

## The Moderating Effect of Shariah Governance on Financial and Maqasid Shariah Performance: Evidence from Islamic Banks in Indonesia

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### Abstract

The aim of this research is to assess the effect of financial performance to Maqasid Shariah performance with shariah governance as a moderating variable. Financial performance can be measured based on three criteria: firm size (FS), return on asset (ROA) and asset structure, while Maqasid Shariah performance is measured by zakat, infaq, shadaqoh and awqaf (ZISWAF) and qordhul hasan (QH). Shariah governance (SG) is measured by the proportion of independent board of commissioners' members, board size, audit committee, and shariah supervisory board. The data in this study are the secondary data from Islamic Banking Financial Report (IBFR) of 2012-2016. This research employed a quantitative approach with panel data regression using E-views 9.0 software. The method for the data analysis used factor analysis. The results show that the effects of FS and ROA on Maqasid Shariah performance are significant, and the implementation of shariah governance is generally proven to play a significant role in moderating the effect of FS and ROA on Maqasid Shariah performance. The better the implementation of SG, the stronger the predictability of Maqasid Shariah, and shariah governance has a positive effect on Maqasid Shariah.

**Keywords:** Proportion of independent board of commissioners; Board size, audit committee; Shariah Supervisory Board (SSB); Financial performance; ZISW; Qardhul hasan.



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### 1. Introduction

In the Islamic Financial Service Industry Stability Report 2016, it is stated that Indonesian Islamic banking is currently one of the contributors to the development of global Islamic banking, which was estimated to have total assets of \$ 1.9 trillion at the end of 2016, contributing 2.5% of total Islamic financial assets (IFSB, 2016).

Indonesia has gained international recognition as follows: (1) together with the UAE, Saudi Arabia, Malaysia and Bahrain, it is now considered to be in a position to offer lessons to other countries in the world for the development of Islamic finance and (2) together with Qatar, UAE, Saudi Arabia, Malaysia and Turkey (QISMUT), Indonesia is considered to be a future Shariah financial driving force (Ernst and Young, 2016).

Positive growth marked the development of Shariah banking in 2016, after a slowing of growth in the three previous years. Islamic banking assets in 2016 were recorded to have increased by Rp 412,101 billion, or a growth of 20.28%. Shariah banking contributed the most to the increase in Islamic banking assets, with Rp 356,504 billion (The Financial Services Authority, 2016b;2016a).

Islamic banks carry out their business activities based on Shariah principles, which are in accordance with the fatwa of the National Sharia Board (DSN); specifically, must be free from *riba* (interest), *maysir* (games of chance or speculation) and *gharar* (excessive uncertainty) in all their operations. Therefore, the objectives of Islamic banking must also be in accordance with the objectives of Shariah, or Islamic Law (Bank Indonesia, 2013).

Measurement of the performance of Islamic banks in accordance with the objectives of Shariah, or Islamic Shariah, is yet to be developed, so any performance measurement of such banks still uses measures which highly focus on financial aspects. Little attention has been paid to non-financial aspects (Ascarya, 2014; Triuwono, 2011).

More specifically, research integrating the value of Islamic principles with measurement of the performance of Islamic banks began to emerge in 2008, in which social aspects should be of concern to Islamic banks (Akram and Furqani, 2013; Chapra, 2008; Dusuki and Bouheraoua, 2011; Mohammed and Razak, 2008); (Dusuki, 2013). Islamic banking carries out social functions, the most visible of which are realized through the activities of collecting and distributing *zakat*, *infaq*, *sadaqah*, grants, and *waqf* (ZISW) (Auda, 2008; Chapra, 2008; Vejzagic and Smolo, 2011); (Dusuki, 2013).

This background has motivated this research to establish whether the financial performance of Islamic banks influences the performance of Maqasid Shariah, especially as seen in the activity of ZISW.

This research is important because the relationship between financial performance and Maqasid Shariah performance is expected to provide information, especially to stakeholders, on the extent financial information can be an indication of continuity of social aspects, in this case ZISW, in the performance of Maqasid Shariah (Hainš and Bockaj, 2018).

In addition to testing the influence of financial performance on the performance of Maqasid Shariah, this study also assesses the role of Shariah governance (SG) in moderating the relationship between financial performance and Islamic Maqasid. The Shariah governance structure assessed in this study is regulated by Bank Indonesia Regulation No.11/33/2009 on the implementation of GCG for Islamic commercial banks, including the proportion of independent commissioners, the number of meetings held by the board of commissioners, the size of the audit committee, the number of meetings held by the audit committee, and the size and educational background of the Shariah Supervisory Board. Therefore, this study is expected to comprehensively describe the role of SG. On the other hand, the motivation to conduct this research is also to measure the performance of Islamic banks, which integrate the value of Maqasid Shariah, so that the social aspects, in this case ZISW and *Qordhul Hasan*, become the main concerns. Essentially, Islamic banks should be more concerned with social welfare goals than their commercial goals (Dusuki, 2007).

## 2. Literature Review and Hypothesis Development

### 2.1. Shariah Governance

In Islamic banks, the aim of SG is specifically to ensure fairness to all stakeholders (Choudhury and Nurul, 2013). This is achieved through good transparency and accountability (Grassa, 2013). In the context of Islamic financial institutions, SG should include: (1) organizational arrangements in which the manager's actions are in line with the interests of stakeholders; (2) organ governance (which includes the Board of Directors, the Shariah Supervisory Board, and management) should have the purpose of meeting stakeholder interests and facilitating the process of effective monitoring, so that resource use can be efficient; and (3) obedience to the rules and principles of Islamic law (IFSB, 2016).

The SG concept for Islamic banks issued by IFSB views SG as complementary to the existing corporate governance system. In addition to having a board of directors, internal and external audits, and a compliance unit as key elements of the corporate governance system, Islamic banks must have a Shariah board (Shariah Supervisory Board: SSB), internal and external Shariah audits and a Shariah compliance unit as the main elements of the Shariah governance system. In this system, the Shariah Supervisory Board plays an important role in the process of supervising, monitoring, auditing and providing opinions on Shariah compliance to the Islamic financial institutions (Grassa, 2013; Hasan, 2001; Muliadi and Feriyanto, 2018; Yadiat *et al.*, 2017).

### 2.2. Financial Performance in Relation to Maqasid Shariah

Based on the Regulation of Bank Indonesia No. 6/10/PBI/2004 dated 12 April 2004 concerning the Rating System for Commercial Banks, and Bank Indonesia Circular No. 6/23/ DNPB dated May 31, 2004 concerning the Rating System for the Health of Commercial Banks, a number of CAMELS (Capital, Assets Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk) factors were determined (The Financial Services Authority, 2014). According to Syafii (2012), the performance measurement of Islamic banking with this method has many weaknesses. First, by making financial ratios the main determinant of the performance of a company, managers act in the short term and ignore the long term. Second, ignoring non-financial and asset measurement aspects will give a wrong view to company managers in the present and even in the future. Finally, financial performance is only based on past performance, so it cannot help a company to achieve plans in the following period. Thus CAMELS is an instrument that is not in accordance with the values that underlie Islamic banks (Kamran and Zhao, 2016; Triyuwono, 2011).

Bedoui H. E. and Mansour (2015) also state that the Islamic view of performance is closely related to ethics; it is not limited to the financial dimension, but also includes additional dimensions that mean the company is not oriented to the owner, but to all stakeholders and society as a whole, which is an important issue in performance based on the concept of Islamic Maqasid. Triyuwono (2016) also adds that in running a business, the goal is not only to make a profit, but also concerns the planet and society in order to maintain the sustainability of the environment and the community itself. In this context, research integrating the values of Islamic law to measure the performance of Islamic banking began to emerge. Dusuki (2007) conducted a survey to establish the views of stakeholders on the objectives of Islamic banks in countries that adhere to the dual-banking system (with Malaysia as a case study). The study concluded that stakeholders in Islamic banks believe that the banks are more concerned with their social welfare goals than with their commercial goals. Chapra (2008) put the aim of Maqasid Shariah could be used to measure the achievement of the objectives of the Maqasid. This study was later referred to by Bedoui M. H. (2012) and further developed by Akram and Furqani (2013), Syafii (2012), Triyuwono (2016) and (Ascarya d. R. H., 2017). This explanation motivated the development of hypothesis 1 as follows:

**H<sub>1</sub>:** Current financial performance has a positive relationship with the achievement of Masaqid Shariah.  
Shariah Governance as a Relationship Moderator between Financial Performance and Masaqid Shariah

In general, the factors relating to governance in this study consist of the Board of Commissioners, the Audit Committee and the Shariah Supervisory Board, which refer to the Regulation of Bank Indonesia No. 11/33/PBI/2009 ([Bank Indonesia, 2009](#)).

### **2.3. Regulations on the Board of Commissioners (BOC) in Islamic Banks**

The Board of Commissioners (BoC) is the organ of the company in charge of carrying out general and/or special supervision in accordance with the articles of association and of advising the directors. The BOC is required to carry out its duties and responsibilities: (i) in accordance with the principles of GCG; (ii) by supervising the implementation of GCG in every Islamic Banks activity; (iii) by carrying out supervision of the implementation of the duties and responsibilities of the Board of Directors, and providing advice to them; (iv) by monitoring and evaluating the implementation of the strategic policy of Islamic Banks; (v) by being prohibited from being involved in making decisions on Islamic Banks operational activities, except for making decisions on granting financing to the Board of Directors; (vi) by ensuring that the Board of Directors has followed up on audit findings and/or recommendations from the results of BI supervision, independent auditors, SSB and/or external auditors; (vii) by having binding work guidelines and rules; and (viii) by providing sufficient time to carry out their duties and responsibilities optimally ([Boonvut and Saratchanut, 2017](#)).

### **2.4. Shariah Regulation on Audit Committees (ACs) in Islamic Banks**

Members of an audit committee (AC) consist of: (i) an independent commissioner; (ii) an independent party who has expertise in financial accounting; and (iii) an independent party who has expertise in Islamic banking. The committee has duties and responsibilities for: (i) evaluating the implementation of internal audits in order to assess the adequacy of internal controls, including the adequacy of the financial reporting process; (ii) coordinating with the Public Accountant Office in the framework of effective implementation of external audits; (iii) evaluating the implementation of tasks carried out by the internal audit function; (iv) evaluating the implementation of any follow-ups by the Board of Directors on audit findings and/or recommendations from the results of supervision by Bank Indonesia, internal auditors, the Shariah Supervisory Board, and/or external auditors, to provide recommendations to the Board of Commissioners; and (v) providing recommendations regarding the appointment of a public accountant and Public Accountant Office to the Board of Commissioners.

### **2.5. Regulation of Shariah Supervisory Boards (SSBs) in Islamic Banks**

Proposals for the appointment and/or replacement of members of the Shariah Supervisory Board (SSB) to the Annual General Meeting of Shareholder are made by taking into account the recommendations of the Remuneration and Nomination Committee. The term of office of the DPS members is the same as that of the members of the Board of Directors or BOC. The BOC has duties and responsibilities for: (i) carrying out their tasks in accordance with the principles of GCG; (ii) providing advice and recommendations to the Board of Directors and monitoring the activities of the bank to comply with Shariah principles; (iii) assessing and ensuring compliance with Shariah principles on operational guidelines and products issued by the bank; (iv) monitoring any new bank product development process so that it complies with the DSN-MUI fatwa; (v) requesting a fatwa from DSN-MUI for any new bank product that has no fatwa; (vi) conducting periodic reviews on the fulfillment of Shariah principles to the mechanism of raising funds and channeling bank services; and (vii) requesting data and information related to Shariah aspects of the bank's work unit in the framework of carrying out its duties ([Wasike, 2017](#)).

According to [Laela \(2012\)](#), SG, which consists of the various elements mentioned above, plays a role in the contract and monitoring mechanism, so directors tend to be more in line with the interests of shareholders; this is usually followed by better organizational performance. The extent to which this SG mechanism is effective will have an impact on Shariah banking performance. [Ghayad \(2008\)](#), [Mollah and Zaman \(2015\)](#), [Farag et al. \(2018\)](#) concludes that the level of SG implementation is positively related to the performance of Islamic banking, both financially and non-financially. [Bhagat \(2009\)](#) and [Ghaffar \(2014\)](#) prove that there is a significant relationship between Islamic governance practices and the performance of Islamic banking. Based on this discussion, the second hypothesis proposed is:

**H2:** Better implementation of SG will strengthen the influence of financial performance on Maqasid Shariah

### **2.6. Shariah Governance in Relation to Shariah Maqasid Performance**

Shariah Governance (SG) is a concept which emerged in the nineteenth century after the birth of Islamic banking and the Islamic finance, according to ([Muneeza and Hassan, 2014](#)). Shariah governance, according to [Grassa \(2013\)](#), is a unique characteristic of corporate governance in the financial architecture and is related to religious aspects, Islamic activities and their implementation in Islamic Financial Institutions (IFIs). [Chapra \(2008\)](#) and [Ahmed, Sabirzyanov and Rosman, \(2014\)](#) further define corporate governance as a series of relationships between company management, the Board of Directors, shareholders and other stakeholders. Thus, SG creates a better management control process, which usually has a positive impact on the performance of Islamic banking ([Alahoul et al., 2016](#)).

In its CG structure, Islamic banks have two boards, the Board of Directors, as in conventional banks, and the Shariah Supervisory Board (SSB). The task of the second board is to ensure that bank operations and contracts are in accordance with Islamic law (Shariah compliance) (PBI No 11/33 / PBI / 2009) ([Bank Indonesia, 2009](#)). The existence of this dual boards will theoretically improve the process of monitoring the actions of managers, so that the

implementation of SG in Islamic banks can play a stronger role in improving the quality of the performance of Maqasid Shariah. Thus, the third hypothesis is formulated as follows:

**H3:** Better implementation of SG has a positive impact on the achievement of the performance of Maqasid Shariah.

### 3. Research Method

#### 3.1. Sample and Data Selection

This study used a population of 12 Islamic banks from fiscal years 2012-2016. All the data were obtained from the directory of Bank Indonesia financial reports and SG implementation reports, obtained directly from each bank.

The preliminary data consisted of a 5-year financial statement book consisting of five financial reports from each of the 12 Islamic banks. These banks comprised all the Islamic banks in Indonesia until 2016 (the total up to November 2016 was 13 banks; however, because the new bank began its operation in January 2016, no data were used until the 3rd quarter and were made proportional to its total assets).

Three types of data were required in the study, namely: (1) financial performance (firm size, return on assets and asset structure); (2) Maqasid Shariah performance (ZISW and *Qordhul Hasan*), and (3) Shariah governance (proportion of independent commissioners; number of meetings of the Board of Commissioners; size and number of meetings of the Audit Committee; and size, educational background, and number of meetings of the Shariah Supervisory Board). Some parts of the third type of data were taken from annual reports, while the others were presented separately in the SG implementation report.

#### 3.2. Data Analysis Method

The data analysis was conducted in several stages. The first stage involved factor analysis to reduce the invalid indicators measuring each of the latent variables. The second stage was carried out after obtaining the loading value that met the validity requirements, and the factor analysis produced a score factor for each latent variable. The factor score results for the FP, SG and Performance (MSP) variables were further analyzed by panel data regression. The panel regression model is as follows:

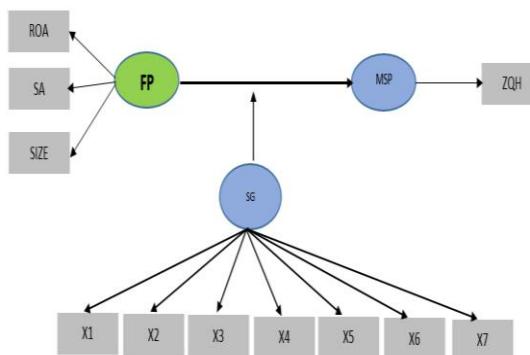
$$MSP_{it} = b_0 + b_1 FP_{it} + b_2 SG_{it} + b_3 FP_{it} * SG_{it} + e_{it} \quad (1)$$

### 4. Results and Discussion

#### 4.1. Stages of the Analysis

The first stage used factor analysis to reduce the indicators on the Z variable (Maqasid Shariah performance) and the Shariah Governance variable. After obtaining the loading value that met the requirements, the next step was to calculate the Z score with the Shariah governance score to be processed by panel regression.

**Figure-1.** Types of panel data: 12 Islamic commercial banks in the period 2012-2016.



**Stage 1.** Results of Analysis of the Shariah Governance (SG) Variable

**Figure-2.** Results of Stage 1 factor analysis for the Shariah Governance variable

| KMO and Bartlett's Test                          |                    |        |
|--|--------------------|--------|
| Kaiser-Meyer-Olkin Measure of Sampling Adequacy. |                    | ,517   |
| Bartlett's Test of Sphericity                    | Approx. Chi-Square | 73,359 |
|  | df                 | 21     |
|  | Sig.               | ,000   |

| Communalities |         |            |
|---------------|---------|------------|
|               | Initial | Extraction |
| X1            | 1.000   | ,789       |
| X2            | 1.000   | ,790       |
| X3            | 1.000   | ,800       |
| X4            | 1.000   | ,847       |
| X5            | 1.000   | ,812       |
| X6            | 1.000   | ,831       |
| X7            | 1.000   | ,833       |

Extraction Method: Principal Component Analysis.

#### Total Variance Explained

| Component | Initial Eigenvalues |               |              | Extraction Sums of Squared Loadings |               |              | Rotation Sums of Squared Loadings |               |              |
|-----------|---------------------|---------------|--------------|-------------------------------------|---------------|--------------|-----------------------------------|---------------|--------------|
|           | Total               | % of Variance | Cumulative % | Total                               | % of Variance | Cumulative % | Total                             | % of Variance | Cumulative % |
| 1         | 2,082               | 29,748        | 29,748       | 2,082                               | 29,748        | 29,748       | 1,781                             | 25,438        | 25,438       |
| 2         | 1,409               | 20,125        | 49,871       | 1,409                               | 20,125        | 49,871       | 1,393                             | 19,904        | 45,342       |
| 3         | 1,161               | 16,580        | 66,451       | 1,161                               | 16,580        | 66,451       | 1,344                             | 19,196        | 84,538       |
| 4         | 1,050               | 15,002        | 81,453       | 1,050                               | 15,002        | 81,453       | 1,184                             | 16,915        | 81,453       |
| 5         | ,548                | 7,803         | 89,256       |                                     |               |              |                                   |               |              |
| 6         | ,437                | 6,248         | 95,505       |                                     |               |              |                                   |               |              |
| 7         | ,315                | 4,495         | 100,000      |                                     |               |              |                                   |               |              |

Extraction Method: Principal Component Analysis.

#### Rotated Component Matrix\*

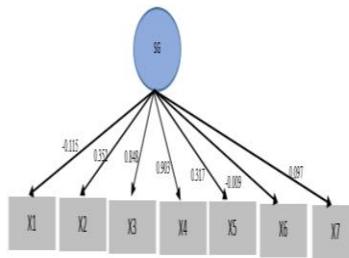
|    | Component |       |       |       |
|----|-----------|-------|-------|-------|
|    | 1         | 2     | 3     | 4     |
| X1 | -.115     | -,006 | -,881 | -,003 |
| X2 | ,352      | -,030 | ,378  | -,722 |
| X3 | ,848      | -,063 | ,276  | -,024 |
| X4 | ,903      | ,152  | -,075 | ,064  |
| X5 | ,317      | -,083 | ,267  | ,796  |
| X6 | -,009     | ,805  | ,419  | ,083  |
| X7 | ,097      | ,842  | -,311 | -,130 |

Extraction Method: Principal Component Analysis.

Rotation Method: Varimax with Kaiser Normalization.

a. Rotation converged in 6 iterations.





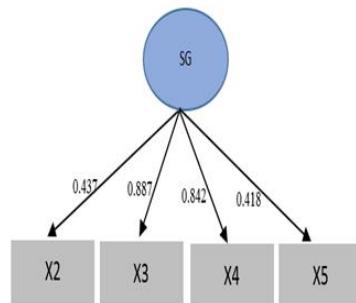
The results of the stage 1 factor analysis show that three indicators had to be dropped because they had a loading value of less than 0.3 and so that the results of stage 2, after the three indicators had been removed, were able to produce loading values of > 0.3.

**Figure-3.** Results of Stage 2 factor analysis for the Shariah Governance variable

| Communalities |         |            | KMO and Bartlett's Test                          |  |                    |        |  |
|---------------|---------|------------|--|--|--------------------|--------|--|
|               | Initial | Extraction | Kaiser-Meyer-Olkin Measure of Sampling Adequacy. |  |                    |        |  |
| X2            | 1,000   | .770       |  |  |                    | ,554   |  |
| X3            | 1,000   | .791       | Bartlett's Test of Sphericity                    |  | Approx. Chi-Square | 42,246 |  |
| X4            | 1,000   | .713       |  |  | df                 | 8      |  |
| X5            | 1,000   | .763       |  |  | Sig.               | ,000   |  |

| Component | Total Variance Explained |               |              |                                     |               |              |                                   |               |              |
|-----------|--------------------------|---------------|--------------|-------------------------------------|---------------|--------------|-----------------------------------|---------------|--------------|
|           | Initial Eigenvalues      |               |              | Extraction Sums of Squared Loadings |               |              | Rotation Sums of Squared Loadings |               |              |
|           | Total                    | % of Variance | Cumulative % | Total                               | % of Variance | Cumulative % | Total                             | % of Variance | Cumulative % |
| 1         | 1,863                    | 46,575        | 46,575       | 1,863                               | 46,575        | 46,575       | 1,863                             | 46,572        | 46,572       |
| 2         | 1,173                    | 29,331        | 75,907       | 1,173                               | 29,331        | 75,907       | 1,173                             | 29,334        | 75,907       |
| 3         | ,803                     | 15,072        | 90,979       |                                     |               |              |                                   |               |              |
| 4         | ,361                     | 9,021         | 100,000      |                                     |               |              |                                   |               |              |

|    | Rotated Component Matrix <sup>a</sup> |       |
|----|---------------------------------------|-------|
|    | Component                             |       |
|    | 1                                     | 2     |
| X2 | ,437                                  | -,781 |
| X3 | ,887                                  | -,054 |
| X4 | ,842                                  | ,060  |
| X5 | ,418                                  | ,787  |



The results of the stage 2 factor analysis showed that there were four indicators: the number of meetings of the Board of Commissioners, the size of the Audit Committee, the number of meetings of the Audit Committee, and the size of the Shariah Supervisory Board. After the number of these indicators had been reduced, a loading value of > 0.3 for the Shariah governance score could be obtained.

#### Stage-2. Results of Analysis of the Financial Performance (FP) Variable Factor

**Figure-4.** Results of Stage 1 factor analysis for the Financial Performance variable

**KMO and Bartlett's Test**

|  |       |
|--|-------|
| Kaiser-Meyer-Olkin Measure of Sampling Adequacy. | ,481  |
| Bartlett's Test of Sphericity                    | 3,197 |
| df   | 3     |
| Sig.   | ,362  |

**Communalities**

|    | Initial | Extraction |
|----|---------|------------|
| Y1 | 1,000   | ,840       |
| Y2 | 1,000   | ,929       |
| Y3 | 1,000   | ,670       |

Extraction Method: Principal Component Analysis.

□

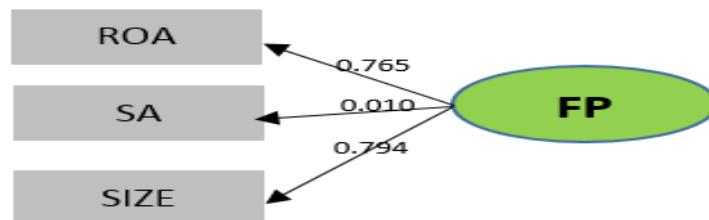
**Total Variance Explained**

| Component | Initial Eigenvalues |               |              | Extraction Sums of Squared Loadings |               |              | Rotation Sums of Squared Loadings |               |              |
|-----------|---------------------|---------------|--------------|-------------------------------------|---------------|--------------|-----------------------------------|---------------|--------------|
|           | Total               | % of Variance | Cumulative % | Total                               | % of Variance | Cumulative % | Total                             | % of Variance | Cumulative % |
| 1         | 1,220               | 40,681        | 40,681       | 1,220                               | 40,681        | 40,681       | 1,215                             | 40,512        | 40,512       |
| 2         | 1,020               | 33,993        | 74,674       | 1,020                               | 33,993        | 74,674       | 1,025                             | 34,162        | 74,674       |
| 3         | ,760                | 25,326        | 100,000      |                                     |               |              |                                   |               |              |

Extraction Method: Principal Component Analysis.

**Rotated Component Matrix<sup>a</sup>**

|    | Component |       |
|----|-----------|-------|
|    | 1         | 2     |
| Y1 | ,765      | ,236  |
| Y2 | ,010      | ,964  |
| Y3 | ,794      | -,200 |



Based on the results of stage 1 factor analysis, the indicator that was dropped was X2 (Asset Structure) because it had a loading value of less than 0.3.

**Figure-5.** Results of stage 2 factor analysis for the Financial Performance variable  
**KMO and Bartlett's Test**

|  |                    |
|--|--------------------|
| Kaiser-Meyer-Olkin Measure of Sampling Adequacy. | ,500               |
| Bartlett's Test of Sphericity                    | Approx. Chi-Square |
|  | df                 |
|  | Sig.               |

**Communalities**

|    | Initial | Extraction |
|----|---------|------------|
| Y1 | 1,000   | ,698       |
| Y3 | 1,000   | ,608       |

Extraction Method: Principal Component

Analysis.

**Total Variance Explained**

| Component | Initial Eigenvalues |               |              | Extraction Sums of Squared Loadings |               |              |
|-----------|---------------------|---------------|--------------|-------------------------------------|---------------|--------------|
|           | Total               | % of Variance | Cumulative % | Total                               | % of Variance | Cumulative % |
| 1         | 1,216               | 60,789        | 60,789       | 1,216                               | 60,789        | 60,789       |
| 2         | ,784                | 39,211        | 100,000      |                                     |               |              |

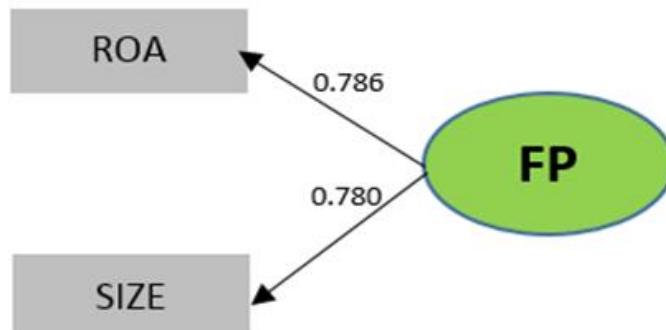
Extraction Method: Principal Component Analysis.

**Component Matrix\***

|    | Component |      |
|----|-----------|------|
|    | 1         |      |
| Y1 |           | ,786 |
| Y3 |           | ,780 |

Extraction Method: Principal Component Analysis.

a. 1 components extracted.



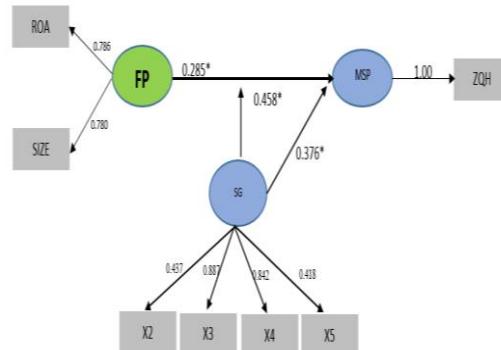
The results of the stage 2 factor analysis indicate that there are two indicators: Return on Assets and Firm Size. After these indicators had been reduced, a loading value of > 0.3 for the Financial Performance (FP) score could be obtained.

### Stage 3. Results of the Regression Panel Analysis with the Moderation Variable

**Figure-6.** Results of panel regression with moderation variables

Dependent Variable: Z2  
Method: Panel Least Squares

| Variable           | Coefficient | Std. Error            | t-Statistic | Prob.              |
|--------------------|-------------|-----------------------|-------------|--------------------|
| FP                 | 0.285171    | 0.080370              | 3.548216    | 0.0010 Significant |
| SG                 | 0.375890    | 0.110729              | 3.394693    | 0.0015 Significant |
| FP*SG              | 0.458114    | 0.085020              | 5.388278    | 0.0000 Significant |
| C                  | -0.012316   | 0.054864              | -0.224491   | 0.8234             |
| R-squared          | 0.228660    | Mean dependent var    | 0.032458    |                    |
| Adjusted R-squared | 0.156907    | S.D. dependent var    | 1.117794    |                    |
| S.E. of regression | 1.026359    | Akaike info criterion | 2.988245    |                    |
| Sum squared resid  | 45.29677    | Schwarz criterion     | 3.183162    |                    |
| Log likelihood     | -66.71788   | Hannan-Quinn criter.  | 3.061904    |                    |
| F-statistic        | 3.186782    | Durbin-Watson stat    | 2.806499    |                    |
| Prob(F-statistic)  | 0.022276    |                       |             |                    |



The direct influence of financial performance (FP) on Maqasid Shariah performance (MSP) is significant, i.e. 0.285, and the influence of FP on MSP is significant if it interacts with Shariah Governance (SG) by 0.458, indicating that SG is able to moderate the influence of FP on MSP. The value of loading of the ROA factor is 0.786 times greater than the SIZE loading value of 0.780, indicating that the level of influence on FP is stronger in ROA than in SIZE. Meanwhile, the highest loading values that reflect SG are X3 (number of Audit Committee members) at 0.887 and X4 (number of meetings of the Audit Committee annually at 0.842. The loading value of X2 is the number of annual meetings of the Board of Commissioners of 0.437 and the amount of loading X5 (number of SSB) of 0.418. SG's direct influence on Maqasid Shariah performance (MSP) is significant, with a coefficient value of 0.376.

This study reviews the impact of the implementation of Shariah Governance (SG) on Islamic banks, which strengthens the relationship between Financial Performance (FP) and Maqasid Shariah Performance (MSP). It is proven to have an influence on monitoring operations, thereby improving the quality of the implementation of Islamic ethical values in Islamic banks in the form of the implementation and management of *Zakat*, *Infaq*, *Shodaqoh*, and *Waqf* (ZISW), as well as the *Qordhul Hasan*. The study is expected to have special implications for Islamic banks, at least in creating individual and cultural control mechanisms that influence managerial behavior to be more compliant with Shariah (Shariah compliance), thereby reducing their opportunistic behavior. This finding supports the results of previous studies (Ghaffar, 2014; Ghayad, 2008; Yadiat *et al.*, 2017).

## 4. Conclusion

Based on the results of the tests carried out in the study, it can be concluded that current financial performance has a direct influence on the performance of Islamic Maqasid. However, better implementation of Shariah Governance will improve financial performance capability in the performance of Shariah Maqasid. This is in accordance with the hypotheses proposed. Although the role of the Shariah Supervisory Board (SSB) is still minor, it has been proven to have a controlling influence. The results of the study have various implications. First, for regulators, although the implementation of SG has been proven to strengthen financial performance toward Maqasid Shariah, the process needs to be evaluated and monitored more closely so that Shariah governance has fully implemented ethical values and Shariah principles. Second, another implication of the research relates to the Shariah Supervisory Board (SSB) in Indonesia developing the performance of the Shariah Maqasid in the practice of *Zakat*,

*Infaq, Shadaqoh, and Waqf*, as well as the *Qordhul Hasan* in the Islamic banks that they supervise, as a concrete manifestation of the banks continuously improving their financial performance based on Shariah principles.

This research has a number of limitations. It only focuses on the impact of SG from financial performance on the Maqasid Shariah Performance as seen by the indicators of ZISW and *Qordhul Hasan*. Future research could be developed with other Maqasid Shariah Performance indicators. This would be interesting, since a number of studies that integrate the values of Islamic Maqasid have begun to emerge. Moreover, the purpose of Shariah banking is to support the implementation of national development in order to improve justice, togetherness and equal distribution of people's welfare; however, it needs to be tested whether these objectives have played a role in minimizing the opportunistic behavior of managers.

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