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The Influence of Profitability and Cash Holding on Income Smoothing in an Islamic Perspective

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ABSTRACT

This study aims to analyze the effect of profitability and cash holdings on income smoothing from an Islamic perspective in Islamic commercial banks in Indonesia from 2020 to 2023. The sampling technique used was purposive sampling with 10 Islamic commercial banks in Indonesia over 4 years. This study used a quantitative approach using logistic regression. The model testing uses the Hosmer and Lemeshow model goodness-of-fit test, the coefficient of determination test, and the partial and simultaneous significance tests. The study's results indicate that, partially, profitability and cash holdings do not influence income smoothing, as evidenced by the significance values of each variable being greater than 0.05. However, simultaneously, both variables influence income smoothing. From an Islamic perspective, the results of this study indicate that Islamic commercial banks are committed to the principles of transparency, honesty, and accountability in financial reporting. This study found no indication that Islamic bank management smokes income based on profitability or cash holdings. This study expands the literature on Islamic accounting by emphasizing the importance of ethical and responsible profit management and providing an overview of how Islamic principles are applied in current financial practices.

Keywords: Profitability, Cash Holding, Income Smoothing.

JEL Code: M41, M42, G21, G32, Z12.

I. Introduction

Financial statements reflect a company's condition and contain information needed by parties interested in the company. Financial statements present important information about an entity's financial condition, performance, and cash flow in a specific period. Financial statements are crucial for both internal and external parties. For internal parties, financial statements serve as a tool for managers to assess company performance and as a basis for decision-making and policy formulation. Meanwhile, for external parties, financial statements are used for various purposes, such as tax calculations and as a benchmark for performance evaluation by investors (Lufianda & Syafri, 2023). Financial statements contain important information, namely balance sheets, income statements, cash flow statements, statements of changes in equity, and notes to the financial statements. These components provide a comprehensive picture of the entity's financial condition, enabling stakeholders to make better decisions based on the available



information. This is the focus of attention in measuring management performance or accountability, and it also helps owners assess the company in the coming period. In the banking sector, Islamic commercial banks can attract investors to invest their funds to run operations based on profit-sharing principles in accordance with Islamic principles (Harianto et al., 2020). The development of Islamic banking has always experienced an increase, showing improved performance from year to year (Khairun Nisa, Atika, 2024). This is reflected in the continuous growth of businesses, investment funds, public deposits, and financing disbursements, which are increasing daily. Banking itself, as a financial system that functions as a financial intermediary, is an institution that plays a role in efficiently bringing together fund owners and users on a macro and micro scale (Rahmaniar & Fitriani Rizky, 2022). As an institution operating under Islamic law, Islamic banks are expected to present financial information honestly, transparently, and without manipulation, including income smoothing practices. This must be reviewed in accordance with the principles of honesty (sidq), fairness ('adl), and responsibility (Iskandar et al., 2022). In financial statements, profit in business is considered potential information because profit determines whether a company's performance is good or bad. Banks that earn high profits can be more stable in determining the profit-sharing ratio for customers, thus providing certainty for investors. If profits fluctuate, but with sufficient cash reserves, the bank can pay stable profit-sharing ratios to customers. This helps maintain fair and stable profit-sharing ratios for all parties (Assefa et al., 2021). A manager is typically associated with the company's performance, which is presented through reported profits. This profit information encourages managers to manage the profits earned by the company, commonly known as income smoothing, to attract investors by creating a better performance than the actual condition (Nasrifah, 2022).

The phenomenon of income smoothing has also led to cases in the financial statements of Indonesian banks. One issue related to income smoothing is at PT Bank Bukopin Tbk. Detik Finance (2018) reported that one of the banks that made changes or revisions to its financial statements is PT Bank Bukopin Tbk, which revised its financial statements for 2015, 2016, and 2017. It was noted that the bank modified credit cards over five years, with over 100,000 credit cards being modified. The commission income and initial administrative fees from credit card income decreased from 1.06 trillion to 317.88 billion, and there was an increase in provisions for losses due to the decline in the value of specific debtors. The bank's management also revised the 2016 net profit from Rp 1.08 trillion to Rp 183.56 billion. The existence of income smoothing in companies has led to several scandals in financial reports, which have caused concern among users of financial reports, especially regarding the issue of transparency (El-halaby et al., 2021).

Previous studies have extensively examined income smoothing practices, both in the context of public companies and conventional banking. However, research specifically examining the influence of profitability and cash holdings on income smoothing in Islamic commercial banks, particularly from an Islamic perspective, is still limited. Additionally, previous studies have shown varying results regarding these two variables, leaving room for further examination. For example, research conducted by Winanda and Putra Astika (2021) and Inayah and Izzaty (2021) states that profitability does not affect income smoothing, while research conducted by Marlina and Samosir (2022) states that profitability affects income smoothing. In the studies by Milasari et al. (2024) and Mangngalla & Kartini (2022), it was stated that cash holdings do not affect income smoothing. However, the studies conducted by Andini & Agustina (2020) and Angreini & Nurhayati (2022) stated that cash holdings affect income smoothing. Given these issues, this study focuses on the influence of profitability and cash holdings on income smoothing in Islamic commercial banks in Indonesia from 2020 to 2023. This study can help evaluate the extent to which Islamic commercial banks have managed their finances honestly and transparently so that, in their operations, they not only consider economic aspects but also social, moral, and ethical values of financial management from an Islamic perspective. It can also contribute new insights to enrich the literature on income smoothing in Islamic financial institutions, which has been more extensively studied in conventional financial institutions.

II. Literature Review and Hypothesis Development

2.1. Agency Theory

Agency theory explains the relationship between owners/shareholders (principals) and managers (agents), which is assumed to be a factor in the emergence of income smoothing practices. Shareholders authorize management to run the business in accordance with the agreed contract. Meanwhile, management is granted the authority to manage costs with full responsibility by the principal. It is said that agents seek to maximize their personal interests and do not always act according to the principal's wishes. This conflict arises when all parties strive to achieve or maintain the level of prosperity they desire, and the differences in interests between management and owners often influence the policies approved by management (Sarah et al., 2023). The difference in interests between the two parties, especially on the part of managers whose performance is assessed based on reported profits, causes managers to try to achieve their goals by smoothing income in financial reports to attract investors (Mutinda, 2024). Income smoothing practices can be identified through higher profitability and cash flow, which give managers more room to manage profits (Lim & Yong, 2020). Practices carried out to deceive others are considered haram and prohibited in Islam. As Allah SWT says, prohibiting cheating in (Q.S. An-Nisa [4]: 29).

يَا أَيُّهَا الَّذِينَ آمَنُوا لَا تَأْكُلُوا أَمْوَالَكُمْ بَيْنَكُمْ بِالْبَاطِلِ إِلَّا أَنْ تَكُونَ تِجَارَةً عَنْ تَرَاضٍ مِنْكُمْ وَلَا تَقْتُلُوا أَنْفُسَكُمْ إِنَّ اللَّهَ كَانَ بِكُمْ رَحِيمًا

"O you who believe, do not consume one another's wealth unjustly, except in a manner that is mutually agreed upon among you. Do not kill yourselves. Indeed, Allah is Most Merciful to you." (Q.S. An-Nisa [4]: 29).

The verse emphasizes the prohibition of consuming the wealth of others through unjust means and commands fair transactions. Islam prohibits all forms of fraud (tadlis) and uncertainty (gharar), including income smoothing practices that can manipulate a company's financial statements. The management of assets must adhere to Sharia principles, namely honesty, fairness, trustworthiness, and transparency, with the permission of Allah. In reality, income smoothing is an act of manipulating profits that can eliminate Allah's pleasure. The consequences of such practices result in inaccurate reported profits and may harm specific stakeholders, as they do not accurately reflect the company's financial condition. However, Fatwa DSN-MUI No. 87/DSN-MUI/XII/2012 permits the formation of reserves for income smoothing in Islamic banks, provided it is approved by customers and done to maintain the stability of customer returns (Mardian, 2022).

2.2. Income Smoothing

Company managers deliberately take income smoothing to reduce excessive profit fluctuations in financial statements. This usually occurs because the profits generated do not meet the company's expectations. This practice can be detrimental to many parties, especially investors, because they do not know the position and fluctuations in the company's finances. Income smoothing can be understood from the agency theory perspective, which states that income smoothing is driven by conflicts of interest between management (agents) and owners (principals). Several factors that cause income smoothing include bonus purposes, political motivation, and taxation motivation, which can motivate management to engage in income smoothing based on personal or company interests. Many managers view income smoothing as a reasonable and ethical action and a legitimate tool for managers to fulfill their responsibility to generate company returns. Although income smoothing is based on applicable financial accounting standards, it does not mean it is an appropriate action to justify fraud. In predicting income smoothing, investors must analyze and assess the company's financial condition. In line with agency theory, the agency relationship serves as the foundation for understanding corporate governance and the issue of income smoothing practices. In this

context, profitability and cash holdings can be used to predict income smoothing and serve as considerations for investors when making investment decisions. (Abogun & Adigbole, 2021).

2.3. Profitability

Profitability ratios can be used to assess the efficiency of banks in generating profits or earnings through utilizing their assets. Profitability is one of the indicators of a company's ability to generate profits. If a company's profitability increases, it indicates that the company has the capacity to generate income and will also provide benefits to investors because the company strives to manage investment funds maximally, enabling the company to achieve the expected profits. To assess the health of a company, investors typically use return on assets (ROA) when making decisions. The formula used to calculate profitability is as follows:

$$ROA = \frac{\text{Net Income}}{\text{Total Assets}} \times 100\%$$

Profitability is one of the internal factors that can influence management's tendency to engage in income smoothing, as low profitability provides a poor picture, causing a manager's performance to appear poor in the eyes of investors (Octafilia et al., 2020). Therefore, companies with low profitability are often driven to engage in income smoothing to maintain investor confidence. Conversely, companies with high profitability may feel less pressure from the market and do not require income smoothing techniques. This aligns with the findings of studies by Hendrastuti and Harahap (2023) and Marlina and Samosir (2022), which state that profitability influences income smoothing, as investors are more interested in companies with stable profitability, as they are perceived to be effective in generating profits. This is reinforced by agency theory, which states that management is incentivized to present financial statements with stable profits to reduce the risk of negative perceptions from principals (Pratami et al., 2024). Based on agency theory and previous research results, managers under pressure to demonstrate good performance tend to be driven to engage in income smoothing.

2.4. Cash Holding

Cash holdings are the amount of cash or liquid assets a company has to support its operations (Mariska et al., 2025). The information in the financial statements regarding the company's cash allows investors to assess management performance. A stable increase in cash within a company makes management performance appear favorable to investors. Maintaining stable cash reserves indicates that the company has a low risk level, as it is perceived as capable of fulfilling its obligations. This aligns with agency theory, where the relationship between owners and company managers carries the potential for conflicts of interest. As agents, managers are incentivized to present stable financial statements to be positively evaluated by owners. Companies with significant cash holdings have high flexibility in managing revenue or expense recognition, enabling management to implement strategies to achieve objectives, including stabilizing reported profits (Haj-salem, 2021). Managers use cash holdings as a tool in running company operations. Cash holdings can be calculated using the following formula:

$$\text{Cash Holding} = \frac{\text{Cash and Cash Equivalent}}{\text{Total Assets}} \times 100\%$$

Cash holdings should not be used to conceal the actual financial condition of a company. Cash holdings are significant for companies because they can be used to carry out activities within the company

(Habib et al., 2021). The same opinion is expressed by Musyafa and Kholilah (2023) that cash holdings are significant because they provide liquidity for companies, meaning that companies can pay off their obligations in critical situations. This aligns with the research of (Andini & Agustina, 2020) and (Afninofia et al., 2023), which states that cash holdings influence income smoothing. In agency theory, extensive cash holdings allow managers to make decisions that benefit themselves through income smoothing practices.

This study aims to determine how profitability and cash holdings influence income smoothing. A detailed theoretical framework has been developed to understand each indicator used in this study. Previous studies have provided diverse conclusions regarding the factors influencing income smoothing. A hypothesis is an initial assumption in the problem statement formulated as a question. They are called initial assumptions because these statements are derived from relevant theories and have not yet been based on facts that will be obtained through data collection. Based on the above explanation, this study proposes the following hypotheses:

- H1: Profitability influences income smoothing
- H2: Cash holdings influence income smoothing
- H3: Profitability and cash holdings jointly influence income smoothing

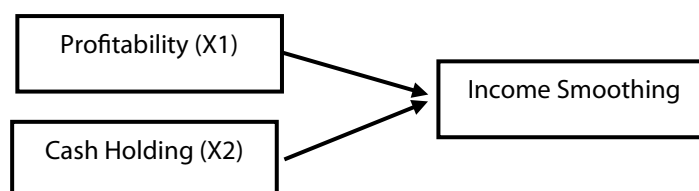


Figure 1. Conceptual Framework

III. Research Method

The type of research used is quantitative, which reveals the magnitude or smallness of an influence or relationship between statistical variables by collecting data that supports the influence between variables to test the established hypothesis (Sugiyono, 2020). This study analyzes the relationship between independent variables, namely profitability and cash holdings, and the dependent variable, namely income smoothing. This study uses logistic regression analysis because the dependent variable is dichotomous or can be referred to as a dummy variable (0 and 1), where a company suspected of not engaging in income smoothing is assigned a value of 0. A company suspected of engaging in income smoothing is assigned a value of 1 (Hilbe, 2019). This regression determines whether profitability and cash holdings influence income smoothing. The study covers a period of 4 years (2020-2023).

3.1. Population and Sample

The population consists of objects with specific qualities and characteristics that the researcher determines to be studied, and then conclusions are drawn. The sample itself is part of the characteristics possessed by the population. The sampling method used in this study is purposive sampling, a sample selected based on the suitability of the sample characteristics determined to obtain a representative sample (Lenani, 2021). The population in this study is all Islamic commercial banks in Indonesia, and 10 samples were obtained based on predetermined criteria. The criteria used in this study are as follows:

- a. Banks classified as Islamic commercial banks (not Islamic business units)
- b. Banks that publish annual financial reports in rupiah
- c. Observation period 2020-2022

3.2. Data Sources

This study uses secondary data, which has been collected and is available from other sources (Andini & Agustina, 2020). The data in this study were obtained from the annual financial reports of each Islamic commercial bank for the period 2020-2023.

3.3. Data Analysis Techniques

Data analysis techniques used descriptive analysis, model feasibility testing using the Hosmer and Lemeshow goodness of fit test, coefficient of determination test, logistic regression analysis, partial testing, and simultaneous testing. All data processing in this study was performed using Eviews 10 software.

1. Analisis Descriptive Analysis

Descriptive statistical analysis is used to describe the characteristics of the sample in terms of the highest value, lowest value, standard deviation, and mean value. This test reveals ways of presenting data using frequency distributions, ordinary tables, circles, bar, or line graphs (Mutinda, 2024).

2. Regression Model Suitability Test

- Hosmer and Lemeshow's Goodness of Fit Test

This test uses the following hypotheses:

H0: There is no significant difference between the predicted classification and the observed classification (Model fits/matches the data)

H1: There is a significant difference between the predicted classification and the observed classification (The model does not fit/match the data)

If sig > 0.05, H0 is accepted.

If sig < 0.05, H0 is rejected.

If the goodness-of-fit test measured in the Hosmer and Lemeshow test is greater than 0.05, then H0 is accepted, and the regression model is suitable for further analysis.

3. Coefficient of Determination Test (Nagelkerke's R Square)

Suppose the coefficient of determination value approaches 0. In that case, the influence of the independent variable on the dependent variable is negligible. However, if the coefficient value approaches 1, the influence of the independent variable on the dependent variable is greater (Lauren & Nugroho, 2024).

4. Logistic Regression Analysis

This regression is suitable for research where the dependent variable is dichotomous (performing profit leveling and not performing profit leveling), with Y = 1 indicating the presence of a characteristic and Y = 0 indicating the absence of a characteristic. Logistic regression is a logit equation (Rahmaniar & Fitriani Rizky, 2022).

$$\text{Logit}(p) = \beta_0 + \beta_1 X_1 + \beta_2 X_2$$

5. Partial Significance Test

The partial test determines the effect of each independent variable, namely profitability and cash holdings, on the dependent variable, namely income smoothing. The decision criteria used in this partial test are based on the significance level, namely, if sig < 0.05, it can be said that the independent variable hypothesis partially affects the dependent variable. If sig > 0.05, then the hypothesis of the independent variable partially does not affect the dependent variable (Fadillah & Luthan, 2023).

6. Simultaneous Significance Test

This test determines whether the independent variables collectively influence the dependent variable (Afninofia et al., 2023). The likelihood ratio test (LRT) is used in this logistic regression. If the probability value is < 0.05, H0 is rejected and H1 is accepted if the probability value is > 0.05.

IV. Results and Discussion

4.1. Statistical Result

4.1.1 Descriptive Statistic Test Result

Table 1. Descriptive Statistics Test

Variable	Obs	Mean	Std. Dev	Min	Max
Profitability	40	-0,934978	9,436273	-56,71095	16,93727
Cash Holding	40	5,596316	23,23505	0,033609	118,4692
Income smoothing	40	0,700000	0,464095	0,000000	1,000000

Based on the results in Table 1, the number of observations used in the study is 40, for the average value of the profitability variable is -0.93, the cash holding variable is 5.60, and the average value of the income smoothing variable is 0.70. The standard deviation value on the profitability variable is 9.44, the cash holding variable is 23.24, while the income smoothing variable has a standard deviation of 0.46. The minimum value of each variable is -56.71 for profitability, 0.03 for cash holding, and 0.00 for income smoothing. The maximum value of the profitability variable is 16.94, the cash holding variable is 118.47, and the income smoothing variable is 1.00. The statistical results in the table above show that the profitability variable has a minimum value of -56.71095 and a maximum value of 16.93727. These results prove that the profitability is between -56.71095 and -16.93727. The mean (average) value is -0.934978 at a standard deviation of 9.436273, which means that the mean value is smaller than the standard deviation, so it is stated that the profitability value is uneven, or the difference between one data point and another is high. The descriptive statistical results in the table above show that the minimum value of the cash holding variable is 0.033609 and the maximum value is 118.4692. These results prove that the value of cash holding ranges from 0.033609 to 118.4692. The mean value of the cash holding variable is 5.596316 with a standard deviation value of 23.23505, which means that the mean value is smaller than the standard deviation, so it is stated that the value of cash holding is uneven, or the difference between one data point and another is high. The above analysis shows that profitability and cash holdings vary significantly. ROA is considered good if it is above 1.5-2%, but in this study, the average profitability was -0.93, reflecting the challenges faced by several banks during the study period. Meanwhile, cash holdings averaged 5.60%, indicating that banks had a pretty good level of liquidity.

4.1.2 Hosmer and Lemeshow's Goodness of Fit Test

Table 2. Results of Hosmer and Lemeshow's Goodness of Fit Test

Statistic	Value	Degrees of freedom	p-value Prob. Chi-Sq
H-L Statistic	2,2448	8	0,9726
Andrews Statistic	3,2475	10	0,9750

Table 2 explains that the H-L Statistic value is 2.2448 with a significance probability of 0.9726, where the value is more than 0.05. So that H0 is accepted, the model can be accepted because it is in accordance with the observation data, because the statistical value of Hosmer and Lemeshow's goodness of fit test > 0.05.

4.1.3 Test of the Coefficient of Determination (Nagelkerke's R Square)

Table 3. McFadden R² Test Results

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	-0,012637	0,668226	-0,018911	0,9849
Profitability	-2,252652	2,219539	-1,014919	0,3101
Cash Holding	5.456325	4,157825	1,312303	0,1894

McFadden R-squared	0,137707	Mean dependent var	0,700000
S.D. dependent var	0,464095	S.E. of regression	0,444691
Akaike info criterion	1,204343	Sum squared resid	7,316763
Schwarz criterion	1,331009	Log likelihood	-2108685
Hannan-Quinn criterion	1,250141	Deviance	42,17371
Restr. deviance	48,86914	REstr. Log likelihood	-24,43457
LR statistic	6,695435	Avg. Log likelihood	-0,527171
Prob (LR statistic)	0,035165		
Obs with Dep = 0	12		
Obs with Dep = 1	28		
Total obs	40		

This test determines the percentage of variation in variable Y that the variables in the model can explain, while other variables outside the model explain the rest. Based on the table above, the McFadden R-Squared value is 0.137007. This shows that the independent variables in the model can explain changes in the probability of income smoothing by 13.7% and other variables outside the model of this study can explain 86.3%.

4.1.4 Logistic Regression Analysis

Table 4. Logistic Regression Test Result

Variable	Coefficient	Std. Error	z-Statistic	Prob
C	-0,012637	0,668226	-0,018911	0,9849
Profitability	-2,252652	2,219539	-1,014919	0,3101
Cash Holding	5,456325	4,157825	1,312303	0,1894

Based on the results in Table 4, the logit model equation is obtained as follows:

$$\text{Logit (Y)} = -0,012637 - 2,252652 \times \text{Profitability} + 5,456325 \times \text{Cash Holding}$$

Based on the regression equation in Table 4, the regression coefficient for the constant is -0.012637 with a p-value of 0.9849, meaning that the constant is not statistically significant. The negative coefficient value for the profitability variable of -2.252652 indicates that statistically, every increase in profitability tends to reduce income smoothing practices, as the probability value of 0.3101 > 0.05 shows a statistically insignificant relationship at the 95% confidence level, thus having no effect. The positive coefficient value for cash holdings of 5.456325 indicates that cash holdings tend to increase the likelihood of income smoothing. The p-value of 0.1894 > 0.05 indicates a statistically insignificant relationship. Therefore, the profitability and cash holdings variables do not influence income smoothing because the p-value > 0.05.

4.1.5 Partial Significance Test

A partial test determines the effect of each independent variable, namely profitability and cash holding, on the dependent variable, namely income smoothing. The decision-making criteria used in this partial test are based on the significance level, namely, if sig < 0.05, then it can be said that the independent variable hypothesis partially affects the dependent variable. If sig > 0.05, the independent variable hypothesis does not affect the dependent variable. Based on Table 4 above, the hypotheses can be interpreted: the hypothesis on variable X1 (H1): profitability significantly affects income smoothing. The results of the test can be obtained by calculating the Z value from the logistic regression above, of -1.0114919, and a significance level (probability) of 0.3101 (p > 0.05) with a regression coefficient value of -2.252652. So it can be concluded that profitability as an independent variable has no significant effect on the dependent variable, namely

income smoothing. The negative sign on the coefficient shows the opposite relationship: the higher the profitability, the greater the tendency to practice income smoothing. Thus, H1, which states that profitability significantly affects income smoothing, is rejected.

4.1.6 Simultaneous Significance Test

This test determines whether the independent variables jointly affect the dependent variable. In this logistic regression, the Likelihood Ratio Test (LRT) is used, where H0 has no effect simultaneously because the probability value < 0.05 , H0 is rejected, and H1 is accepted if the probability value > 0.05 , then there is a simultaneous influence. Based on the table above, the F test results show that the LR statistic is 6.695435 with a probability value (LR statistic) of $0.035165 > 0.05$, which means that the profitability and cash holding variables simultaneously or together have a significant effect on income smoothing practices in Islamic commercial banks 2020-2023.

4.2. Discussion

4.2.1. Effect of Profitability on Income Smoothing

Based on the results of the data analysis Table 4, the calculated z-value from the logistic regression above is -1.0114919 ($p < 0.05$). Profitability has a regression coefficient of -2.252652 with a significance level of 0.3101 . Since the significance value is greater than 0.05 ($0.3101 > 0.05$), hypothesis 1 (H1) is rejected. It can be concluded that profitability does not affect income smoothing. Profitability indicates a bank's efficiency in generating profits by utilizing its assets. This serves as a tool for investors to predict risk and returns in investments and enhances investor confidence in the company. Theoretically, the results of this study align with agency theory, which states that strong oversight and good governance can prevent managers from acting opportunistically. (Winanda & Putra Astika, 2021). Profitability is not the only consideration for investors when making investments, in line with research that states that high and low profitability is not a reference for managers to practice income smoothing. The resulting research results are in line with research (Winanda & Putra Astika, 2021), (Inayah & Izzaty, 2021), and (Lauren & Nugroho, 2024), which states that profitability does not affect income smoothing. In Islamic commercial banks, prioritizing fairness, transparency, and profitability are not always determining factors in income smoothing. The operational characteristics of Islamic commercial banks, which are based on profit sharing and the principle of prudence, create a mechanism suitable for maintaining cash flow stability without the need for income smoothing.

4.2.2. Effect of Cash Holding on Income Smoothing

Based on the data processing results in Table 2, the cash holding variable has not been able to influence income smoothing because this test shows that cash holding has a coefficient of 5.456325 with a probability value of 0.1894 . Therefore, cash holdings have no effect on income smoothing at Islamic commercial banks in Indonesia from 2020 to 2023. This shows that the cash companies hold does not influence management to engage in income smoothing practices. Cash is only used for its intended purpose, namely to finance company operations and dividend payments. The results of this study can be explained through agency theory, which emphasizes the conflict between managers (agents) and owners (principals). Managers with high flexibility in cash management can manipulate income to achieve profit targets. However, in Islamic commercial banks supervised by a sharia supervisory board, stricter internal oversight may be possible to curb such practices, focusing on transparency and accountability in financial reporting. The availability of large amounts of cash will lead to agency problems and a desire on the part of management to engage in income smoothing practices. Managers use cash holdings to minimize external financing and company operations (Septyorini & Sofie, 2022). Managers can easily control cash holding, motivating

managers to pursue their personal interests. This can increase income smoothing practices due to the characteristics of the cash available in the company (Linda Santioso, 2020). However, in this study, there is no effect of cash holding on income smoothing, which indicates that managers do not utilize excess cash to perform opportunistic actions. Managers tend to hold cash for liquidity and not for manipulative purposes, especially in companies with good governance and strong internal controls. The results of this study are in line with research (Milasari et al., 2024) and (Mangngalla & Kartini, 2022), which states that cash holdings are not used as a tool for income smoothing, which is expected to reduce conflicts of interest between management and shareholders.

4.2.3. The Effect of Profitability and Cash Holding on Income Smoothing

Based on the research results on the F test, the LR statistic is 6.695435 with a probability value (LR statistic) of $0.035165 > 0.05$, which means that the profitability and cash holding variables simultaneously or together affect the practice of income smoothing in Islamic commercial banks 2020-2023. These results indicate that both variables are important in influencing management decisions related to income smoothing practices. Profitability as a measure of financial performance can incentivize management to engage in income smoothing to create a more stable perception in the eyes of investors. If a company's profitability increases, this indicates that the company has the capacity to generate income and will also benefit investors because the company strives to manage investment funds optimally, enabling the company to achieve the expected profits (Rafiana, 2021). Meanwhile, cash holdings provide liquidity, enabling management to manage cash flow and profits effectively. Having stable cash in a company indicates a low risk level because it is considered capable of paying its obligations. In the context of agency theory, management seeks to reduce conflicts of interest with shareholders through income smoothing practices that can increase investor confidence and company stability. The results of this study are in line with research conducted by Amalia Haniftian & Dillak (2020), Marlina & Samosir (2022), and Afninofia et al. (2023), which states that profitability and cash holdings influence income smoothing, i.e., if a company has high profitability and cash holdings, this provides an opportunity for management to adjust profits so that they appear stable in order to maintain the company's image.

4.2.4. Income Smoothing in Islamic Perspective

The practice of income smoothing from an Islamic perspective needs to be studied more deeply, both from a legal and ethical standpoint. Islam strongly emphasizes honesty (Sidq), justice ('adl), and responsibility in every financial transaction. This study shows that Islamic commercial banks in Indonesia tend to maintain the integrity of their financial reports. This can be seen from the absence of evidence indicating that management engages in income smoothing practices based on profitability or the amount of cash held. Income smoothing, which is carried out to manipulate and conceal the actual financial condition to maintain the company's image dishonestly, is contrary to these principles. It is considered a form of unlawful action. In financial statements, presenting profit data that does not reflect the actual situation is considered a form of fraud prohibited by Islamic law. In the Qur'an, the prohibition of fraud is stated explicitly, one of which is in QS. An-Nisa [4]: 29.

يَا أَيُّهَا الَّذِينَ آمَنُوا لَا تَأْكُلُوا أَمْوَالَكُم بَيْنَكُم بِالْبَاطِلِ إِلَّا أَنْ تَكُونَ تِجَارَةً عَنْ تَرَاضٍ مِّنْكُمْ وَلَا تَقْتُلُوا
أَنْفُسَكُمْ إِنَّ اللَّهَ كَانَ بِكُمْ رَحِيمًا

"O you who have believed, do not eat your neighbor's wealth by false means, except in the form of consensual trade between you. Do not kill yourselves. Indeed, Allah is Most Merciful to you" (Q.S. An-Nisa [4]:

Islamic accounting theory emphasizes the importance of honesty, accountability, fairness, and transparency. Honesty refers to all matters, including financial issues. In preparing financial statements, managers must communicate openly and honestly and not conceal relevant information. The concept of accountability in Islam includes accountability to Allah and fellow human beings. Every financial action must be carried out with moral and ethical awareness and responsibility so that all actions will be accounted for before Allah SWT. Fairness and transparency mean that users and presenters of financial reports have the right to obtain clear and transparent information about financial transactions and ensure that rights are fulfilled proportionally (A'yuni & Wahyudi, 2024). Fatwa DSN-MUI No. 87/DSN-MUI/XII/2012 permits the formation of reserves for income smoothing to maintain the stability of returns for customers, provided that it is done transparently, honestly, and with the approval of the relevant parties, namely the Sharia Supervisory Board, the management of the Islamic financial institution, and the customers. Islam permits income smoothing to safeguard the common good and prevent collective losses, provided it is not intended to manipulate or harm specific parties.

This study contributes new insights to the literature on income smoothing in Islamic commercial banks by incorporating an Islamic perspective as an analytical framework for how Islamic commercial banks balance financial performance management with ethical reporting practices. This indicates that Islamic commercial banks' financial management is functioning according to Islamic principles and that the Sharia Supervisory Board plays a role in upholding Islamic values in decision-making related to reporting (Iskandar et al., 2022). Thus, it can be concluded that income smoothing in Islamic commercial banks is relatively controlled and does not conflict with Islamic teachings as long as it continues to prioritize the principles of transparency, honesty, and responsibility. Islam prohibits fraud and encourages every business entity to internalize moral values in financial reporting activities. Therefore, income smoothing practices that remain within ethical boundaries and are accompanied by public interest considerations can be accepted within the framework of Islamic finance. The limitations of this study lie in the data used, which only covers a specific period in Islamic commercial banks, as well as the possibility of other variables influencing income smoothing practices that were not included in this study. In future research, it is hoped that the scope of data can be expanded, and different variables and methodologies can be considered to obtain more significant results. This study is expected to broaden understanding of income smoothing practices from an economic and governance perspective and an ethical and Sharia principles perspective, which have not been extensively studied previously.

V. Conclusion

Profitability has not been able to influence income smoothing, as the partial results of this test show that the probability values of each variable exceed the significance level of 0.05, namely 0.3101 for profitability and 0.1894 for cash holdings. Simultaneously, the F-test results indicate that profitability and cash holdings jointly influence income smoothing, as evidenced by a probability value of 0.035165 below the significance level of 0.05. In the Islamic perspective, this study indicates the commitment of Islamic financial institutions to maintain the principles of transparency, honesty, fairness, and responsibility in the preparation of financial statements as explained in Q.S. An-Nisa verse 29 and strengthened by DSN-MUI Fatwa No. 87/DSN-MUI/XII/2012, which allows income smoothing if done transparently and approved by related parties. This indicates that Islamic values are internalized in the financial practices of Islamic commercial banks in Indonesia. Although there is managerial authority in managing profits, there is no indication that managers smooth out income based on profitability or cash. This shows the suitability of Islamic financial practices with the value of accountability in Islam. Social responsibility requires companies to pursue profits, maintain public trust, and not harm other parties through inaccurate and misleading information.

This study has several limitations that can be used as a basis for further research, as it is based on only two independent variables: profitability and cash holdings. Future researchers are encouraged to consider other variables to obtain more accurate results. This study only uses data from Islamic commercial banks in

Indonesia from 2020 to 2023. Therefore, it is hoped that future research can use a broader scope to gain a deeper understanding. Indicators are needed to measure how much Islamic principles are internalized in corporate financial reporting practices. Given the limitations of this study, it is hoped that readers and future researchers can use this study as a reference to expand their studies.

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