



The Effect of Good Corporate Governance Implementation on Islamic Bank Financial Performance

Amrina Rosada ✉

Faculty of Economics and Business, Universitas Singaperbangsa Karawang, Karawang, Indonesia

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Abstract

This study aims to examine the effect of Good Corporate Governance on Financial Performance at Islamic Banks. The independent variable in this study is Good Corporate Governance as measured by the board of directors, the independent board of commissioners, the islamic supervisory board and the audit committee. The population in this study were 11 Islamic commercial banks listed on the Indonesia Stock Exchange. This research data was obtained from the annual report for 2015-2019. The results showed that the audit committee has an effect on financial performance as measured by return on assets, while the board of directors, independent commissioners, and islamic supervisory board has no effect on financial performance as measured by return on assets. Together the board of directors, independent commissioners, islamic supervisory board and audit committee have an effect on return on asset.

INTRODUCTION

We often hear that many companies have collapsed because the governance of a company is not good so that there are many frauds or practices of corruption, collusion and nepotism that occur, resulting in an economic crisis and a crisis of investor confidence, which results in no investor willing to buy the company's shares. that is, it can be said that the company is not implementing good corporate governance.

But this has no effect on islamic banks, because islamic banks are not burdened with the obligation to pay interest on deposits to their customers. Islamic banks only pay for the results to their customers according to the profits the bank gets from the investment it does. With this system, islamic banks do not experience a negative spread as experienced by conventional banks that use the interest system. In carrying out their investments, islamic banks give confidence that their own funds (equity), as well as other funds available for investment, generate income that is in accordance with islamic and benefits the community.

In running its business, at a minimum, islamic banks have five operational principles consisting of: pure deposit principle, profit sharing principle, sale and purchase principle and profit margin, lease principle, and fee principle. This is evidenced by one of the islamic bank in Indonesia (at that time the only bank operating under the islamic system) which was not affected by economic conditions. The weak application of Corporate Governance is the main trigger for the occurrence of various financial scandals in the company's business. Many companies went bankrupt, which is indicated as a result of not implementing the principles of good corporate governance. Besides the many practices of corruption, collusion and nepotism (Eksandy, 2018).

Nisasmara and Musdholifah (2016) explain that the signaling theory is an action taken by the management company to give guidance to investors about how management views the company's prospects. Agency theory arises because there are differences in interests between agents and principals so that each party tries to seek the maximum benefit for yourself. This crea-

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✉ Correspondence Address:

Faculty of Economics, Universitas Singaperbangsa Karawang

Jl. HS.Ronggo Waluyo, Puseurjaya, Telukjambe Timur, Karawang, Jawa Barat, 41361

E-mail: 1710631030033@student.unsika.ac.id

tes a conflict between the agent and the principal if each party acts in its own interest. In this case, managers or agents tend to convey information related to the achievement of their performance in various ways in order to maximize the wishes of the principals in dealing with creditors, owners and the government.

Signaling theory suggests how a company should provide signals to users of financial reports. Based on research conducted by Sukanto (2011), the signal theory explains that companies will be motivated to convey information due to the presence of asymmetric information between management and outsiders and management has more information about the company's perspective in the future compared to outsiders. Several methods can be used to reduce agency problems and lowering agency costs (Maftukhah, 2013). The signal given to outsiders includes company financial data which is believed to minimize uncertainty about the company's future perspectives and will have an impact on increasing the company's credibility and success. This is a way that can be done to minimize information asymmetry between agent and principal.

According to the Forum for Corporate Governance in Indonesia in Indriati (2018) Good Corporate Governance is a set of regulations governing the relationship between shareholders, company managers, creditors, government, employees as well as other internal and external stakeholders relating to their rights and obligations or with another word is a system that controls the company. The role of corporate governance as a process of managing, directing and monitoring corporate business to create shareholder value while protecting the interests of the other staff (creditors, suppliers, government and community) (Syamsudin et al., 2017).

The number of board of directors in a company that does not comply with the rules or does not under go a self-assessment process will reduce a form of monitoring of good and controlled financial performance. The number of the board of directors is the company's organ which is authorized and fully responsible for the management of the company for the interests of the company, in accordance with the aims and objectives of the company as well as representing the company, both inside and outside the court in accordance with the articles of association.

The proportion of independent boards of commissioners who are not affiliated with the directors or have no family or financial relationship in share ownership can affect their ability to act independently. Currently, the presence of an

Independent Commissioner is very much needed on the Board of Commissioners of a company. The function of the Board of Commissioners is supervision, which must be carried out properly for the benefit of the company. The main objective of having an Independent Commissioner in the Board of Commissioners is basically to balance the supervision and balance of the necessary approvals or decisions.

The council has been set by the islamic supervisory board on regulations. Institutional ownership can affect the use of company assets and as a prevention against waste by management. Lack of supervision over management activities by the board of commissioners resulted in a reduction in work that was less effective. Insufficient number of audit committees can lead to fraud in the company. External audits are carried out based on auditing standards set by the Indonesian Institute of Accountants. These standards require the auditor to plan and perform the audit in order to obtain reasonable assurance that the financial statements are free from material misstatement. In principle, the main task of the audit committee is to assist the Board of Commissioners in carrying out its supervisory function on company performance. This is mainly related to reviewing the company's internal control system, ensuring the quality of financial reports, and increasing the effectiveness of the audit function. The financial report is a product of management which is then verified by an external auditor. In this relationship pattern, it can be said that the audit committee functions as a bridge between the company and the external auditor. The duties of the audit committee are also closely related to the review of the risks faced by the company, as well as compliance with regulations.

According to Agustina and Ardiansari (2015) states that internal factors that affect capabilities companies that go public in achieving their goals in the long run to increase in value the company can be seen from its financial performance. The company's financial performance is one factors considered by investors in invest. Good management in a company or banking today is not only an obligation but has become a necessity in every operational activity. Likewise, Islamic banking financial institutions, including Islamic commercial banks and Islamic business units. Nowadays public interest in Islamic banks is quite large. In each province which is mostly Muslim, almost part of it wants Islamic banking services because they already understand the products and services offered. So that the old growth and development of Islamic banking in Indonesia

grew rapidly with the increasing number of networks and services and the increasingly diverse products of Islamic banks which led to good management. Management determines the performance of a bank in generating profits. So that the bank's operational activities do not depend on advancing on good financial management and the important role of banking organs, namely the board of directors, the board of independent commissioners, the islamic supervisory board and the audit committee.

In this study, the calculation of return on assets is used to determine the performance of Indonesian Islamic banking companies. According to Ang (1997) Return On Asset (ROA) is a comparison between Net Income After Tax (NIAT) to total assets obtained from the average total assets at the beginning of the year and the end of the year).

Hypotheses Development

Board of Directors

In order to monitor the internal control of Islamic banks, the board of directors has the responsibility establish policies, strategies and internal control procedures, implement policies and strategies that have been approved by the board of commissioners. Maintaining an organizational structure, ensuring that delegation of authority runs effectively supported by consistent application of accountability and monitoring the adequacy and effectiveness of the internal control system. Research conducted by (Veno, 2015) said that the board of directors has a significant effect on the company's financial performance.

H1: The Board of Directors has a positive effect on the performance of Islamic banking companies.

Proportion of the Independent Commissioner

The independent board of commissioners is a member of the board of commissioners who has no relationship with the company. With the increasing composition of the independent board of commissioners in a company, it is expected that the level of independence in controlling management will be more objective. According to Indriati (2018) the greater the proportion of independent commissioners, the better the supervisory function. Research conducted by Sarafina and Saifi (2017) said that the independent board of commissioners had a significant effect on financial performance.

H2: The proportion of the Independent Commissioners has a positive effect on the performance of Islamic banking companies.

Sharia Supervisory Board

The Sharia Supervisory Board is the board on duty provide advice and suggestions to the board of directors as well as supervise the activities of Islamic banks accordingly with sharia principles. The more the number of sharia supervisory boards, the more effective the supervision of sharia principles will be. So, if the number of sharia supervisory boards increases but does not exceed the maximum limit set, then the performance based on sharia principles will have an impact on customer confidence and will automatically increase level of profitability of Islamic banks. as revealed in research (Mustaghfiroh, 2016) the sharia supervisory board has a significant positive effect on financial performance (ROA).

H3: The Sharia Supervisory Board has a positive effect on the performance of Islamic banking companies.

Audit Committee

The audit committee is a committee that works professionally and independently whose task is to assist the board of commissioners in carrying out its supervisory function on financial reports and the implementation of good corporate governance. Because the task of the audit committee is to assist the board of commissioners, with the increasing number of members of the audit committee, the better the supervision will be carried out and it is hoped that it can minimize management's efforts to manipulate data related to finance and accounting procedures, so that the company's financial performance will be increasingly increased. Research conducted by Peruno (2015) states that the existence of an audit committee affects the company's financial performance.

H4: The Audit Committee has a positive effect on the performance of Islamic banking companies.

METHOD

The population in this study were 11 islamic banks listed on the Indonesia Stock Exchange. The sampling method was purposive sampling. This method is based on certain considerations or criteria. The considerations or criteria taken are as follows: An islamic bank that was consistently listed on the Indonesia Stock Exchange during the 2015-2019 period, complete financial reports are available during the 2015-2019 research period and not delisted during the 2015-2019 research period

The number of samples of islamic banks that meet the criteria is 8 companies. The variables in this study are the independent variable and the dependent variable. The independent variable is good corporate governance as measured by the board of directors, independent board of commissioners, islamic supervisory board and audit committee and the dependent variable is the financial performance of islamic banks as measured by ROA.

Data for independent variables consisting of the board of directors, independent board of commissioners, islamic supervisory board and audit committee are taken from the Indonesia Stock Exchange for the period 2015-2019. Meanwhile, data for return on assets is obtained by using the formula calculation from net income data divided by the book value of assets at the beginning of the fiscal year on the Indonesia Stock Exchange for the period 2015-2019.

The data analysis method used in this study is multiple regression analysis. Regression analysis is an analysis related to the study of the dependence of one variable, namely the dependent variable or dependent variable on one or more other variables, namely the independent variable or the independent variable with the aim of estimating and or estimating the population average value of the dependent variable from known values or fixed value of the independent variable (Asmi, 2014).

In forming a regression model or equation, several approaches can be used. This study uses the Ordinary Least Square approach. The Ordinary Least Square approach emphasizes not only estimating, but can draw conclusions on the correct value (Ghozali, 2009). The following is the equation or regression model:

$$\text{ROA} = \alpha + \beta_1 \text{ Board of Directors} + \beta_2 \text{ Independent Commissioner} + \beta_3 \text{ Islamic Supervisory Board} + \beta_4 \text{ Audit Committee}$$

Where :

ROA = Return on Asset (ROA)

α = Constant

β = regression coefficient (used to explain in the effect of an independent variable on the dependent variable)

μ = Error

RESULT AND DISCUSSION

Descriptive Analysis

Descriptive statistics are used to analyze data by looking at the description of the data,

for example the mean value, standard deviation, variance, mode and so on. The following are the results of the SPSS output on descriptive analysis:

Table 1. Descriptive Statistics

	N	Min.	Max.	Mean	Std.Dev
ROA	60	-0.05	0.09	0.05	0.03
BD	60	40.71	98.27	80.15	15.36
IC	60	0.01	0.87	0.53	0.14
ISB	60	2.00	13.00	6.40	2.84
AC	60	1.00	9.00	3.90	1.42

Based on Table 1 above, several things can be concluded as follows:

The average board of directors is 80.15, the minimum value is 40.71, the maximum value is 98.27 and the standard deviation is 15.36 with the number of observations (n) is 60. The average proportion of the independent board of commissioners is 0.53, the minimum value is 0.01 the maximum value is 0.87 and the standard deviation is 0.14 with the number of observations (n) of 60. The average number of islamic supervisory boards is 6.40, the minimum value is 2, the maximum value is 13 and the standard deviation is 2.84. The average of the audit committee is 3.90, the minimum value is 01, the maximum value is 9, and the standard deviation is 1.42 with the number of observations (n) is 60. The average ROA is 0.049, the minimum value is -0.54. a maximum of 0.09, and a standard deviation of 0.03 with the number of observations (n) of 60. Results of Multiple Linear Regression Analysis:

Table 2. Results of Multiple Linear Regression

	Unstandardized Coefficients	Std. Error	Standardized Coefficients	t	Sig.
Model	B		Beta		
(Constant)	0.11	0.03		4.12	0.00
BD	-0.00	-0.00	-0.30	-2.23	0.01
IC	-0.05	0.02	-0.27	-2.14	0.02
ISB	-0.00	0.00	-0.13	-897.00	0.19
AC	0.01	0.00	0.27	2.03	0.02

The explanation of the regression equation is as follows: A constant of 0.11 means that if the board of directors, the independent board of commissioners, the islamic supervisory board and the audit committee are absent, then the company's performance (ROA) will be 0.11, the regression coefficient (b) of the board of directors is -0.00, which means that the increase in the board of directors is 1, then the company performance (ROA) is 0.00, the coefficient value of the proportion of independent commissioners is -0.05, which means that an increase in the proportion of independent commissioners is 1, it will decrease the company's performance (ROA) by 0.05, the coefficient value of the number of islamic supervisory boards is -0.00, which means that an increase in the number of independent boards of directors is 1, it will decrease the company's performance (ROA) by 0.00 and the audit committee regression coefficient value of 0.0051 means an increase in the audit committee is 1, it will increase the company's performance (ROA) by 0.00.

Hypothesis test

Table 3. Results of the Coefficient of Determination

Model	R	Square R	Adjusted R Square	Std. Error of the Estimate
1	0.44a	0.20	0.14	0.02

a. Predictors: (Constant), LnBD, LnIC, LnISB, LnAC

b. Dependent Variable: LnROA

Table 3 above shows that the adjusted R² value is 0.137, this means that 13.7% of the dependent variable can be explained by the independent variable and 86.3% of the dependent variable can be explained by other variables outside the model.

Simultaneously Test (F Test)

F test aims to determine the effect of independent variables together on the dependent variable (Juwita & Diana, 2012).

In Table 4 below, the F test or ANOVA test shows an F value of 3.33 with a significance of 0.009, which means less than 0.05, it can be concluded that H_A is accepted. This means that not all regression coefficients are equal to zero or all independent variables simultaneously affect the dependent variable.

Table 4. F Test Results

ANOVA ^b					
Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	0.01	5	0.00	3.33	0.01a
Residual	0.03	56	0.00		
Total	0.04	60			

a. Predictors: (Constant), LnBD, LnIC, LnISB, LnAC

b. Dependent Variable: LnROA

Partially Test (t-Test)

Table 5. t test results

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	0.1050	0.026		4.120	0.001
BD	-0.0006	-0.0003	-0.303	-2.230	0.0126
IC	-0.0496	0.0232	-0.272	-2.140	0.0186
ISB	-0.0012	0.0013	-0.126	-0.897	0.1871
AC	0.0051	0.0025	0.274	2.027	0.0241

Based on table 5 the results of the above tests, the hypothesis testing can be described as follows:

Hypothesis Testing

H₁: Board of Directors has a positive effect on return on assets (ROA)

Based on Table 4, the regression coefficient value for the board of directors variable is -0.0006 with a significance of 0.0126, this means that the significance value is much smaller than 0.05 and shows that the board of directors variable no significant effect on financial performance as measured by return on asset (ROA) with a negative regression coefficient direction. Thus, the hypothesis which states that the board of directors has a positive effect on company performance (ROA) in islamic banking is rejected.

A low number of boards is detrimental to the company from a resource dependence point of view, namely that the company depends on its boards to be able to better manage its resources.

H₂: Independent Commissioner has a positive effect on return of assets (ROA)

Based on Table 4, the regression coefficient value for the independent board of commissioners variable is -0.05 with a significance of 0.02, this means that the significance value is less than 0.05 and shows that the independent board variable no significant effect on financial performance as measured by return on assets (ROA) with a negative regression coefficient direction. Thus, the hypothesis which states that the independent board of commissioners has a positive effect on company performance as measured by the return on assets (ROA) of islamic banking is rejected.

An independent commissioner is a member of the board of commissioners who is not an employee or person who deals directly with the company, and does not represent shareholders. An independent commissioner is appointed because his experience is considered useful for the company. They can oversee the board of commissioners and oversee how the company is run.

H3: Islamic Supervisory Board has a positive effect on return of assets (ROA)

Based on Table 4, the regression coefficient value for the islamic supervisory board variable is -0.00 with a significance of 0.19, this means that the significance value is greater than 0.05 and indicates that the islamic supervisory board variable no significant effect on financial performance as measured by return on assets (ROA) with a negative regression coefficient. Thus, the hypothesis which states that the islamic supervisory board has a positive effect on performance as measured by the return on assets (ROA) of islamic banking companies is rejected. In fact, the sharia supervisory board has no effect on banking performance, this is because the sharia supervisory board in a bank has multiple positions as the sharia supervisory board in other banks which results in less good or less focused performance of a sharia supervisory board in supervising a bank. So that the performance of the sharia supervisory board is considered less good and does not affect banking performance.

H4: Audit Committee has a positive effect on return of assets (ROA)

Based on Table 4, the regression coefficient value for the audit committee is 0.00 with a significance of 0.02, this means that the significance value is less than 0.05 and shows that the audit committee variable has a significant effect on financial performance as measured by return on asset (ROA) with a positive regression coefficient direction. Thus, the hypothesis which states that the audit committee has a positive effect on

performance as measured by the return on assets (ROA) of Islamic banking companies is accepted.

CONCLUSION AND RECOMMENDATION

After analyzing and testing the effect of the hypothesis testing of the implementation of good corporate governance which consists of the board of directors, the proportion of the independent board of commissioners, the Islamic supervisory board, and the audit committee on company performance in 11 islamic banking companies listed on the Indonesia Stock Exchange in 2015-2019, respectively, then the following conclusions are drawn:

Discussion that has been described, the following conclusions can be drawn: Of all the independent variables (board of directors, independent commissioners, sharia supervisory board and audit committee in good corporate governance) that are thought to have an effect on financial performance, only the audit committee variable which has a positive effect on the financial performance of Islamic banking. From the results of the t test by looking at the significance value, the variables of the board of directors, independent commissioners, supervisory board and sharia have insignificant values and do not affect the financial performance of Islamic banking with t values of 0.01, 0.02 and 0.19, respectively.

While the audit committee variable has a positive effect on the financial performance of Islamic banking with a significance value of t of 0.02. From the results of the F test, it is proven that the significance value of F is greater than the predetermined significance value, namely 0.05. This means that all independent variables in this study jointly (simultaneously) have an effect but are not significant on the financial performance of Islamic banking as the dependent variable. The result of the coefficient of determination test shows that the adjusted R-squared value in the regression model is 0.14 which shows the ability of the independent variables (board of directors, independent commissioners, sharia supervisory board and audit committee) to explain the dependent variable financial performance (ROA) is 13.7% while the rest of 86.3% explained other variables not included in this study.

Further research will be better if consider the size of the company, make deeper observations of the audit committee, as well as observations on company structure related to good corporate governance mechanisms.

For investors, the results of this study can be used as a useful consideration for investment

decision making, especially in assessing the performance of an islamic bank in Indonesia.

For islamic banking, this research can be used as one of the bases for assessing the soundness level of Islamic banking through published financial reports. So that it can be used as material for consideration for decision making.

For the author, it can be used as a study and reference material to add insight and for further research development. In future research, it is expected not only to pay attention to the size of the board of directors, independent commissioners, islamic supervisory board and audit committee but also to pay attention to other factors related to personal professionalism in their fields. It is also hoped that the relationship between corporate structures will be further explored in order to create the good corporate governance that every company wants in running its company.

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