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# THE IMPLEMENTATION OF CORPORATE GOVERNANCE IN ISLAMIC BANKING IN INDONESIA BASED ON AAOIFI STANDARD

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**Abstract:** This study aims to analyze the implementation of Corporate Governance in Islamic banking in Indonesia and the implementation of Corporate Governance in Islamic banking in Indonesia according to the standards of Corporate Governance by AAOIFI. This study used secondary data obtained from the annual report of Good Corporate Governance of Sharia Commercial Bank which has been published in 2016. The method used in this study is qualitative with the type of research is content analysis from the annual Good Corporate Governance report of Islamic bank in Indonesia. The results of this study indicate that the implementation of Corporate Governance at Sharia Commercial Banks in general have done good corporate governance which is marked with the result of self-assessment of every Sharia Commercial Bank which on average gets a good predicate. The results of research on the implementation of AAOIFI standards of Corporate Governance in general have applied some of the AAOIFI standards, but there is one standard AAOIFI that has not been applied by Sharia Commercial Banks other than Bank Muamalat. The standard that has not been applied is Internal Sharia Reviews which should be established in the policy. Thus it can assist the Sharia Supervisory Board and become the Liaison Officer between the Bank and the Sharia Supervisory Board in supervising the aspects of sharia regularly and helping to prepare the supervisory report of the Sharia Supervisory Board every semester which must be submitted to the Financial Services Authority (OJK). For further research, it is expected to re-analyze the implementation of Corporate Governance based on AAOIFI standard by using GCG report in several periods and to examine other components of the annual report and not only use AAOIFI governance standards.

**Keywords:** Islamic Banking, Corporate Governance, AAOIFI

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## 1. Introduction

That the growth and development of Islamic banking are so rapidly lately marked by the increasing number of Islamic banking services network and the increasing diverse products leading to the implementation of Good Corporate Governance (GCG) in Islamic banking is becoming increasingly important (Peraturan Bank Indonesia, 2009; Hastuti, 2015). Good Corporate Governance (GCG) that serves to anticipate various risks, both financial risk and reputation, is also an important pillar that must be applied to create a Islamic bank that is superior and resilient. The Implementation of GCG in Islamic banks is important because Islamic banks are banks that use the principle of profit sharing (profit shared by the bank and customers) (Chapra & Ahmed, 2002).

The implementation of Good Corporate Governance in Islamic banking in order to make Islamic bank become more shar'i because its application in Islamic banking industry must fulfill sharia principles. Islamic banking operations must be strictly enforced based on sharia principles. On the other hand, the direction of development and regulation of

Islamic banking is to ensure compliance with sharia principles in its operations by implementing fatwas issued by Dewan Syariah Nasional (DSN) & Majelis Ulama Indonesia (MUI)<sup>1</sup>. The international standards specifically are established to realize Islamic Financial Institutions (IFI) which is totally fair, professional, and in accordance with sharia standard / principle. The majority of international Islamic banking adopts this standard and uses it as reference of compliance of Islamic bank to sharia standard / principle issued by AAOIFI institution.

AAOIFI is one of the prominent International standard-setting organizations for Islamic institutions. The AAOIFI sets compliance standards for institution that wish to gain access to the Islamic financial market and ensures that its participants also comply with the regulations set out within the domain of Islamic finance (hartomy, 2018). The objectives of the AAOIFI are as follows<sup>2</sup>:

1. To develop accounting and auditing thoughts relevant to Islamic financial institutions.
2. To disseminate accounting and auditing ideas relevant to Islamic financial institutions and its application through training, seminars, publication of periodical, the carrying out and commissioning of research and other means.
3. To prepare, promulgate and interpret accounting and auditing standards for Islamic financial institutions.
4. To review and amend accounting and auditing standards for Islamic financial institutions.

Hussainey stated that the compliance rate of Islamic Banks based on AAOIFI standards assessed in terms of Sharia Supervisory Board (SSB) is about 68%, while the compliance rate for CSR is 27%, and compliance rate for financial accountability is 73%. The aggregate disclosure based on the three indices is 56%. The analysis also shows that bank size, the existence of Sharia Auditing Department (SAD), the age of banks and Corporate Governance are the main determinants of compliance level<sup>3</sup>.

The purpose of this study is to assess and understand the implementation of Corporate Governance in Islamic banking in Indonesia according to the standards of Corporate Governance by AAOIFI.

## **B. Literature Review**

### **1. Islamic Banking**

#### *1.1. Definition of Islamic Banks*

Islamic Banks is a part of Islamic Banking in Indonesia. The definition of Islamic banking is contained in Law No. 21 of 2008 Article 1 point 1 which states<sup>4</sup>,

"Islamic banking is everything that concerns about Islamic bank and Islamic Business Unit, includes institutional, business activity, as well as the manner and process in carrying out its business activities."

In addition, the definition of Islamic Bank is specifically contained in Law No. 21 Article 1 point 7 which states<sup>5</sup>,

"Islamic Bank is a bank that runs its business activities based on Sharia Principles and according to its kind consisting of Sharia Commercial Bank and Rural Islamic Bank."

Meanwhile, Sharia Principles which become the operational basis of Islamic Bank are described in Law No. 21 of 2008 Article 1 point 12 which states<sup>6</sup>,

"Sharia principle is the principle of Islamic law in banking activities based on fatwas issued by institutions that have authority in the establishment of fatwa in the field of Sharia."

#### 1.2. *Types of Islamic Bank in terms of its Function*

##### a. Sharia Commercial Bank

The definition of Sharia Commercial Bank is contained in Law No. 21 of 2008 Article 1 point 8 which states<sup>7</sup>,

"Sharia Commercial Bank is an Islamic Bank which in its activities provides services in the payment traffic."

##### b. Islamic Business Unit

The definition of Islamic Business Unit is contained in Law No. 21 of 2008 Article 1 point 10 which states<sup>8</sup>,

"Islamic Business Unit, hereinafter referred to as UUS, is a work unit of the head office of a Conventional Commercial Bank functioning as the holding office of an office or unit conducting business based on Sharia Principles, or a work unit in a branch office of a Bank domiciled in a foreign country to carry out conventional business activities that function as the head office of the Sharia sub-branch office and / or sharia unit."

##### c. Rural Islamic Bank

The definition of Rural Islamic Bank is contained in Law No. 21 of 2008 Article 1 point 9 which states<sup>9</sup>,

"Rural Islamic Bank is an Islamic Bank which in its activities does not provide services in the payment traffic."

### 2.1 *Definition of Good Corporate Governance*

The term "Corporate Governance" was first introduced by the Cadbury Committee in 1992 in a report known as Cadbury Report. This report also marks a decisive turning point for Corporate Governance practices worldwide. In Cadbury Report, Corporate Governance is a system that serves to direct and control the organization. The Cadbury Report defines corporate governance as<sup>10</sup>:

"GCG is a principle that directs and controls the company to achieve a balance between the strength and authority of the company in providing accountability to its shareholders in particular, and stakeholders in general."

According to the World Bank, GCG is a rule, standards and organizations in the economic field which is governing the behavior of company owners, directors, and managers as well as details and elaboration of duties and authorities and accountability to investors (shareholders and creditors). The goal is to create a system of control and balance to prevent possible misuse of corporate resources and keep the company growing (Wibowo, Setyono, & Abadi, 2013)

## 2.2 *The Principle of Good Corporate Governance*

A description of the principles of Corporate Governance is set forth in the Peraturan Otoritas Jasa Keuangan Number 30 / POJK.05 / 2014 Chapter 2 Article 2, paragraph 2, namely<sup>11</sup>:

- a. Transparency, that is disclosure in the process of decision making and disclosure in the disclosure and provision of relevant information about the Company, which is easily accessible to stakeholders in accordance with the laws and regulations in the field of financing as well as the standards, principles and the practice of conducting healthy financing business;
- b. Accountability, that is the clarity of functions and implementation of corporate organs so that the company's performance can be transparent, reasonable, effective and efficient;
- c. Responsibility, that is the conformity of the Company's management with the laws and regulations in the field of financing and ethical values and standards, principles and practices of the implementation of a healthy financing business;
- d. Independency, that is the state of the Company which is managed independently and professionally and is free from Conflict of Interest and the influence or pressure of any party that is not in accordance with the laws and regulations in the field of financing and ethical values and standards, principles and practice healthy financing business; and
- e. Equity and fairness that is equality, balance and fairness in fulfilling the rights of stakeholders arising under agreements, rules and regulations, and ethical values and standards, principles and the practice of healthy financing operations.

## 2.3 *The Purpose of Good Corporate Governance*

According to Komite Nasional Kebijakan Governance (KNKG), Good Corporate Governance has six main objectives. The six main objectives are as follows<sup>12</sup>:

- a. Encouraging the achievement of corporate sustainability through management based on the principle of transparency, accountability, responsibility and fairness and equity.
- b. Encouraging the empowerment of functions and independence of each company's organs i.e. dean commissioners, directors and general meeting of shareholders (GMS).
- c. Encouraging shareholders, members of the board of commissioners and members of the board of directors to make decisions and carry out their actions based on high moral values and compliance with laws and regulations ( Hastuti & Anggara, 2017).
- d. Encouraging the emergence of awareness and corporate social responsibility to society and environmental sustainability, especially around the company.
- e. Optimize corporate value for shareholders by watching other stakeholders.

f. Enhancing the competitiveness of companies both nationally and internationally so as to increase market confidence that can encourage investment flows and the growth of national and sustainable economic.

### **3. Governance Standard by Accounting and Auditing Organization for Islamic Financial Institutions**

#### *3.1 Shari'ah Supervisory Board: Appointment, Composition and Report*

This standard was adopted in the AAOIFI meeting held on 15-16 June 1997 but it was effective commencing from 1 January 1999. The salient points are as follows:

Shari'ah Supervisory Board (SSB) refers to an independent body of specialised and competent jurists in Islamic commercial jurisprudence (fiqh al-mu'amalat). It may also be comprised of experts in Islamic financial institutions but with sufficient knowledge of fiqh al-mu'amalat.

The appointment of Sharia Supervisory Board (SSB) must be made by shareholders of Islamic financial institutions upon the recommendation of its board of directors.

There are several elements contained in the SSB's report, inter alia, the title report should be clear and the purpose of the engagement must be explicitly identified. The report should state that the management has performed its duty and properly complied with Shari'ah principles. To this end, the report must be published in the annual report.

#### *3.2 Shari'ah Review*

This standard was adopted in the AAOIFI meeting held on 21-22 June 1998 but it was effective commencing on 1 January 1999. The salient features of this standard are as follows:

Shari'ah review refers to an examination of financial activity which must be compliant with Shari'ah principles. This must be done on all policies, agreements, transactions and the like. In addition, the SSB should have full access to all information and records

Shari'ah review is done under the purview of the SSB. However, it does not waive management of the responsibility to provide all information to the SSB in relation to the Islamic financial Institutions activities and services which must be compliant with Shari'ah principles. In this regard, both SSB and management play a pivotal role in ensuring Shari'ah compliance

The core of this guideline is the procedures set out pertaining to Shari'ah review consisting of three stages. All paperwork done in each stage must be properly documented. Firstly, planning review procedures must be sufficiently developed to understand the Islamic Financial Institutions operation as a whole including product and management. Secondly, the executing review procedures which include reviewing of contracts and discussing findings with the Islamic Financial Institutions management. Lastly, conclusions must be properly documented and reported to shareholders at the annual general meeting.

#### *3.3 Internal Shari'ah Review*

This standard was adopted in the AAOIFI meeting held on 13-14 June 1999 but it was effective commencing on 1 January 2000. It should be noted that internal shari'ah review

is the extension of the general notion of Shari'ah review (hartomi). This guideline is designed to complement the previous guideline. Governance Standard No.2 The salient features of this guideline are as follows:

The organizational status of the internal Shari'ah review must not be lower than the internal audit or internal control department. Management and the board of directors must support internal Shari'ah reviewers and the head of the internal Shari'ah review must be responsible to the board of directors. In addition, Shari'ah reviewers are also expected to communicate with the SSB and external auditors. As a whole, the performance of the internal Shari'ah reviewers must be independent.

Shari'ah reviewer must be competent and possess appropriate educational background, i.e proficient in Islamic commercial jurisprudence (fiqh al-muamalat). They are expected to exercise due professional care. The Shari'ah review must be consistently supervised and the evidence of such supervision must be properly documented. It is recommended that the internal Shari'ah review must comply with the Code of Ethics for Accountants and Auditors of IFIs.

It should be borne in mind that the nature and scope of internal Shari'ah review is distinct from the normal auditing process. Generally, the scope of work comprises examination and evaluation in relation to the effectiveness of IFIs.

Apart from being responsible to the board of directors, the head of internal Shari'ah review has to properly manage the internal Shari'ah review and ensure that there is coordination between both internal and external review efforts. The head also has to establish a quality assurance programme.

### *3.4 Audit and Governance Committee for Islamic Financial Institutions*

This standard was adopted in the AAOIFI meeting held on May 2001 and it was effective over the financial periods commencing on 1 January 2002. The AAOIFI strongly recommend the establishment of an Audit and Governance Committee (AGC) at the board level. The AGC is also internationally known as the Audit Committee. This guideline provides for the roles and responsibilities of the AGC relevant to an IFI. Having the AGC as one of the main organs of an institution is evidently important to enhance greater transparency and disclosure. The salient features of this guideline are as follows:

The AGC is authorized by the board of directors to undertake various responsibilities. As such, the AGC is expected to have full communication with the board of directors including procuring consent from the latter to organize meetings and subsequently ensure the submission of reports.

The AGC consists of a minimum of three members appointed by the board of directors from its non-executive and independent board members who are knowledgeable on the affairs of the institutions and all applicable relevant laws and rules including a sufficient understanding of this Guideline. In addition, they are also required to have an adequate comprehension of relevant Shari'ah rules and principles.

The responsibilities of the AGC as enumerated in the Guideline are, inter alia, reviewing the internal controls and accounting practices and the audit plan.

### *3.5 Independence of Shari'a Supervisory Board*

This standard was adopted in the AAOIFI meeting held on 7-8 June 2005 but it was only effective about three years later, commencing from 1 January 2008. The salient features of this guideline are as follows:

The Shari'ah board cannot compromise employees of the same IFI who are involved in managerial decisions and operational responsibilities. This is so as to maintain fairness and independence. This Guideline also requires the SSB to regularly assess its relationship with IFIs to ensure that the SSB is independent

The performance of the SSB in decision-making must be honest and impartial. It also must avoid any form of impediments to being independent in making its judgment. Therefore, issues that may lead to such an impediment must be strictly taken into consideration, such as financial involvement with client affairs and personal and family relationships between the board of directors, management and the SSB.

### *3.6 Statement on Governance Principles for Islamic Financial Institutions*

This governance standard is known as the Statement, adopted by the AAOIFI in its meeting held on 21 November 2005. This statement is aimed at providing framework for governance practices and standards.

Shari'ah compliance structures must be effective so that communication between the SSB, board of directors, management and auditors transparent.

Equity holders must be given fair treatment and thus fair disclosure

Equitable treatment should be given to fund providers and other significant stakeholders. Information needs to be adequately and timely provided.

The board of directors and management must fulfill fit and proper criteria.

There must be an effective oversight of governance and hence, the board of directors should play an effective role in leadership, directing and monitoring the implementation of its policies

An audit and governance committee should be established comprising non-executive members of directors.

In terms of risk management, the board of directors should actively manage this.

At all times, any possible conflicts of interest between the organs of governance i.e. board of directors, SSB, management and other relevant parties, must be avoided.

There must be an appropriate compensation policy oversight set out by IFIs

In relation to public disclosures, IFIs are responsible for adopting high standard of reporting and for maintaining high standard of transparency.

Code of conduct and ethics must be implemented in accordance with Shari'ah rules and principles.

There must be appropriate enforcement of governance principles and standards.

### *3.7 Corporate Social Responsibility Conduct and Disclosure for Islamic Financial Institutions*

This governance standard was adopted at the AAOIFI meeting convened on 2 April 2009, effective beginning 1 January 2010. The standard was issued in order to prescribe compatible guidelines on corporate social responsibility activities and compliance for IFIs. It is also aimed at ensuring transparency and effective communication for relevant stakeholders of IFIs. There are several policies stipulated in the standard such as dealing with customers and on earnings and expenditures that must be Shari'ah compliant. Disclosure requirements are also further provided in the guideline. This standard underlines some important elements of corporate governance namely, transparency and accountability.

### C. Research Methods

The approach used in this study is a qualitative approach. Qualitative method is a research procedure that produces descriptive data in the form of written or oral words of people and observed behavior<sup>13</sup>. The reason of this research using qualitative approach is because in this research, the data produced in the form of descriptive data are obtained from the data in the form of writings, words and documents derived from sources or informants who studied and can be trusted.

Type of research used in this research is content analysis, which aims to find out the implementation of Corporate Governance in Islamic banking in Indonesia in terms of AAOIFI's Corporate Governance standard through the analysis of the annual Good Corporate Governance report of Islamic banking in Indonesia. The author used content analysis because the data to be researched requires descriptive explanation<sup>14</sup>. Content analysis is a systematic technique for analyzing the content of messages and processing messages, or a tool for observing and analyzing the contents of open communication behavior of selected communicators. Content analysis can be used to analyze newspapers, websites, advertisements, interview records, as well as company annual reports<sup>15</sup>.

The approach and the type of research use qualitative content analysis. This research method is an integrative analysis method of conceptual and more to find, identify, process, and analyze the documents to understand meaning, significance and relevance<sup>16</sup>.

The type of data used in this study is secondary data. Secondary data is an indirect source of data to data collectors, such as through other people or document boards<sup>17</sup>. Secondary data used in this study were collected from the annual report of Good Corporate Governance of each Islamic Bank in 2016 which can be seen from the official website of each company.

Research subjects used in this study are 11 Sharia Commercial Banks in Indonesia. Meanwhile, as the object of research, the author used annual corporate governance report at Sharia Commercial Bank in Indonesia.

The sample in this study is a Sharia Commercial Bank which has been issued Good Corporate Governance report in 2016. Based on data from [www.bi.go.id](http://www.bi.go.id) there are 11 Sharia Commercial Banks that can be sampled, namely:



1. Bank Muamalat Indonesia (BMI)
  2. Bank Syariah Mandiri (BSM)
  3. Bank Mega Syariah (BMS)
  4. Bank Rakyat Indonesia Syariah (BRIS)
  5. Bank Syariah Bukopin (BSB)
  6. BCA Syariah (BCAS)
  7. BNI Syariah (BNIS)
  8. Bank Maybank Syariah (BMYS)
  9. Bank Jabar Banten Syariah (BJBS)
  10. Bank Victoria Syariah (BVS)
  11. Bank Panin Syariah (BPS)
- D. Result and Discussion

### 1. Implementation of GCG in Islamic Banking in Indonesia

In connection with the promulgation of Circular Letter of Financial Services Authority Number 10 / SEOJK.03 / 2014, every Islamic bank has conducted Self-Assessment on the implementation of Good Corporate Governance. The following is the result of self-assessment of each Islamic bank:

**Table 1.1 The Predicate Value of Self-Assessment Results on the Implementation of GCG in Islamic Bank 2016**

No	Bank Name	Bank Code	Predicate
1	Bank Syariah Mandiri	BSM	Very Good
2	Bank Muamalat Indonesia	BMI	Good
3	Bank Rakyat Indonesia Syariah	BRIS	Good
4	Bank Negara Indonesia Syariah	BNIS	Good
5	Bank Mega Syariah Indonesia	BMSI	Good
6	Bank Central Asia Syariah	BCAS	Very Good
7	Bank Panin Syariah	BPS	Good
8	Bank Syariah Bukopin	BSB	Good
9	Bank Victoria Syariah	BVS	Good

10	Bank Maybank Syariah	BMS	Pretty Good
11	Bank Jawa Barat Syariah	BJBS	Pretty Good

Source: GCG Report of Islamic Banking Year 2016

**1. Implementation of GCG in Islamic banking in Indonesia based on AAOIFI Standard**

**Table 2.1 Implementation of AAOIFI Standard No. 1**

No	Sharia Supervisory Board: Appointment, Composition and Report	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	A Shari'a supervisory board is an independent body of specialized jurists in <i>fiqh almua'malat</i>	√	√	√	√	√	√	√	√	√	√	√
2	The appointment of Sharia Supervisory Board (SSB) must be made by shareholders of Islamic financial institutions upon the recommendation of its board of directors.	√	√	√	√	√	√	√	√	√	√	√
3	The Shari'a supervisory board shall consist of at least three members.	-	√	-	-	√	√	-	-	√	-	-
4	Each report should state that the management has performed its duty and properly complied with Shari'ah principles. To this end, the report must be published in the annual report.	√	√	√	√	√	√	√	√	√	√	√

Source: Secondary data processed, 2018

Information:

√ : disclosed

- : not disclosed

**Table 2.2 Implementation of AAOIFI Standard No. 2**

No	Shari'ah Review	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	Shari'ah review refers to an examination of financial activity which must be compliant with Shari'ah principles. This must be done on all policies, agreements, transactions and the like. In addition, the SSB should have full access to all information and records	√	√	√	√	√	√	√	√	√	√	√
2	Shari'ah review is done under the purview of the SSB. However, it does not waive management of the responsibility to provide all information to the SSB in relation to the Islamic financial institutions activities and services which must be compliant with Shari'ah principles. In this regards, both SSB and management play a pivotal role in ensuring Shari'ah compliance	√	√	√	√	√	√	√	√	√	√	√
3	The core of this guideline is the procedures set out pertaining to Shari'ah review consisting of three stages. All paperwork done in each stage must be properly documented. Firstly, planning review procedures must be sufficiently developed to understand the Islamic Financial Institutions operation as a whole including product and management. Secondly, the executing review procedures which it includes reviewing of contracts and discussing findings with the Islamic Financial Institutions management. Lastly, conclusions must be properly documented and reported to shareholders at the annual general meeting.	√	√	√	√	√	√	√	√	√	√	√

Source: Secondary data processed, 2018

Information:

√ : disclosed

- : not disclosure

**Table 2.3 Implementation of AAOIFI Standard No. 3**

No	Internal Shari'ah Review	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	The organizational status of the internal Shari'ah review must not be lower than the internal audit or internal control department. Management and the board of directors must support internal Shari'ah reviewers and the head of the internal Shari'ah review must be responsible to the board of directors. In addition, Shari'ah reviewers are also expected to communicate with the SSB and external auditors. As a whole, the performance of the internal Shari'ah reviewers must be independent.	-	-	-	-	-	√	-	-	-	-	-
2	Shari'ah reviewer must be competent and possess appropriate educational background, i.e proficient in Islamic commercial jurisprudence ( <i>fiqh al-muamalat</i> ). They are expected to exercise due professional care. The Shari'ah review must be consistently supervised and the evidence of such supervision must be properly documented. It is recommended that the internal Shari'ah review must comply with the <i>Code of Ethics for Accountants and Auditors of IFIs</i> .	-	-	-	-	-	√	-	-	-	-	-
3	It should be borne in mind that the nature and scope of internal Shari'ah review is distinct from the normal auditing process. Generally, the scope of work comprises examination and evaluation in relation to the effectiveness of IFIs. As such, internal Shari'ah reviewers must exercise their duty diligently in term of analysing, collecting and interpreting information and must timely and clearly report their findings. They should also monitor continuously that appropriate action is taken on these findings. They must follow up on all relevant matters decided upon by the SSB, external auditors and regulatory agencies.	-	-	-	-	-	√	-	-	-	-	-

Source: Secondary data processed, 2018

Information:

√ : disclosed

- : not disclosed

**Table 4. 1 Implementation of AAOIFI Standard No. 4**

No	Audit and Governance Committee for Islamic Financial Institutions	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	The AGC is authorized by the board of directors to undertake various responsibilities. As such, the AGC is expected to have full communication with the board of directors including procuring consent from the latter to organize meetings and subsequently ensure the submission of reports.	√	√	√	√	√	√	√	√	√	√	√
2	The AGC consists of a minimum of three members appointed by the board of directors from its non-executive and independent board members who are knowledgeable on the affairs of the institutions and all applicable relevant laws and rules including a sufficient understanding of this Guideline. In addition, they are also required to have an adequate comprehension of relevant Shari'ah rules and principles.	√	-	√	√	√	√	√	√	√	√	√
3	The responsibilities of the AGC as enumerated in the Guideline are, inter alia, reviewing the internal controls and accounting practices and the audit plan.	√	√	√	√	√	√	√	√	√	√	√

Source: Secondary data processed, 2018

Information:

√ : disclosed

- : not disclosed

**Table 2.5 Implementation of AAOIFI Standard No. 5**

No	Independence of Shari'a Supervisory Board	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	This Guidelines require the SSB to regularly assess its relationship with IFIs to ensure that the SSB is independent	√	√	√	√	√	√	√	√	√	√	√
2	The performance of the SSb in decision-making must be honest and impartial. It also must avoid any form of impediments to being independent in making its judgment. Therefore, issues that may lead to such an impediment must be strictly taken into consideration, such as financial involvement with client affairs and personal and family relationships between the board of directors, management and the SSB.	√	√	√	√	√	√	√	√	√	√	√

Source: Secondary data processed, 2018

Information:

√ : disclosed

- : not disclosed

**Table 2.6 Implementation of AAOIFI Standard No. 6**

No	Statement on Governance Principles for IFIs	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	Shari'ah compliance structures must be effective so that communication between the SSB, board of directors, management and auditors transparent.	√	√	√	√	√	√	√	√	√	√	√
2	Shareholders must be given fair treatment and thus fair disclosure	√	√	√	√	√	√	√	√	√	√	√
3	Equitable treatment should be given to fund providers and other significant stakeholders. Information needs to be adequately and timely provided.	√	√	√	√	√	√	√	√	√	√	√
4	The board of directors and management must fulfill fit and proper criteria.	√	√	√	√	√	√	√	√	√	√	√
5	There must be an effective oversight of governance and hence, the board of directors should play an effective role in leadership, directing and monitoring the implementation of its policies	√	√	√	√	√	√	√	√	√	√	√
6	An audit and governance committee should be established comprising non-executive members of directors.	√	√	√	√	√	√	√	√	√	√	√
7	In terms of risk management, the board of directors should actively manage this.	√	√	√	√	√	√	√	√	√	√	√
8	At all times, any possible conflicts of interest between the organs of governance i.e. board of directors, SSB, management and other relevant parties, must be avoided.	√	√	√	√	√	√	√	√	√	√	√
9	There must be an appropriate compensation policy oversight set out by IFIs	√	√	√	√	√	√	√	√	√	√	√
10	In relation to public disclosures, IFIs are responsible for adopting high standard of reporting and for maintaining high standard of transparency.	√	√	√	√	√	√	√	√	√	√	√
11	Code of conduct and ethics must be implemented in accordance with Shari'ah rules and principles.	√	√	√	√	√	√	√	√	√	√	√
12	There must be appropriate enforcement of governance principles and standards.	√	√	√	√	√	√	√	√	√	√	√

Source: Secondary data processed, 2018

Information:

√ : disclosed

– : not disclosed

**Table 2.7 Implementation of AAOIFI Standard No. 7**

No	Corporate Social Responsibility Conduct and Disclosure for Islamic Financial Institutions	BCAS	BJBS	BNIS	BRIS	BMSI	BMI	BPS	BSB	BSM	BVS	BMS
1	IFI shall implement a CSR policy for screening prospective clients.	√	√	√	√	√	√	√	√	√	√	√
2	IFIs shall implement a CSR policy for responsible dealing with client, including provisions relating to avoidance of onerous terms on clients, marketing ethics, implementing responsible financing practices in all types of transactions with clients and dealing with late repayments and insolvent client.	√	√	√	√	√	√	√	√	√	√	√
3	IFIs shall implement a CSR policy for earnings and expenditure prohibited by Shariah. (impermissible of haram transactions). This policy must include a due process procedure wherein the following must be documented for impermissible transactions	√	√	√	√	√	√	√	√	√	√	√
4	IFIs shall implement a CSR policy for employee welfare. This policy shall stipulate provisions for the rights and obligations of employees, including provisions affording fair treatment of all employees, avoidance of discrimination, as well as expected behaviour of all employees.	√	√	√	√	√	√	√	√	√	√	√
5	The terms and conditions under which a Zakat policy must be established are stated in Sharia Standard No. 35, Statement of Financial Accounting No. 2 Concepts of Financial Accounting for Islamic Banks and Financial Institution section 4/6 and Financial Accounting Standards No 9 on Zakah	√	√	√	√	√	√	√	√	√	√	√

Source: Secondary data processed, 2018

Information:

√ : disclosed

– : not disclosed

### **E. Conclusion**

1. The implementation of Good Corporate Governance in Islamic banking in Indonesia has been running very well especially in Bank BCA Syariah and Bank Syariah Mandiri. This is because in the results of its own assessment (Self-Assessment) on the implementation of Good Corporate Governance in 2016, received a very good predicate, and also surpassed the pioneer of Islamic banking in Indonesia, namely Bank Muamalat on the value obtained by Bank Muamalat that only get good ratings. This is a decline in the predicate for Bank Muamalat because in Ihsan's research stated that Bank Muamalat received a very good predicate from 2010-2013<sup>18</sup>.

2. The implementation of Corporate Governance in Islamic banking in Indonesia has not fully implemented the Corporate Governance standard issued by AAOIFI except Bank Muamalat which has implemented all AAOIFI standards. Some of the AAOIFI standards have not been applied by all other banks except Bank Muamalat which applies AAOIFI standard no 3 that is Internal Sharia Review. Bank Muamalat in the GCG report has stated that the division relating to Internal Sharia Review at Bank Muamalat is Sharia Compliance. The results of this study support the Mardian research indicating that Bank Muamalat Indonesia has disclosed in the GCG Report on the policy of extending the implementation of DPS duties through a special division called Sharia Compliance Department (ShCDep) which has 4 members and has Sharia competence and job clear description<sup>19</sup>. DPS should be assisted by the Compliance Division or the Sharia Compliance Department who assist DPS as a liaison officer with business units within Islamic banks and the Sharia Compliance Department facilitates the Islamic bank's interest in sharia aspects to be discussed and consulted to DPS and accompanying DPS to conduct routine supervision.

### **F. Suggestion**

1. For Bank BCA Syariah and Bank Syariah Mandiri which have received good predicate in self-assessment, there is a need to continue to maintain and also for other sharia commercial banks to continue practicing the implementation of good corporate governance to become a healthy company and also become part in building Islamic banking industry in Indonesia.

2. For all sharia commercial banks in order to make policies and have special units related to the Internal Shari'a Review. The objective is to assist the duties of the Sharia Supervisory Board and as a Liaison Officer between the Bank and the Sharia Supervisory Board in exercising regular monitoring of sharia aspects and to assist in preparing the supervisory reports of the Sharia Supervisory Board every semester that must be submitted to the Financial Services Authority.

3. For regulators should be able to clarify and make the rules regarding sharia supervision, because the regulator has an important role in realizing GCG in Islamic financial institutions and control and supervise the business activities of Islamic financial institutions. This is reinforced by the findings from Baehaqi which states that the evaluation of Sharia principles in sharia banking in Indonesia either with institutional approach or system approach is still not optimal<sup>20</sup>.



4. For further research it is expected to re-analyze the implementation of corporate governance based on AAOIFI standard by using GCG report in several periods and is expected to be able to examine other components of the annual report and not only use AAOIFI governance standards. This is necessary in order to re-know the development of the implementation of corporate governance in Islamic banking. REFERENCES

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