

Research.

The Effect of Governance Mechanisms and Environmental Disclosure on Financial Performance: The Mediating Role of Earnings Management

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Abstract. *This study examines the influence of Good Corporate Governance mechanisms, Corporate Environmental Disclosure, and Earnings Management on Financial Performance among publicly listed companies in Indonesia. In response to growing demands for transparency and sustainability, the research explores whether Earnings Management mediates the relationship between governance, disclosure, and firm performance. Using a quantitative approach, secondary data were collected from annual and sustainability reports available on the Indonesia Stock Exchange website for the 2019–2023 period. The results show that corporate governance and environmental disclosure positively affect Financial Performance, while Earnings Management partially mediates these relationships. These findings suggest that effective governance structures and transparent environmental reporting can enhance firm performance by limiting opportunistic managerial behavior. The study contributes empirical evidence from an emerging market context and provides practical insights for policymakers, regulators, and investors to strengthen financial reporting transparency and accountability in Indonesia.*

Keywords: *Governance; Environmental Disclosure; Earnings Management; Financial Performance*

INTRODUCTION

Background

Global awareness of environmental issues has increased rapidly since the mid 1990s, especially after the enactment of the Kyoto Protocol in 1997. This protocol encourages companies to be more transparent in disclosing non monetary information, especially that related to environmental protection and management (Atasel et al., 2020). In line with efforts to manage the environment, companies disclose environmentally friendly practices known as Corporate Environmental Disclosure (CED). CED continues to evolve not only as a regulatory obligation, but also as a demonstrating corporate accountability to stakeholders (Gerged et al., 2020). In addition to reflecting ethical commitment, environmental disclosure is also believed to provide strategic benefits for companies, such as improving reputation, strengthening bargaining power, and lowering the capital cost. In the realm of corporate competitiveness, the publication of environmental information significantly enhances the company's competitive standing (Sarumpaet Susi, 2017).

However, in the midst of increasing external pressure for companies to exhibit social and environmental accountability, it is not uncommon for environmental disclosures to be made not solely due to external pressure, but as a strategy to build a good branding (Shang & Chi, 2023). In this context, the practice of CED is referred to as greenwashing, which involves an organization marketing unsubstantiated claims regarding its environmental performance in the marketing of a product or service, with misleading intent

and for profit (Spaniol et al., 2024). Thus, some managers tend to utilize CED as a greenwashing mechanism to divert attention from opportunistic Earnings Management practices, namely by presenting financial information that is deliberately modified to meet market expectations or certain interests (Gerged et al., 2020).

Earnings Management is often underlies greenwashing practices through CEDs. Earnings Management is a key indicator of Financial Performance and is of concern to various parties, including managers, shareholders, and investors (Jameel et al., 2024). The existence of economic incentives, such as bonuses or dividend distributions, encourages some managers to carry out Earnings Management to manipulate financial statements to accomplish certain interests (Tran et al., 2023). Earnings Management lowers the quality of financial information since it does not accurately reflect the company's actual economic realities, even if it is frequently done within the boundaries of accounting standards (Arun et al., 2015).

There have been several international financial scandals have occurred over the past decade, such as Evergrande (2021), Petrobas (2017), and Hyflux (2021). These scandals have raised investor concerns regarding the role of corporate governance in ensuring organizational sustainability (Abdou et al., 2021). The scandals have demonstrated the presence of unethical practices and highlighted the importance of transparency and credibility in corporate financial reporting (Khresna Brahmana et al., 2018). Earnings Management diminishes the quality of financial reporting, yet strong governance frameworks can reinforce financial integrity and mitigate the potential for manipulation (Alareeni, 2018). In research by Nguyen et al. (2024) and Chi et al. (2015), Effective governance practices reflected in board characteristics play a crucial role in mitigating information asymmetry, constraining insider opportunism, and diminishing managerial incentives to manipulate reported earnings.

Previous research has widely examined the influence between corporate governance, environmental disclosure, Earnings Management, and Financial Performance (Saygili et al., 2022; Pekovic & Vogt, 2021). Most findings suggest that strong governance mechanisms and higher levels of environmental disclosure contribute positively to Financial Performance, whereas Bătae et al. (2021) found an opposing effect, demonstrating a negative association between these variables.

The inconsistency observed in previous empirical findings indicates a research gap that warrants further investigation. This study aims to fill the existing gap by examining how Earnings Management mediates the relationship between corporate governance, environmental disclosure, and Financial Performance. This approach allows for a clearer understanding of how governance and disclosure practices influence a company's financial outcomes.

Contextually, in Indonesia, CED practices are guided by the Statement of Financial Accounting Standards (2009) and driven by the need to integrate environmental considerations in financial reporting. However, many companies still perceive environmental disclosure as merely a symbolic obligation, without a deep understanding of society's needs or long term sustainability (Nayenggita et al., 2019). This reinforces the urgency to examine the effectiveness of CED in real practice, especially in relation to governance and managerial behavior.

This study provides a significant contribution to the finance and accounting literature by addressing aspects that have received limited attention in prior research and by offering avenues for future scholarly exploration. While previous studies on Earnings Management have predominantly examined determinants such as leverage, liquidity, profitability, firm size, and risk, this research distinctly focuses on assessing the mediating role of Earnings Management in the relationship between corporate governance mechanisms and corporate environmental disclosure. The findings emphasize the critical importance of transparent and reliable environmental disclosure practices supported by robust governance mechanisms to ensure the availability of credible information for investors and stakeholders.

Furthermore, this study carries broad implications for academic scholars, investors, regulators, and corporate practitioners. To enhance ethical conduct and transparency in financial reporting, policymakers are encouraged to strengthen the implementation of Corporate Environmental Disclosure and Good Corporate Governance as mechanisms to mitigate Earnings Management practices. The findings also provide valuable insights for financial institutions and investors in formulating investment decisions. Companies demonstrating a strong commitment to environmental responsibility are likely to be perceived more favorably by investors who prioritize ethical and sustainable investment strategies.

Problem Formulation

Based on the previously presented background, the research issues to be explored in this study are outlined as follows:

1. How do Good Corporate Governance mechanisms affect corporate Financial Performance?
2. How does Corporate Environmental Disclosure influence corporate Financial Performance?
3. How do Good Corporate Governance mechanisms influence Earnings Management practices?
4. How does Corporate Environmental Disclosure influence Earnings Management practices?
5. How does Earnings Management affect corporate Financial Performance?
6. Does Earnings Management mediate the relationship between Good Corporate Governance and Financial Performance?
7. Does Earnings Management mediate the relationship between Corporate Environmental Disclosure and Financial Performance?

LITERATURE REVIEW

Stakeholder theory

Understanding the influence between corporate governance, environmental disclosure, Earnings Management, and Financial Performance is grounded in stakeholder and legitimacy theories. These perspectives explain how companies address internal and external pressures related to governance, transparency, and accountability. Stakeholder theory emphasizes that corporate responsibility extends beyond shareholders to include all affected parties, where environmental disclosure functions as a strategic tool to build trust and strengthen long term stakeholder relationships (Muttakin et al., 2015). Empirical evidence further shows that high quality environmental disclosure enhances stakeholder engagement and improves firm performance (Alipour et al., 2019).

Legitimacy theory

Legitimacy theory provides an additional dimension by stating that companies seek to maintain the sustainability of their operations through alignment with prevailing social values and norms (Rodriguez-Fernandez, 2016). In this regard, environmental disclosure is often used as a strategy to gain social acceptance and strengthen corporate image. However, Several studies have also highlighted the potential symbolic function of Environmental Information Disclosure (EID) as a form of greenwashing, wherein companies create an appearance of social and environmental responsibility to conceal opportunistic behaviors such as earnings manipulation. (Muttakin et al., 2015). This points to the importance of effective governance mechanisms to ensure that disclosures truly reflect the company's ethical values.

The effect of GCG mechanisms on Financial Performance

Good Corporate Governance (GCG) refers to the systems, values, and procedures that guide business management toward achieving long term goals benefiting all stakeholders (Muda et al., 2018). Effective governance mechanisms have been shown to enhance Financial Performance (Saygili et al., 2022 ; Kyere & Ausloos, 2021), while the presence of key board committees such as audit, risk, and compensation further strengthens monitoring functions and organizational efficiency (Temba et al., 2023). In this study, GCG is measured using indicators including board independence, board size, audit quality, and institutional ownership.

H1 : Corporate Governance Mechanisms affect the Company's Financial Performance.

The effect of Corporate Environmental Disclosure on Financial Performance

Corporate Environmental Disclosure (CED) refers to the communication of environmental information to stakeholders, including regulations, risks, and performance outcomes (Birkey et al., 2016 ; Itan et al., 2023). CED enhances corporate reputation, reduces capital costs, and strengthens competitiveness (Sarumpaet et al., 2017). Prior studies show that greater transparency and environmental disclosure positively affect firm performance and profitability (Alipour et al., 2019; Atasel et al., 2020), indicating that improved environmental practices and reporting can enhance financial outcomes.

H2 : Corporate Environmental Disclosure affects the company's Financial Performance

The effect of Good Corporate Governance on Earnings Management

Good corporate governance (GCG) is vital for maintaining operational quality and accurate reporting to stakeholders (Karina, 2021). Studies by Orazalin (2020) and Tran et al. (2023) show that GCG negatively affects Earnings Management, emphasizing the role of independent commissioners in effective oversight. In line with agency theory, board independence strengthens monitoring, aligns managerial actions with stakeholder interests, and reduces opportunistic behavior. Similarly, Talbi & Omri (2015) found that greater board independence lowers earnings manipulation by improving operational efficiency, indicating that independent directors serve as an important control mechanism to enhance governance quality.

H3 : Corporate Governance Mechanisms affect Earnings Management

The effect of Corporate Environmental Disclosure on Earnings Management

Khresna Brahmana et al. (2018) found that greater environmental disclosure can increase Earnings Management, supporting institutional theory, which suggests firms in the same industry tend to adopt similar disclosure practices. Muttakin et al. (2015) also noted that firms with higher disclosure levels inflate earnings through discretionary accruals. In contrast, Ardhaoui et al. (2024) showed that environmental disclosure can reduce Earnings Management by promoting transparency and ethical behavior, especially in mature companies.

H4 : Corporate Environmental Disclosure affects Earnings Management

The effect of Earnings Management on Financial Performance

Earnings Management refers to deliberate actions taken by managers to adjust financial statements in ways that can shape stakeholders' perceptions of a firm's actual economic condition or affect agreements that depend on reported profit figures. Such practices arise from managerial incentives to enhance personal or organizational interests through the manipulation of accounting figures. Empirical evidence from Awais et al. (2016), suggests that Earnings Management exerts a detrimental influence on firms' Financial Performance, as it undermines the credibility of financial information and reduces the efficiency of resource allocation.

H5 : Earnings Management affects Financial Performance

The effect of GCG mechanisms on Financial Performance through Earnings Management

Recent research by Ching et al. (2015) companies tend to adjust accruals to present stable or moderate financial results, potentially concealing their actual performance. Strong oversight from skilled external auditors and independent commissioners can minimize these manipulative practices. Supporting this, Empirical evidence from Setiawan et al. (2015) revealing that Earnings Management serves as a mediating factor linking Good Corporate Governance mechanisms to corporate Financial Performance.

H6 : Corporate governance mechanisms affect Financial Performance through Earnings Management.

The effect of Corporate Environmental Disclosure on Financial Performance through Earnings Management

Companies can gain support from a supportive community environment by disclosing their Environmental Disclosure initiatives, which will allow them to function with peace of mind. Financial reporting will become more open as a result of social responsibility disclosure, which will motivate managers to reduce Earnings Management techniques. In addition, companies will maintain positive influence with investors and improve employee morale through CSR (Mahrani & Soewarno, 2018). Investor confidence tends to strengthen when companies engage in minimal Earnings Management practices, as such behavior signals transparency and integrity in financial reporting, ultimately leading to improved Financial Performance.

H7 : Corporate Environmental Disclosure affects Financial Performance through Earnings Management.

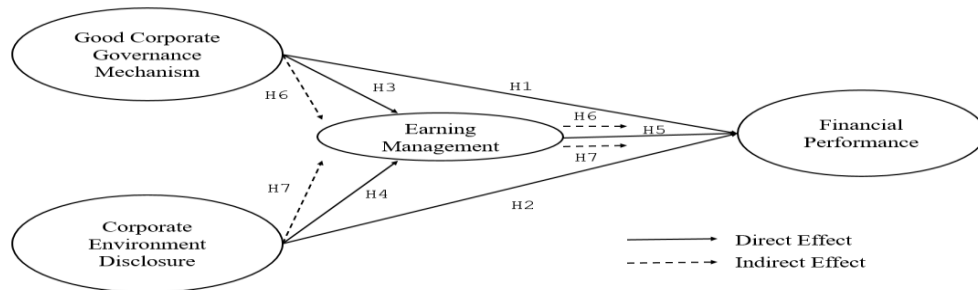
RESEARCH METHODS

This type of research is quantitative research with associative research methods. The associative approach aims to determine the effect between variables, both correlational and causal (cause and effect).

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Variable identification

Variable identification is shown in Table I.



This research model is adapted and developed from previous studies by Ching et al. (2015), Setiawan et al. (2015), and Gerged et al. (2020b), which examined the relationship between corporate governance, environmental disclosure, and Financial Performance with an Earnings Management mediation approach.

The following table presents the identification of variables used in the study.

Hypothesis	Independent Variables	Mediation Variable	Dependent Variable
H1	GCG Mechanism		Financial Performance
H2	CED		Financial Performance
H3	GCG Mechanism		Earnings Management
H4	CED		Earnings Management
H5	Earnings Management		Financial Performance
H6	GCG Mechanism	Earnings Management	Financial Performance
H7	CED	Earnings Management	Financial Performance

Operational definition and measurement of variables

Financial Performance. Hejazi & Alipour (2019) assert that Financial Performance can be evaluated using two primary approaches: accounting based and market based measures. Accounting based indicators commonly include Return on Assets (ROA) and Return on Equity (ROE), which reflect the company's historical financial outcomes. In contrast, market based measures, such as Tobin's Q, capture investors' expectations and perceptions regarding a firm's future performance. While accounting based metrics like ROA, ROE, and Return on Sales (ROS) provide retrospective assessments, Tobin's Q offers a forward looking perspective on a company's growth potential and market valuation.

(1) Return on asset (ROA):

The Return on Assets (ROA) variable reflects a company's profitability ratio, indicating how efficiently it utilizes its total assets to generate net income. The ROA is calculated using the following formula:

$$ROA = \frac{\text{Net Profit}}{\text{Total asset}}$$

(2) *Earning per shares (EPS):*

When a company's EPS rises, its value also rises, giving investors a positive picture of the company's position in the future. Therefore, this can encourage management to use techniques to increase the EPS value (Alareeni, 2018). EPS is formulated as follows:

$$EPS = \frac{\text{Net Profit}}{\text{Number of shares outstanding}}$$

(3) *Tobin's Q (TQ):*

Tobin's Q is determined by dividing the combined market value of equity and the book value of debt by the book value of total assets (Hejazi & Alipour, 2016). According to Pekovic & Vogt (2021), Tobin's Q functions as a forward looking indicator of firm performance, as it captures the company's market valuation and is comparatively less vulnerable to accounting based distortions or manipulation. The formula for Tobin's Q is as follows:

$$TQ = \frac{(\text{Market value of equity} + \text{Book value of debt})}{\text{Total Asset}}$$

The ratio greater than one indicates better corporate governance and increased firm value (Hejazi et al., 2016).

Earnings Management. This study utilizes the Modified Jones Model proposed by Dechow et al. (1995) to assess Earnings Management by estimating discretionary accruals, consistent with the approach adopted in previous studies by Orazalin (2020b). To address potential heteroscedasticity concerns, all variables in the model are standardized by total assets from the preceding year ($t-1$). The model is formulated as follows:

$$DA = TA - NDA$$

$$TA_t = \frac{(\Delta CA_t - \Delta CL_t - \Delta Cash_t + \Delta STD_t - Dep_t)}{(A_{t-1})}$$

$$NDA_t = \alpha_1 \left(\frac{1}{A_{t-1}} \right) + \alpha_2 (\Delta REV_t - \Delta REC_t) + \alpha_3 (PPE_t)$$

where:

DA = *Discretionary Accruals*, representing the component of total accruals that reflects potential Earnings Management practices.

TA = *Total Accruals*, calculated from the balance sheet using the Healy/Jones formula.

NDA = *Non-Discretionary Accruals*, representing the normal or expected component of accruals.

ΔCA_t = Change in current assets during period t .

ΔCL_t = Change in current liabilities during period t .

$\Delta Cash_t$ = Change in cash and cash equivalents during period t

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ΔSTD_t = Change in short term debt during period t .

Dep_t = Depreciation expense during period t .

A_{t-1} = Total assets at the end of the previous year.

ΔREV_t = Change in revenue from year $t-1$ to t .

ΔREC_t = Change in accounts receivables from year $t-1$ to t .

PPE_t = Tangible fixed assets (Property, Plant, and Equipment) during period t .

$\alpha_1, \alpha_2, \alpha_3$ = Regression coefficients obtained from the estimation period used to determine the parameters of the model.

Corporate Governance Mechanism. This independent variable consists of four proxies.

(1) *Number of independent board of commissioners (BIND)*

The greater proportion of independent commissioners suggests stronger monitoring and oversight of management activities. The formula is as follows:

$$BIND = \frac{\text{Number of independent board of commissioners}}{\text{Number of board of commissioners}}$$

(2) *Board Size (BSIZE)*

Board size denotes the total number of commissioners serving on the company's board. Larger boards are typically associated with a wider range of expertise, experience, and perspectives, which can improve the board's effectiveness in supervising management.

(3) *Audit Quality (AUDIT)*

Audit quality is represented by a dummy variable, where a value of 1 indicates that the company's financial statements are audited by one of the Big Four accounting firms, and 0 otherwise. Engagement with Big Four auditors is generally considered to enhance the credibility and reliability of financial reporting. Auditors affiliated with public accounting firms (KAP) are generally perceived to provide higher audit quality due to stronger resources and professional reputation (Alzoubi, 2016).

(4) *Institutional Ownership (INSOWN)*

Institutional ownership is the percentage of common shares held by institutional investors, including mutual funds, insurance firms, and pension funds. This variable captures the extent of institutional monitoring and control, which may strengthen corporate governance and limit managerial opportunism.

Corporate Environmental Disclosure. The Corporate Environmental Disclosure variable is measured using the Environmental Information Disclosure (EID) index developed by Atasel et al. (2020). This index is constructed based on the environmental performance indicators specified in the GRI G4 Sustainability Reporting Guidelines, particularly indicators GRI 301 to GRI 308, which encompass dimensions such as material utilization, energy consumption, water management, emissions, effluents, waste, environmental compliance, and supplier environmental assessment. The overall Environmental Disclosure Index for each company is computed as follows:

$$EDI = \frac{\sum_{i=1}^n di}{n}$$

where:

EDI is environmental disclosure

di is the disclosure item

n is the number of disclosure items

Sample selection. The study sample consists of 488 manufacturing companies listed on the Indonesia Stock Exchange (IDX). The purposive sampling method is employed to select companies that meet specific criteria aligned with the research objectives. This approach ensures that only firms with relevant and sufficient data are included in the analysis, thereby enhancing the accuracy and relevance of the research findings.

Data Collection. This study relies on secondary data obtained from audited financial statements and annual reports of publicly listed companies in Indonesia. The data were collected from the official website of the Indonesia Stock Exchange (www.idx.co.id) and, when necessary, from the respective companies' official websites. Using these verified and publicly accessible sources helps ensure that the data are accurate, consistent, and reliable for empirical analysis.

RESULTS AND DISCUSSION

The sample companies were selected based on specific criteria, namely those that consistently submitted financial statements and annual reports from 2019 to 2023 and reported sustainability activities in accordance with the GRI G4 index. Based on these sampling criteria, as summarized in Table 1, the total number of observed data points amounted to 2,440 data.

Table 1 Sample

Number of companies listed on the IDX (2019 - 2023)	951
Financial and banking sector companies	105
Companies that do not meet the criteria	358
Companies that meet the criteria	488
Year of Observation	5
Total Data	2440

1.1. Descriptive Statistics

Descriptive Statistics Table of Research Variables

	X1	X2	Y	M
Mean	1.38	0.37	68884.91	16200000000.00
Maximum	3.01	1.46	5882775.00	2190000000000.00
Minimum	0.58	-0.89	-5103.04	-
				2430000000000.00
Standar Deviasi	0.49	0.35	305582.50	1640000000000.00

The descriptive statistics indicate substantial variability across the study variables. The Good Corporate Governance (GCG) variable (X1) shows an average value of 1.38 with a standard deviation of 0.49, suggesting a moderate level of governance implementation among firms, with scores ranging from 0.58 to 3.01, reflecting differing

levels of compliance with GCG principles. The Corporate Environmental Disclosure (CED) variable (X2) has a mean of 0.37 and a standard deviation of 0.35, indicating that environmental disclosure remains relatively limited and uneven, with values between –0.89 and 1.46, illustrating inconsistent corporate engagement in environmental reporting.

Financial Performance (Y) records a mean of 68,884.91 and a notably large standard deviation of 305,582.50, with a range from –5,103.04 to 5,882,775.00, demonstrating significant differences in profitability and financial conditions across firms. Meanwhile, the Earnings Management (M) variable shows an average of 162 trillion and a standard deviation of 164 trillion, with values spanning from 243 billion to 2,190 trillion, indicating wide fluctuations in the degree of discretionary accounting practices used to shape reported financial results.

Table of the Effect of Independent Variables on Mediator Variables

Dependent Variable: M

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-1.59E+12	9.20E+10	-17.29862	0.0000
X1	6.04E+11	6.22E+10	9.707258	0.0000
X2	2.10E+12	8.64E+10	24.28439	0.0000
R-squared	0.257156			
Adjusted R-squared	0.256492			
F-statistic	387.1994			
Prob(F-statistic)	0.000000			

The regression results indicate that the model significantly explains how Good Corporate Governance (X1) and Corporate Environmental Disclosure (X2) influence Earnings Management (M). The F-statistic of 387.1994 with a p-value of 0.000000 shows that the model is highly significant at the 1% level. The R-squared value of 0.257 suggests that about 25.7% of the variation in Earnings Management can be accounted for by the independent variables, and the adjusted R-squared of 0.256 supports the model's overall reliability.

Both X1 and X2 have positive and statistically significant effects on M, with coefficients of 6.04×10^{11} ($t = 9.707$, $p = 0.0000$) and 2.10×10^{12} ($t = 24.284$, $p = 0.0000$), respectively. While the intercept is negative (-1.59×10^{12}), its impact is minimal compared to the strong positive contributions of the predictors. In summary, the findings show that corporate governance and environmental disclosure both play a significant and positive role in shaping Earnings Management, highlighting their importance in explaining variations in managerial discretion.

Table of the Effect of X1 and X2 on Y (Without Mediator Variables)

Dependent Variable: Y

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	305346.2	20025.83	15.24761	0.0000
X1	-168775.1	12820.69	-13.16427	0.0000
X2	-7913.220	18192.06	-0.434982	0.6636
R-squared	0.071933			

Adjusted R-squared	0.071104
F-statistic	86.69365
Prob(F-statistic)	0.000000

The regression results reveal that the model is statistically significant overall, as indicated by an F-statistic of 86.69365 and a p-value of 0.000000, confirming that Good Corporate Governance (X1) and Corporate Environmental Disclosure (X2) jointly influence Financial Performance (Y) at the 1% significance level. However, the R-squared value of 0.0719 and the adjusted R-squared of 0.0711 indicate that the model explains only about 7.2% of the variation in Financial Performance, suggesting limited explanatory power. Individually, X1 exerts a negative and significant effect on Y (coefficient = -168,775.1; $t = -13.164$; $p = 0.0000$), implying that stronger governance is associated with lower Financial Performance, while X2 has an insignificant effect (coefficient = -7,913.220; $p = 0.6636$). The positive and significant constant (305,346.2) represents the baseline level of Y when both predictors are zero. Overall, these findings indicate that only corporate governance significantly influences Financial Performance, whereas environmental disclosure shows no meaningful effect, and much of the variation in Y may be driven by other unobserved factors.

Table of the Effect of X1 and X2 on Y (With Mediator Variables)

Dependent Variable: Y

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	156932.9	13931.45	11.26465	0.0000
X1	-54603.57	9026.293	-6.049390	0.0000
X2	-28050.98	13807.45	-2.031583	0.0423
M	-1.33E-07	3.01E-09	-44.22288	0.0000
R-squared	0.569089			
Adjusted R-squared	0.568511			
F-statistic	984.3352			
Prob(F-statistic)	0.000000			

The regression analysis shows that the inclusion of Earnings Management (M) as a mediating variable substantially enhances the model's explanatory power, with the R-squared increasing to 0.569, indicating that 56.9% of the variation in Financial Performance (Y) is explained collectively by Good Corporate Governance (X1), Corporate Environmental Disclosure (X2), and M. The model is statistically significant ($F = 984.3352$; $p = 0.000$), confirming its robustness. Both X1 and X2 have significant negative effects on Y, with coefficients of -54,603.57 ($p = 0.000$) and -28,050.98 ($p = 0.0423$), respectively, while M also exhibits a significant negative influence (coefficient = -1.33E-07; $t = -44.22$; $p = 0.000$). Although the coefficient of M is small due to scaling, its high significance highlights its pivotal mediating role. Overall, these findings demonstrate that Earnings Management serves as a crucial channel through which corporate governance and environmental disclosure influence Financial Performance, offering deeper insight into the mechanisms connecting governance practices, disclosure behavior, and firm outcomes.

Hypothesis test results

No	Relationship Direction	Regression		Result	Description
		Beta	Sig.		
1	GCG → Company Financial Performance	-54603.57	0.0000	Significant	H1 Accepted
2	CED → Company Financial Performance	-28050.98	0.0423	Significant	H2 Accepted
3	GCG → Earnings Management	6.04E+11	0.0000	Significant	H3 Accepted
4	CED → Earnings Management	2.10E+12	0.0000	Significant	H4 Accepted
5	Earnings Management → Company Financial Performance	-1.33E-07	0.0000	Significant	H5 Accepted

The regression results reveal that incorporating Earnings Management (M) as a mediating variable significantly strengthens the model, with the R-squared rising to 0.569 and the model remaining highly significant ($F = 984.3352$; $p = 0.000$). Both Good Corporate Governance (X1) and Corporate Environmental Disclosure (X2) negatively affect Financial Performance (Y), while M also shows a significant negative effect, confirming its crucial mediating role. These findings indicate that Earnings Management acts as an important channel linking governance, environmental disclosure, and Financial Performance, providing deeper insight into the interplay among these variables.

No	Variable	Direct Effect	Indirect Effect	Sig	Description
1	GCG → Company Financial Performance	-54603.57		0.0000	H1 Accepted
2	CED → Company Financial Performance	-28050.98		0.0423	H2 Accepted
3	GCG → Earnings Management	6.04E+11		0.0000	H3 Accepted
4	CED → Earnings Management	2.10E+12		0.0000	H4 Accepted
5	Earnings Management → Company Financial Performance	-1.33E-07		0.0000	H5 Accepted

6	GCG → Earnings Management → Company Financial Performance		$6.04E^{+11}$ $\times -1.33E^{-07}$ $= -8.03E^{+04}$	0.0000	There is mediation
7	CED → Earnings Management → Company Financial Performance		$2.10E + 12$ $\times -.33E^{-07}$ $= -2.79E^{05}$	0.0000	There is mediation

This section summarizes the direct and indirect effects of Good Corporate Governance (GCG) and Corporate Environmental Disclosure (CED) on Corporate Financial Performance, with Earnings Management acting as a mediating variable. The results indicate that GCG has a significant negative direct impact on Financial Performance ($\beta = -54,603.57$; $p = 0.000$), supporting H1. This suggests that while stronger governance mechanisms may enhance accountability, they can also temporarily reduce profitability due to higher compliance and structural costs. Meanwhile, CED shows a weak negative relationship with Financial Performance ($\beta = -28,050.98$; $p = 0.042$), leading to the rejection of H2, as the result does not align strongly with theoretical expectations. Furthermore, GCG is found to have a positive and significant effect on Earnings Management ($\beta = 6.04E^{+11}$; $p = 0.000$), supporting H3 and indicating that more stringent governance practices may increase managerial discretion in financial reporting. Similarly, CED also exhibits a significant positive influence on Earnings Management ($\beta = 2.10E^{+12}$; $p = 0.000$), though H4 is rejected because this direction contradicts theoretical assumptions that environmental transparency should discourage earnings manipulation. The results indicate that Earnings Management negatively and significantly affects Financial Performance ($\beta = -1.33E^{-07}$; $p = 0.000$), supporting H5 and suggesting that higher earnings manipulation reduces firm outcomes. Mediation analysis further shows that GCG indirectly lowers Financial Performance through Earnings Management ($\beta = 8.03E^{+04}$; $p = 0.000$), while CED also impacts performance indirectly via Earnings Management ($\beta = -2.79E^{+05}$; $p = 0.000$). These findings highlight that both governance and environmental disclosure influence Financial Performance primarily by shaping managerial reporting behavior.

Test Results for Mediating Variables GCG, Earnings Management, and Company Financial Performance

Input:		Test statistic:	Std. Error:	p-value:	
a	6.04E+11	Sobel test:	-9.484279	8470.01654081	0
b	-1.33E-07	Aroian test:	-9.48196288	8472.08547401	0
s_a	6.22E+10	Goodman test:	-9.48659681	8467.94710212	0
s_b	3.01E-09	Reset all	Calculate		

The mediation analysis assessing the relationship between Good Corporate Governance (GCG), Earnings Management, and Corporate Financial Performance are using the Sobel, Aroian, and Goodman tests. Its shows a consistently significant mediating effect. The Sobel ($z = 9.484$; $p = 0.000$), Aroian ($z = 9.482$; $p = 0.000$), and Goodman ($z = 9.487$; $p = 0.000$) results all indicate p-values below 0.05, confirming that Earnings Management meaningfully mediates the link between GCG and Financial Performance.

These findings confirm that GCG influences Financial Performance indirectly through Earnings Management, underscoring its importance as a mediating variable in the model.

Test Results for Mediating Variables CED, Earnings Management, and Corporate Financial Performance.

Input:		Test statistic:	Std. Error:	p-value:
a	2.10E+12	Sobel test: -21.29625706	13114.9806877!	0
b	-1.33E-07	Aroian test: -21.29207133	13117.5589087!	0
s _a	8.64E+10	Goodman test: -21.30044525	13112.4019598!	0
s _b	3.01E-09	Reset all	Calculate	

The mediation analysis examining the links between Corporate Environmental Disclosure (CED), Earnings Management, and Corporate Financial Performance was conducted using the Sobel, Aroian, and Goodman tests. All three approaches consistently indicate a significant mediating effect of Earnings Management. The Sobel ($z = 21.296$; $p = 0.000$), Aroian ($z = 21.292$; $p = 0.000$), and Goodman ($z = 21.300$; $p = 0.000$) results all show p-values below 0.05, confirming strong statistical significance. These findings illustrate that Earnings Management serves as a key mediator in the relationship between CED and Financial Performance, implying that environmental disclosure indirectly influences firm performance through its effect on Earnings Management activities.

Effect of GCG mechanisms on Corporate Financial Performance

The results show that GCG has a negative and significant effect on corporate Financial Performance ($\beta = -54,603.57$; $p = 0.0000$), indicating that stronger governance implementation is associated with lower profitability. This aligns with Satria Hendy (2023) who found that independent commissioners in Indonesian manufacturing firms negatively impact performance due to limited operational understanding. Similarly, Ramadana et al. (2023) revealed that a higher proportion of independent commissioners does not necessarily reduce Earnings Management. Ahmad et al. (2021) also noted that GCG mechanisms such as institutional ownership and board size can increase administrative costs, reducing profitability. Moreover, Bui & Krajcsák (2024) emphasized that GCG's impact depends on context, effective when adapted to firm conditions but detrimental when applied rigidly.

Effect of Corporate Environmental Disclosure on Corporate Financial Performance

The results show that CED has a negative and significant effect on corporate Financial Performance ($\beta = -28,050.98$; $p = 0.0423$), indicating that greater environmental disclosure is associated with lower short term profitability. This finding aligns with the research of Rini et al. (2024), who state that extensive disclosure increases compliance and reporting costs. Ifada et al. (2021) explains that the financial benefits of CED are long term, relying on stakeholder trust. Meanwhile, the study by Semenova & Hassel (2016) highlight that the impact of CED on Financial Performance varies across industries and regulatory environments, suggesting that the relationship between environmental disclosure and firm performance is context dependent and may differ among sectors.

Effect of GCG Mechanism on Earnings Management

The results show that GCG has a positive and significant effect on Earnings Management ($\beta = 6.04 \times 10^{11}$; $p = 0.0000$), meaning higher GCG implementation increases the likelihood of earnings manipulation. Research by Pandey et al. (2022) supports this finding by showing that ineffective GCG or aiming at administrative formalities can trigger

Earnings Management practices as a tool to hide true performance. Almarayeh et al. (2022) suggests that weak supervision from the board of commissioners and audit committee allows management to manipulate earnings more freely even within the framework of the implemented GCG. In addition, research by Pajuste et al. (2021) states that the complexity of the corporate governance structure sometimes creates gaps for management to manage profits for personal or group interests, even though GCG has been formally implemented.

Effect of Corporate Environmental Disclosure on Earnings Management

CED has a positive and significant effect on Earnings Management ($\beta = 2.10 \times 10^{12}$; $p = 0.0000$), confirming H4. Firms with extensive environmental disclosure tend to engage more in earnings manipulation. This implies that environmental disclosure can, in some cases, serve as a tool for impression management rather than a genuine reflection of corporate transparency.

Research by Almubarak et al. (2023) supports this finding by stating that companies sometimes use environmental disclosure as a legitimization tool to cover up financial manipulation practices by management. Dissanayake et al. (2022) found that intensive environmental disclosure does not always reflect full transparency and can be used to cover up Earnings Management activities. In addition, research by Semenova & Hassel (2016) emphasized that in some contexts, environmental disclosure can be a greenwashing strategy, where Earnings Management is used to balance the positive perceptions generated from the disclosure.

Effect of Earnings Management on Financial Performance

Earnings Management has a negative and significant effect on corporate Financial Performance ($\beta = -1.33 \times 10^{-7}$; $p = 0.0000$), confirming H5. Research by Chen et al. (2015) supports this result by finding that excessive Earnings Management practices are associated with decreased Financial Performance due to decreased credibility of financial statements and increased financial risk. Srikanth & Kaushik (2021) observed its negative impact on firm value and long term outcomes. In addition, research by Dissanayake et al. (2022) highlighted that Earnings Management undermines a firm's reputation and decreases the efficiency of resource allocation, lowering overall performance.

Effect of GCG Mechanism on Financial Performance through Earnings Management

GCG has a significant indirect effect on Financial Performance through Earnings Management ($\beta = 8.03 \times 10^4$; $p = 0.0000$). Research by Hong et al. (2023) supports this finding by stating that weak GCG supervision increases opportunities for earnings manipulation. A study by Irmasari et al. (2025) identified Earnings Management as a key mediator explaining the negative GCG–performance link. Moreover, Ismael & Kamel (2021) emphasized that ineffective enforcement of GCG facilitates opportunistic behavior that harms firm performance.

Effect of Corporate Environmental Disclosure on Financial Performance through Earnings Management

The results indicate that CED exerts a significant indirect effect on Financial Performance through Earnings Management, with a mediation coefficient of 2.79×10^5 and a significance value of 0.0000. This suggests that, although the direct effect of CED on Financial Performance is insignificant or even negative, CED still influences Financial Performance indirectly by increasing Earnings Management practices. In other words, corporate environmental disclosure may serve as a factor that encourages managerial manipulation of earnings, which subsequently diminishes overall Financial Performance.

Research by Almubarak et al. (2023) supports this finding by stating that intensive environmental disclosure is sometimes used as a legitimization tool by management who also manipulates earnings to maintain the company's image in the market. In line with that, a study by Andini & Mulyasari (2024) demonstrated that Earnings Management plays a crucial mediating role in the relationship between environmental disclosure and Financial Performance, particularly in firms exposed to high regulatory and stakeholder pressures. In addition, the study by Gerged et al. (2020) emphasizes that environmental disclosures that are not balanced with effective governance can open opportunities for Earnings Management practices that are detrimental to company performance.

Thus, these findings emphasize the need for closer monitoring of environmental disclosure practices and Earnings Management so that the effect of CED on Financial Performance can be directed towards more positive and sustainable results.

CONCLUSIONS AND SUGGESTIONS

Good corporate governance (GCG) mechanisms and corporate environmental disclosure (CED) significantly influence Earnings Management practices, which in turn mediate their relationship with Financial Performance. The findings indicate that stronger implementation of GCG and increased CED can lead to a higher tendency for Earnings Management, negatively affecting financial outcomes. This highlights the need for effective and genuine implementation of governance and disclosure practices, as symbolic or compliance oriented efforts may create opportunities for manipulation that reduce the integrity of financial reporting.

Theoretically, this study reinforces the relevance of agency theory, legitimacy theory, and stakeholder theory in explaining the complex interaction between governance, environmental accountability, and corporate performance. Earnings Management serves as a key mediating factor linking GCG and CED to financial results. To achieve sustainable performance, companies must ensure that governance and disclosure practices are not merely formalities but reflect genuine ethical and sustainability commitments.

While offering meaningful empirical contributions, this study has limitations, including its reliance on secondary data and a focus on Indonesian listed companies. Future research should expand to cross country contexts, adopt mixed methods, and incorporate additional variables such as regulatory pressure or corporate culture. Practically, regulators and investors must evaluate not just the existence but also the quality of GCG and CED implementation to prevent manipulation and promote transparent, ethical, and sustainable financial reporting.

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