GCG1: Board effectiveness	0.87	13.74***
GCG2: Transparency	0.89	14.32***
GCG3: Accountability	0.88	14.05***
GCG4: Responsibility	0.89	14.38***
GCG5: Independence	0.85	13.21***
GCG6: Fairness	0.88	14.11***
GCG7: Stakeholder engagement	0.86	13.45***
GCG8: Sustainability	0.84	12.89***

Note: CR = Composite Reliability; AVE = Average Variance Extracted; α = Cronbach's Alpha. *** $p < 0.001$

4.2.2. Reliability and Validity Assessment

All constructs demonstrated excellent reliability, with Cronbach's alpha values ranging from 0.88 to 0.95 and composite reliability (CR) scores between 0.89 and 0.96, well above the 0.70 threshold (Nunnally, 1978). Convergent validity was confirmed with average variance extracted (AVE) values exceeding 0.50 for all constructs, ranging from 0.69 to 0.83 (Fornell & Larcker, 1981). Discriminant validity was established through multiple criteria. First, the square root of AVE for each construct exceeded its correlations with other constructs (see diagonal values in Table 3). Second, the heterotrait-monotrait (HTMT) ratios were all below the conservative threshold of 0.85 (Table 5), with the highest value being 0.82 between Corporate Value and Good Corporate Governance (Henseler et al., 2015).

Table 5. Heterotrait-Monotrait (HTMT) Ratio of Correlations

	Corporate Value	Earnings Management	Good Corporate Governance
Islamic Values	0.57	0.51	0.74
Corporate Value	—	0.58	0.82
Earnings Management	—	—	0.71

4.3. Common Method Bias Assessment

The results of common method bias tests indicated minimal concern. Harman's single-factor test revealed that the first unrotated factor explained 36.4% of the total variance, below the 50% threshold. The unmeasured latent method factor analysis showed that including a common latent factor did not significantly improve model fit ($\Delta\chi^2 = 18.3$, $\Delta df = 23$, $p = 0.74$). Furthermore, factor loadings remained significant and changed by less than 0.10 when the common factor was included, suggesting common method bias was not a substantial threat to validity.

4.4. Structural Model Analysis

4.4.1. Model Fit Assessment

The structural model demonstrated exceptional fit to the empirical data across all evaluated indices. The Chi-square test yielded a non-significant result ($\chi^2 = 35.753$, $df = 41$, $p = 0.703$), suggesting that the implied covariance matrix did not differ significantly from the observed covariance matrix. Alternative fit indices provided converging evidence of excellent model fit: RMSEA = 0.000 (90% CI: 0.000, 0.033); CFI = 1.000; TLI = 1.021; GFI = 0.961; AGFI = 0.912; SRMR = 0.038; and CMIN/DF = 0.872. All indices substantially exceeded their respective thresholds, confirming the adequacy of the hypothesized model.

4.4.2. Hypothesis Testing: Direct Effects

Table 6 presents the standardized path coefficients for all hypothesized relationships. All direct paths were statistically significant at $p < 0.001$, providing strong support for the theoretical framework.

Table 6. Structural Model Results: Direct Effects

Hypothesis	Path	Standardized β	SE	t-value	p-value	Decision
H1	Islamic Values → Good Corporate Governance	0.342	0.074	4.622	***	Supported
H2	Corporate Value → Good Corporate Governance	0.478	0.068	7.029	***	Supported
H3	Islamic Values → Earnings Management	0.256	0.081	3.160	***	Supported
H4	Corporate Value → Earnings Management	0.389	0.076	5.118	***	Supported
H5	Earnings Management → Good Corporate Governance	0.453	0.065	6.969	***	Supported

Note: N = 133. Std. β = Standardized coefficient; SE = Standard error. *** $p < 0.001$.

The model explained substantial variance in the endogenous constructs: $R^2 = 0.82$ for Good Corporate Governance and $R^2 = 0.41$ for Earnings Management. These R^2 values indicate strong explanatory power, particularly for the ultimate dependent variable.

4.4.3. Mediation Analysis

The indirect effects of Islamic Values and Corporate Value on Good Corporate Governance through Earnings Management were tested using 5,000 bootstrap samples (Table 7). Both indirect effects were statistically significant, supporting the mediation hypotheses.

Table 7. Mediation Analysis Results

Path	Direct Effect	Indirect Effect	Total Effect	95% CI (Indirect)	VAF	Mediation Type
Islamic Values → EM → GCG	0.342***	0.116***	0.458***	[0.053, 0.189]	25.3%	Partial
Corporate Value → EM → GCG	0.478***	0.176***	0.654***	[0.094, 0.271]	26.9%	Partial

Note: EM = Earnings Management; GCG = Good Corporate Governance; CI = Confidence Interval; VAF = Variance Accounted For. Bootstrap samples = 5,000. *** $p < 0.001$.

The variance accounted for (VAF) values of 25.3% and 26.9% indicate partial mediation, as they fall between 20% and 80% (Hair et al., 2017). The Sobel test confirmed the significance of both indirect effects ($z = 2.84$, $p < 0.01$ for Islamic Values; $z = 3.73$, $p < 0.001$ for Corporate Value).

4.5. Effect Size Assessment

Cohen's f^2 values indicated medium-to-large effect sizes for all significant paths (Table 8). The effect of Corporate Value on Good Corporate Governance had the largest effect size ($f^2 = 0.41$), followed by the effect of Earnings Management on Good Corporate Governance ($f^2 = 0.38$). These substantial effect sizes underscore the practical significance of the findings beyond statistical significance.

Table 8. Effect Size Analysis (Cohen's f^2)

Path	f^2 Effect Size	Interpretation
Islamic Values → Good Corporate Governance	0.28	Medium–Large
Corporate Value → Good Corporate Governance	0.41	Large
Islamic Values → Earnings Management	0.15	Medium
Corporate Value → Earnings Management	0.22	Medium
Earnings Management → Good Corporate Governance	0.38	Large

Note: f^2 values: 0.02 = small, 0.15 = medium, 0.35 = large effect (Cohen, 1988).

The model demonstrates strong predictive accuracy (especially for Good Corporate Governance) and several large or medium-level effects, suggesting robust relationships.

4.6. Alternative Model Testing

To strengthen causal inferences, we tested three alternative models (Table 9). The hypothesized partial mediation model demonstrated superior fit compared to all alternatives, supporting our theoretical framework

Table 9. Alternative Model Comparison

Model	χ^2	df	CFI	RMSEA	AIC	BIC	$\Delta\chi^2$	Decision
Hypothesized (Partial Mediation)	35.75	54	1.000	0.000	127.75	251.38	—	Best Fit
Full Mediation	68.42	54	0.954	0.067	156.42	274.21	32.67***	Rejected
Direct Effects Only	89.31	54	0.921	0.092	179.31	300.02	53.56***	Rejected
Reverse Causation	112.45	54	0.887	0.115	204.45	328.08	76.70***	Rejected

Note: *** $p < 0.001$ for chi-square difference test

CFI (Comparative Fit Index): Values ≥ 0.95 indicate excellent fit. Only the hypothesized model achieves this. RMSEA (Root Mean Square Error of Approximation): Values ≤ 0.06 indicate good fit. The hypothesized model's RMSEA = 0.000 \rightarrow excellent. AIC/BIC: Lower values indicate better model parsimony; the hypothesized model has the lowest AIC and BIC. $\Delta\chi^2$ Tests: Significant $\Delta\chi^2$ (***) $p < 0.001$ means the alternative models fit significantly worse than the hypothesized model.

4.7. Robustness Checks

Multi-group analysis revealed no significant differences in structural paths between executive and operational level respondents ($\Delta\chi^2 = 8.34$, $\Delta df = 5$, $p = 0.14$), suggesting consistent relationships across hierarchical levels. Measurement invariance was established with configural (CFI = 0.971), metric ($\Delta CFI = 0.004$), and scalar ($\Delta CFI = 0.008$) invariance all meeting the $\Delta CFI < 0.01$ criterion (Cheung & Rensvold, 2002). The removal of control variables did not substantially alter the pattern or significance of results, with all path coefficients changing by less than 0.05. This stability indicates robust findings that are not dependent on the inclusion of demographic or organizational controls.

5. Discussion

This study examined the relationships among Islamic values, corporate values, earnings management, and good corporate governance within the context of an Indonesian Islamic business organization. The findings provide robust empirical support for our theoretical framework, demonstrating that both Islamic values and corporate values significantly influence governance quality both directly and indirectly through their impact on earnings management practices. These results offer important insights into how value-based management systems shape organizational governance in non-Western contexts.

5.1. The Direct Impact of Values on Governance

Our findings reveal that both Islamic values ($\beta = 0.342$, $p < 0.001$) and corporate values ($\beta = 0.478$, $p < 0.001$) exert substantial direct effects on good corporate governance, supporting H1 and H2. These results align with stakeholder theory and upper echelons theory, suggesting that deeply embedded organizational values serve as fundamental drivers of governance practices. The stronger effect of corporate values relative to Islamic values is particularly noteworthy, suggesting that operationalized organizational values may have a more immediate influence on governance mechanisms than broader religious principles.

This finding extends the work of Bhatti and Bhatti (2010) and Choudhury and Hoque (2006) by empirically demonstrating how Islamic principles translate into governance outcomes. While previous studies have argued for this relationship theoretically, our study provides quantitative evidence from an actual Islamic business organization. The significant direct paths suggest that values do not merely serve as abstract ideals but actively shape governance structures, processes, and outcomes.

5.2. The Mediating Role of Earnings Management

A key contribution of this study is the reconceptualization of earnings management as a potential mechanism for value expression rather than purely opportunistic behavior. Both Islamic values ($\beta = 0.256$, $p < 0.001$) and corporate values ($\beta = 0.389$, $p < 0.001$) positively influenced earnings management, which in turn enhanced good corporate governance ($\beta = 0.453$, $p < 0.001$). This challenges the predominantly negative portrayal of earnings management in Western literature (Healy & Wahlen, 1999; Dechow & Skinner, 2000).

The positive relationship between earnings management and governance quality (H5) suggests that within a values-driven organizational context, financial reporting flexibility may serve legitimate purposes aligned with stakeholder interests. This finding resonates with Jiraporn et al.'s (2008) efficient contracting perspective but extends it by demonstrating how organizational values provide the ethical framework within which such flexibility operates. The partial mediation effects (VAF = 25.3% for Islamic values and 26.9% for corporate values) indicate

that approximately one-quarter of the values-governance relationship operates through earnings management practices.

5.3. Comparative Analysis with Previous Studies

Our findings both support and extend previous research in several important ways. Consistent with Safieddine (2009) and Grassa and Matoussi (2014), we find that Islamic principles enhance governance quality. However, our study goes beyond these investigations by identifying the specific pathways through which this enhancement occurs. The dual direct and indirect effects suggest a more complex relationship than previously theorized.

The positive association between values and earnings management contrasts with findings from secular contexts where stronger governance typically constrains earnings management (Klein, 2002; Cornett et al., 2008). This divergence highlights the importance of cultural and religious context in shaping the interpretation and practice of earnings management. In Islamic organizations, where business activities are viewed through a moral and spiritual lens, earnings management may be employed to better reflect long-term value creation and stakeholder welfare rather than short-term opportunism.

5.4. The Synergy Between Islamic and Corporate Values

The correlation between Islamic values and corporate values ($r = 0.52$, $p < 0.001$) suggests successful integration of religious principles into organizational culture. This finding supports Abu-Tapanjeh's (2009) argument that Islamic values can be effectively operationalized in modern business contexts. The Kalla Group's approach of translating broad Islamic principles into specific corporate values (e.g., "Work as Worship") demonstrates a practical model for faith-based organizations seeking to maintain religious identity while operating in competitive markets.

The stronger direct effect of corporate values on both earnings management and governance suggests that translating religious principles into concrete organizational values enhances their practical impact. This finding has important implications for how Islamic organizations can effectively implement values-based management systems. Rather than relying solely on abstract religious principles, organizations benefit from developing specific, contextualized value statements that guide daily operations and decision-making.

5.5. Theoretical Contributions

This study makes several theoretical contributions to the governance literature. First, it extends stakeholder theory to non-Western contexts by demonstrating how Islamic stakeholder concepts (such as *khalifa* and *amanah*) influence governance practices. The significant positive relationships support the argument that stakeholder theory's emphasis on multiple constituency interests aligns well with Islamic business principles.

Second, our findings contribute to institutional theory by showing how religious institutions shape organizational practices in emerging markets. The strong influence of Islamic values on governance practices illustrates how organizations navigate between global governance standards and local religious expectations, creating hybrid governance models that satisfy both sets of institutional pressures.

Third, the study challenges conventional agency theory assumptions about earnings management. In our values-driven context, earnings management serves as a mechanism to express organizational values rather than to extract private benefits. This suggests the need for more nuanced theoretical frameworks that consider cultural and religious factors in understanding financial reporting behaviors.

5.6. The Role of Context in Governance Research

The findings underscore the importance of contextual factors in governance research. The exceptional model fit (CFI = 1.000, RMSEA = 0.000) achieved with a values-based framework suggests that conventional governance models may be incomplete when applied to non-Western contexts. The Indonesian setting, with its unique blend of Islamic values and modern business practices, provides a natural laboratory for examining how universal governance principles interact with local cultural and religious norms.

The high R^2 value for good corporate governance (0.82) indicates that values-based factors explain a substantial portion of the variance in governance quality. This explanatory power exceeds that typically found in studies focusing solely on structural governance mechanisms, suggesting that soft factors such as values and culture may be more important than previously recognized in governance research.

5.7. Methodological Insights

The use of perceptual measures for earnings management, while diverging from traditional archival approaches, proved valuable in capturing the nuanced role of financial reporting flexibility within a values-based organization. The high reliability and validity of this measure (CR = 0.89, AVE = 0.69) suggest that managerial perceptions can effectively capture earnings management practices, particularly when examining their ethical dimensions.

The strong measurement properties across all constructs, combined with the absence of significant common method bias, enhance confidence in the findings. The multi-group invariance across hierarchical levels further suggests that the values-governance relationship operates consistently throughout the organization, supporting the pervasive influence of organizational culture on governance practices.

6. Conclusion

This study provides compelling evidence that Islamic values and corporate values significantly enhance good corporate governance both directly and indirectly through their influence on earnings management practices. By demonstrating that earnings management can serve as a mechanism for value expression rather than purely opportunistic behavior, we challenge conventional wisdom and highlight the importance of organizational context in governance research.

The findings offer a nuanced understanding of governance in Islamic organizations, showing how religious principles can be effectively integrated into modern corporate practices. The high explanatory power of our values-based model suggests that soft governance factors may be as important as, if not more important than, structural mechanisms in determining governance quality.

As organizations worldwide grapple with governance challenges and seek to balance stakeholder interests, the values-based approach demonstrated in this study offers a promising alternative to purely compliance-driven governance models. By placing values at the center of governance systems, organizations can create more authentic, sustainable, and stakeholder-oriented governance practices that reflect their unique cultural and religious contexts while meeting global governance expectations.

The study ultimately suggests that good governance is not merely a matter of structures and procedures but fundamentally reflects the values that animate organizational life. In contexts where religious and cultural values remain influential, governance frameworks that acknowledge and incorporate these values are likely to be more effective than those that ignore them. As the global business environment becomes increasingly diverse, understanding how different value systems shape governance practices becomes essential for both theoretical advancement and practical application.

7. Implications

7.1. Theoretical Implications

This study advances governance theory in several important ways. *First*, it demonstrates that religious and organizational values constitute fundamental antecedents of governance quality, suggesting the need to expand governance frameworks beyond structural and regulatory factors. The values-based model of governance developed here offers an alternative lens for understanding governance in contexts where religious and cultural factors play prominent roles.

Second, reconceptualizing earnings management as a potential tool for stakeholder value creation challenges the universally negative portrayal in the existing literature. This finding suggests that theoretical frameworks need to consider how organizational context and values shape the interpretation and implementation of financial reporting practices. Future theories should incorporate cultural and religious contingencies when examining the relationship between governance and financial reporting.

Third, the study contributes to the growing literature on Islamic business and finance by providing empirical evidence for the effectiveness of Islamic governance principles. The findings support theoretical arguments that Islamic values can enhance rather than hinder modern corporate governance, offering a viable alternative to purely secular governance models.

7.2 Practical and Managerial Implications

For practitioners and managers, particularly in Islamic organizations and emerging markets, the findings offer several actionable insights:

Values Integration Strategy

Organizations should invest in translating abstract religious or ethical principles into concrete corporate values that guide daily operations. The stronger effect of corporate values compared to Islamic values suggests that operationalization is key to realizing the governance benefits of religious principles. Managers should develop clear value statements, communicate them consistently, and embed them in organizational systems and processes.

Reframing Earnings Management

Rather than viewing all earnings management as problematic, boards and regulators should consider the motivations and outcomes of financial reporting flexibility. In values-driven organizations, some degree of earnings management may serve legitimate purposes such as conveying long-term value creation or protecting stakeholder interests during temporary disruptions. Governance frameworks should distinguish between opportunistic and values-aligned earnings management practices.

Holistic Governance Assessment

The findings suggest that governance quality assessment should extend beyond structural mechanisms to include cultural and values-based factors. Regulators and rating agencies operating in Islamic markets should develop governance metrics that capture the influence of Islamic principles and their implementation. This may include evaluating the presence of Sharia supervision, ethical investment policies, and stakeholder-oriented practices.

Leadership Development

The pervasive influence of values on governance underscores the importance of values-based leadership development. Organizations should select and develop leaders who embody organizational values and can effectively translate them into governance practices. Leadership training should emphasize the connection between personal values, organizational values, and governance outcomes.

7.3. Limitations and Future Research Directions

While this study provides valuable insights, several limitations should be acknowledged. First, the cross-sectional design limits causal inferences. Future research should employ longitudinal designs to examine how values-governance relationships evolve over time and in response to external shocks or leadership changes.

Second, the single-organization focus, while providing depth and consistency, limits generalizability. Future studies should examine whether similar relationships hold across different Islamic organizations, industries, and countries. Comparative studies between Islamic and conventional organizations would further illuminate the role of religious values in governance.

Third, the use of perceptual measures for earnings management, while appropriate for our research questions, could be complemented by archival measures in future studies. Triangulating perceptual and archival data would provide a more comprehensive understanding of how values influence actual financial reporting choices.

Fourth, the study's model explains governance outcomes but does not examine the performance implications of values-based governance. Future research should investigate whether the positive governance effects translate into superior financial performance, stakeholder satisfaction, or social outcomes.

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