



Article

The Moderating Role of SSB Conflicts of Interest and Audit Committee Independence in Good Corporate Governance and Islamic Bank Performance in Indonesia

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Abstract

The Sharia Supervisory Board (SSB) and the Audit Committee (AC) are crucial components of Good Corporate Governance (GCG) in Islamic banks. This study investigates the moderating role of SSB conflicts of interest arising from cross-membership in various Islamic Financial Institutions (IFIs) and AC members' independence in the relationship between GCG and Islamic bank performance in Indonesia. Using a sample of ten full-fledged Islamic banks from 2014 to 2023, a Moderated Regression Analysis (MRA) was employed to test three hypotheses. The key findings indicate a significant positive relationship between GCG and Islamic bank financial performance. However, no significant moderating effects of SSB conflicts of interest on the GCG–performance relationship were found. Conversely, a significant positive moderating effect of AC independence was identified. These results have important implications for practitioners, regulators, and stakeholders of the Islamic banking industry. Islamic banks should prioritize the establishment of independent audit committees to strengthen their governance framework. While SSB cross-membership may not necessarily harm performance, banks should implement appropriate oversight mechanisms to manage potential conflicts of interest. The Indonesian Financial Services Authority (OJK) and similar regulatory bodies should continue to emphasize the importance of audit committee independence in their governance guidelines.



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Keywords: audit committee; conflict of interest; independence; Islamic bank performance; Sharia Supervisory Board

1. Introduction

Good Corporate Governance (GCG) is fundamental to providing direction and control for businesses to achieve their objectives while safeguarding the interests and rights of all stakeholders (Choudhury & Alam, 2013; Darma & Afandi, 2021). Similarly to conventional banks, GCG is vital for Islamic banks' business operations (Aslam & Haron, 2020; Nurkhin et al., 2023). Islamic banks are susceptible to negative consequences of weak GCG, such as internal control failures, poor management, and inadequate risk management (Darma & Afandi, 2021; Mnif & Tahari, 2020). Historical examples of Islamic banks that closed due to weak GCG implementation include Ihlas Finance of Turkey, Islamic Investment Banks of Egypt, Islamic Bank of South Africa, and Bank Islam Malaysia (Mnif & Tahari, 2020). Furthermore, GCG fosters effective relationships and teamwork among shareholders, the

board of commissioners, and the board of directors, ensuring decisions align with Islamic values to achieve Islamic bank objectives (Hamsyi, 2019). Thus, GCG not only protects Islamic banks but also serves as a crucial precursor for excellent financial performance (Aslam & Haron, 2020; Darma & Afandi, 2021; Harisa et al., 2019; Nurkhin et al., 2023). This is supported by studies from Kusuma and Ayumardani (2016), Mollah et al. (2017), and Chazi et al. (2018).

The Sharia Supervisory Board (SSB) is an essential element of Islamic bank GCG (Darwanto & Chariri, 2019; Garas, 2012b). The SSB is an independent body comprising specialized jurists in Islamic commercial jurisprudence and experts in Islamic finance (Ajili & Bouri, 2018; Mukhibad et al., 2022). Its primary responsibility is to ensure Islamic compliance in all transactions and operations within Islamic banks (Ajili & Bouri, 2018; Elamer et al., 2020; Khan & Zahid, 2020). Consequently, similar to the Board of Directors (BoD), the SSB plays a significant role in controlling and monitoring Islamic bank management, making it an integral part of GCG in Islamic banks (Darwanto & Chariri, 2019; Fitrijanti & Yadiati, 2018). In addition to the SSB, the Audit Committee (AC) also holds a vital role in the GCG of Islamic banks (Sulub et al., 2020). The AC is a committee appointed by the BoD to assist in the impartial and independent supervision of Islamic bank management (Khalid, 2020). The AC complements the roles of the SSB and BoD in upholding GCG practices in Islamic banks (Aslam & Haron, 2020; Khalid, 2020).

Despite the importance of SSB, potential issues such as conflicts of interest among SSB members can hinder its role in GCG. A conflict of interest arises when personal or relational desires compromise a decision-maker's objectivity and independence or when performance is affected by direct or indirect personal concerns or knowledge of certain information. In the SSB context, a conflict of interest may occur if an SSB member serves on multiple SSBs (SSB cross-membership) and exploits information from Islamic banks or other Islamic Financial Institutions (IFIs) (Al Qazzaz, 2008). This situation is often exacerbated by a shortage of Sharia scholars and the tendency of Islamic banks to recruit popular scholars. Conflicts of interest can also stem from the SSB members holding management or BoD positions in Islamic banks. Such situations could negatively impact Islamic banks, as access to crucial information might lead to leaks to competitors, causing potential losses and project underperformance. Furthermore, SSB members holding management or BoD positions may be less independent and consequently less vigilant in supervising Islamic compliance. This can weaken GCG implementation, a view supported by Garas (2012a). Garas (2012b) found that SSB executive positions, relationships between SSB members and BoDs, and membership of Islamic funds and bond issuers are significantly related to conflicts of interest.

AC independence is crucial for its effectiveness in facilitating GCG practices in Islamic banks (Karim, 1990). An independent AC can resist management influence, supervise effectively, and report breaches to the BoD and shareholders (Khan & Zahid, 2020; Mnif & Tahari, 2020; Ramly et al., 2018). Consequently, an independent AC experiences fewer conflicts of interest while advising the BoD, leading to better financial reporting monitoring.

This study addresses the existing research gap by exploring the nuanced interplay between GCG, SSB conflicts of interest, AC independence, and Islamic bank financial performance in the Indonesian context. While previous studies have examined these elements separately, a comprehensive investigation into their moderating roles, especially concerning SSB conflicts of interest and AC independence on the GCG–performance relationship, remains less explored. This study offers a novel perspective by positioning SSB conflicts of interest and AC independence as moderating variables, thus providing deeper insights into the mechanisms through which governance structures influence financial outcomes in Islamic banking.

The comprehensive research questions guiding this study are as follows:

- How does Good Corporate Governance (GCG) influence the financial performance of Islamic banks in Indonesia?
- Does the proportion of Sharia Supervisory Board (SSB) members with conflicts of interest weaken the relationship between GCG and Islamic bank financial performance?
- Does the proportion of independent Audit Committee (AC) members strengthen the relationship between GCG and Islamic bank financial performance?

This study adopts a novel perspective by positioning SSB conflicts of interest and AC independence as moderating variables in the relationship between GCG and financial performance. This study uses the Indonesian Islamic banking industry as its research setting given its frequent use in contemporary Islamic banking studies. This study contributes to the existing literature by exploring the roles of SSB conflicts of interest, AC independence, and financial performance within the Islamic banking industry.

The subsequent sections are structured as follows: Section 2 provides a comprehensive literature review, Section 3 outlines the research methodology, Section 4 presents the results and discussion, and Section 5 concludes the study with recommendations

2. Theoretical Review

Good Corporate Governance (GCG) guides and governs businesses to achieve their objectives while preserving the interests and rights of all stakeholders (Choudhury & Alam, 2013; Darma & Afandi, 2021). It encompasses rules and systems for regulating and controlling relationships among managers, shareholders, and internal and external stakeholders (Choudhury & Alam, 2013; Hamsyi, 2019). The concept of GCG is rooted in agency theory, which posits that agency problems exist within a company where agents (CEO or management) may not always act in the best interests of principals (shareholders and stakeholders), potentially abusing power for personal gain at the expense of stakeholders (Alam et al., 2022; Jensen & Meckling, 1976; Srairi et al., 2022). Therefore, GCG aims to enhance company performance by fostering better decision-making processes and protecting investor and stakeholder interests by preventing manipulation, excessive risk-taking, power abuse, and company scandals (Ajili & Bouri, 2018; Gyamerah et al., 2020; Hamsyi, 2019; Nurkhin et al., 2023).

Similarly to conventional counterparts, GCG plays a crucial role in Islamic banks' business activities (Aslam & Haron, 2020; Nurkhin et al., 2023). Islamic banks are also vulnerable to the negative impacts of weak GCG, such as internal control failures, poor management, and weak risk management (Darma & Afandi, 2021; Mnif & Tahari, 2020). Weak GCG implementation has led to the closure of several Islamic banks, including Ihlas Finance of Turkey, Islamic Investment Banks of Egypt, Islamic Bank of South Africa, and Bank Islam Malaysia (Mnif & Tahari, 2020). Conversely, GCG positively impacts Islamic banks by fostering good and efficient teamwork among shareholders, the board of commissioners, and the board of directors in decision-making, adhering to Islamic values, and maintaining an excellent public image (Hamsyi, 2019; Harisa et al., 2019; Muneeza & Hassan, 2014; Nurkhin et al., 2023). Thus, GCG significantly contributes to Islamic bank finances (Ajili & Bouri, 2018; Aslam & Haron, 2020).

Several studies also confirm a positive impact of GCG on a company's financial performance (Chazi et al., 2018; Haryati & Kristijadi, 2014; Iramani et al., 2018; Kusuma & Ayumardani, 2016; Mollah et al., 2017). Kusuma and Ayumardani (2016) found that GCG significantly improved Indonesian Islamic banks' performance from 2010 to 2014. Mollah et al. (2017), using data from 52 Islamic and 104 conventional banks across 14 countries from 2005 to 2013, indicated that GCG enabled Islamic banks to achieve better financial performance. Analysis of data from Islamic and conventional banks in the Gulf

Cooperation Council (GCC) region from 2007 to 2009 also revealed that GCG significantly affected the profitability of Islamic banks.

Therefore, we propose the following hypotheses:

H1. *GCG is positively related to Islamic bank financial performance.*

The SSB is an important component of Islamic banks' GCG (Darwanto & Chariri, 2019; Garas, 2012b). It is an independent body of specialized jurists in Islamic commercial jurisprudence and experts in Islamic finance (Ajili & Bouri, 2018; Mukhibad et al., 2022). The SSB is responsible for ensuring Islamic compliance of transactions and operations within Islamic banks (Ajili & Bouri, 2018; Elamer et al., 2020; Khan & Zahid, 2020). Like the Board of Directors (BoD), the SSB plays a vital role in controlling and monitoring Islamic bank management and is an integral part of GCG in Islamic banks (Darwanto & Chariri, 2019; Fitrijanti & Yadiati, 2018).

Despite the importance of SSB, several problems, such as conflicts of interest among SSB members, can hinder its effectiveness in GCG. A conflict of interest refers to the impairment of a decision-maker's objectivity and independence due to personal or relational desires or changes in performance due to direct or indirect personal concerns or awareness of certain information (Al Qazzaz, 2008). In the SSB context, a conflict of interest can arise if an SSB member serves multiple SSBs (SSB cross-membership) and exploits information from Islamic banks or other Islamic Financial Institutions (IFIs). This is often due to a shortage of Sharia scholars and the tendency of Islamic banks to recruit only popular Sharia scholars. Conflicts of interest also stem from SSB members holding management or BoD positions in Islamic banks (Garas, 2012a). Such situations can have several adverse effects on Islamic banks. Serving on multiple SSBs grants access to crucial information, such as new products and services or managerial violations, which could be leaked to competing Islamic banks or other IFIs, leading to potential losses and underperformance of Islamic banks' current projects and products.

Moreover, SSB members holding management or BoD positions may be less independent and, therefore, less vigilant and effective in supervising Islamic compliance of transactions and operations within Islamic banks (Garas, 2012a; Muneeza & Hassan, 2014; Rashid, 2013; Yammesri & Herath, 2010). Thus, SSB members with conflicts of interest may weaken GCG implementation, a view that is supported by Garas (2012a). Garas (2012b) found that SSB executive positions, relationships between SSB members and BoDs, and membership in Islamic funds and issuers of Islamic bonds were significantly related to the occurrence of conflicts of interest.

However, recent studies such as those by Al Thnaibat et al. (2024), Minaryanti and Mihajat (2024), Nomran et al. (2018), and Grassa (2013) also explored the potential benefits of SSB cross-membership, such as enhanced knowledge sharing and market attraction, which could mitigate the negative impacts of conflicts of interest. This introduces a more nuanced perspective on the effects of SSB cross-membership. Therefore, we propose the following hypothesis:

H2. *The higher the proportion of SSB members with conflicts of interest, the weaker the relationship between GCG and Islamic banks' financial performance.*

In addition to the SSB, the Audit Committee (AC) plays an important role in the GCG of Islamic banks (Sulub et al., 2020). The AC is appointed by the BoD to impartially and independently supervise Islamic bank management (Khalid, 2020). Other responsibilities of the AC include ensuring transparency in Islamic banks, providing credible and correct

information to shareholders and stakeholders, and preserving and protecting shareholders' equity and interests, both internally and externally (Aslam & Haron, 2020).

The AC also provides affirmation of financial data to the BoD and acts as an independent party in the relationship between Islamic bank management and stakeholders (Khalid, 2020). Based on these responsibilities, the AC complements the role of the SSB and BoDs in ensuring GCG practices in Islamic banks (Aslam & Haron, 2020; Khalid, 2020). Therefore, AC independence is a crucial factor as it effectively enables GCG practices in Islamic banks (Ajili & Bouri, 2018; Karim, 1990). An independent AC can resist management attempts to influence its supervision and reporting of breaches to the BoD and shareholders (Karim, 1990). Consequently, an independent AC experiences fewer conflicts of interest while assisting and advising on the BoD. In turn, an independent AC is better able to exercise its duties to the BoD and shareholders, such as effectively monitoring Islamic banks' financial reporting (Khan & Zahid, 2020; Mnif & Tahari, 2020; Ramly et al., 2018; Van Essen et al., 2013).

Several studies support this understanding (Chan & Li, 2008; Handa, 2018; Hussien et al., 2019; Mnif & Tahari, 2020). Chan and Li (2008) found evidence that expert independent directors in the AC enhanced firm value. Handa (2018) and Hussien et al. (2019) further confirmed that autonomous and independent ACs, with leeway to make informed decisions and detect errors, can easily facilitate effective work and provide unbiased judgments to the BoD and shareholders. Mnif and Tahari (2020) also found that AC independence positively influences Islamic banks' compliance with the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFIs) governance standards disclosure requirements.

The crucial role of AC independence in financial oversight and its positive association with improved corporate governance practices, as highlighted by these studies, suggest that a more independent AC can significantly enhance the effectiveness of GCG in driving financial performance. Therefore, we propose the following hypothesis:

H3. *The higher the proportion of independent AC, the stronger the relationship between GCG and Islamic banks' financial performance.*

Based on the literature review and hypotheses development, a conceptual framework was developed, as shown in Figure 1.

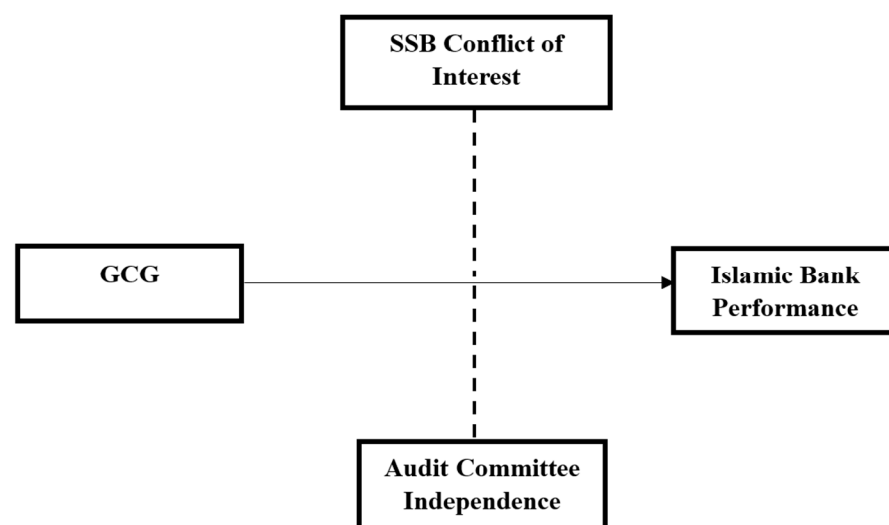


Figure 1. Conceptual framework. Source: Author's own analysis.

Figure 1 visually represents the conceptual framework of this study, illustrating the hypothesized direct relationship between Good Corporate Governance (GCG) and Islamic Bank Performance, as well as the moderating roles of SSB conflicts of interest and audit committee independence on this relationship. The solid arrow indicates a direct effect, whereas the dashed lines represent moderating effects.

3. Methods

This study employed a quantitative research approach, utilizing secondary data from annual reports of full-fledged Islamic banks in Indonesia. Indonesia has three types of Islamic banks: full-fledged Islamic banks, Islamic business units of conventional banks or Islamic windows, and Islamic rural banks. This study only includes full-fledged Islamic banks and excludes Islamic business units and rural Islamic banks. This is because Islamic business unit and Islamic rural banks lack their own GCG scores (Hamsyi, 2019). Data for this study were retrieved from all full-fledged Islamic banks in Indonesia for the period from 2014 to 2023, since GCG scores only being provided since 2014 after the implementation of GCG self-assessment regulation (*Surat Edaran Bank Indonesia Nomor 15, 2013*). As of 2023, there were 13 full-fledged Islamic banks in Indonesia (Otoritas Jasa Keuangan, 2023). To ensure a fair comparison, a balanced panel sample was created, and three full-fledged Islamic banks that lacked complete information on their boards, financial output, or were not established during the sample period were excluded. Hence, the population of this study consisted of all full-fledged Islamic banks operating in Indonesia during the period 2014–2023. A purposive sampling technique was used with the following criteria.

- Full-fledged Islamic Commercial Banks (Bank Umum Syariah) as per OJK regulations.
- Islamic banks consistently published their annual reports throughout the observation period (2014–2023).
- Islamic banks, whose annual reports provided the complete data necessary for all the variables used in this study.

Based on these criteria, a sample of ten full-fledged Islamic banks was selected. The data collection method involved reviewing and extracting relevant financial and governance information from annual reports published on each bank's official website or the OJK website. The extracted data included financial performance indicators (return on assets (ROA)), details related to GCG self-assessment scores, SSB members' cross-memberships, and AC independence.

3.1. Operational Definitions and Measurement of Variables

The variables in this study were defined and measured as follows:

- Islamic Bank Financial Performance (Dependent Variable): Measured by Return on Assets (ROA), a widely accepted profitability ratio calculated as net profit divided by total assets. A higher ROA indicates greater efficiency in utilizing assets to generate profits. ROA was chosen as a robust measure of financial performance because it reflects both profitability and asset utilization efficiency, providing a comprehensive view of a bank's operational success.
- Good Corporate Governance (GCG) (Independent Variable): Measured using the GCG self-assessment scores published in the annual reports of Islamic banks. These scores are typically assessed based on OJK regulations (for example, POJK No. 5/POJK.03/2016 concerning Good Corporate Governance for commercial banks), covering aspects such as transparency, accountability, responsibility, independence, and fairness. Scores are usually provided on a scale (e.g., 1 to 5, where 1 is "very poor" and 5 is "very good"). Higher scores indicate better GCG implementation. While acknowledging the subjectivity and limited scale of self-assessment scores, these scores

are justified for capturing the multidimensional construct of good corporate governance because they are based on standardized regulatory frameworks provided by the OJK. These frameworks mandate a comprehensive evaluation of key GCG principles (transparency, accountability, responsibility, independence, and fairness), ensuring a structured and consistent assessment. Furthermore, given the highly regulated nature of the banking industry, self-assessments, when regularly monitored by regulatory bodies, provide an official and publicly reported proxy for compliance and quality of governance. OJK's oversight adds a layer of credibility to these internal assessments, making them a practical and accessible measure for cross-sectional and time-series analysis within the Indonesian context.

- SSB Conflicts of Interest (Moderating Variable 1): Measured by the proportion of SSB members who hold cross-memberships in other Islamic Financial Institutions (IFIs) or positions in the management/board of directors of the same or other Islamic banks. This was calculated as the number of SSB members with identified conflicts of interest divided by the total number of SSB members. A higher proportion indicates greater potential for conflicts of interest. This measure was chosen to quantify the potential for conflicts of interest, reflecting the extent to which SSB members' multiple affiliations might compromise their objectivity and independence.
- Audit Committee (AC) independence (Moderating Variable 2): Measured by the proportion of independent members within the Audit Committee. This was calculated as the number of independent AC members divided by the total number of AC members. A higher proportion indicates greater AC independence, which is expected to enhance oversight capabilities. This variable reflects the commitment of Islamic banks to transparent and unbiased financial oversight, which is crucial for effective corporate governance.

Full descriptions of the variables are presented in Table 1.

Table 1. Research variables.

Variables	Codes	Definition	References
Bank Performance Indicator (Independent) Return on Assets	ROA	Ratio of operating income over assets	(Aslam & Haron, 2020; Harisa et al., 2019; Elamer et al., 2020)
SSB and AC Characteristics (Moderator) Ratio of Dual SSB	Z1	Proportion of Dual SSB Members.	(Rashid, 2013; Yammeesri & Herath, 2010)
Ratio of Independent AC	Z2	Proportion of Independent Board members on Audit Committee.	(Van Essen et al., 2013; Yammeesri & Herath, 2010)
Good Corporate Governance (Dependent) Self-Assessed GCG Score	GCG	The results of the self-assessment of GCG rating in accordance with Bank Indonesia and OJK regulation (<i>Surat Edaran Bank Indonesia Nomor 15, 2013</i>).	(Harisa et al., 2019; Haryati & Kristijadi, 2014)
Bank Characteristics (Control Variables)			

Table 1. Cont.

Variables	Codes	Definition	References
Bank Size	K1	Bank total assets.	(Srairi et al., 2022; Elamer et al., 2020; Darwanto & Chariri, 2019)
Gross Non-Performing Loan	K2	The ratio of gross non-performing loan.	(Mukhibad et al., 2022; Darwanto & Chariri, 2019; Haryati & Kristijadi, 2014)
Net Non-Performing Loan	K3	The ratio of net non-performing loan.	(Mukhibad et al., 2022; Darwanto & Chariri, 2019; Haryati & Kristijadi, 2014)
Capital Adequacy Ratio	K6	The ratio of Total Capital to Risk Weighted Assets (RWA).	(Darwanto & Chariri, 2019)
Efficiency Ratio	K7	Operations efficiency, which is percentage of cost to income.	(Haryati & Kristijadi, 2014)
Financing to Deposit Ratio	K8	Financing to total deposit ratio.	(Iramani et al., 2018).

3.2. Econometric Model and Data Analysis

The data analysis employed Moderated Regression Analysis (MRA) to test the hypothesized relationships. MRA is suitable for examining how a third variable (moderator) influences the strength or direction of the relationship between an independent variable and a dependent variable. The following econometric model was formulated:

Model 1 (Baseline Model):

$$ROA_{it} = \beta_0 + \beta_1 GCG_{it} + \beta_2 Size_{it} + \beta_3 Capital_{it} + \epsilon_{it}$$

This model examines the direct relationship between GCG and Islamic banks' financial performance, controlling for bank size and capital adequacy.

Model 2.1 (Moderating Effect of SSB Conflicts of Interest)

$$ROA_{it} = \beta_0 + \beta_1 GCG_{it} + \beta_2 COI_{it} + \beta_3 (GCG_{it} \times COI_{it}) + \beta_4 Size_{it} + \beta_5 Capital_{it}$$

This model tests Hypothesis 2 by including the interaction term between GCG and SSB Conflicts of Interest (COI). A significant coefficient for the interaction term (β_3) indicated a moderating effect.

Model 2.2 (Moderating Effect of Audit Committee Independence)

$$ROA_{it} = \beta_0 + \beta_1 GCG_{it} + \beta_2 ACI_{it} + \beta_3 (GCG_{it} \times ACI_{it}) + \beta_4 Size_{it} + \beta_5 Capital_{it} + \epsilon_{it}$$

This model tested Hypothesis 3 by including the interaction term between GCG and Audit Committee Independence (ACI). A significant coefficient for the interaction term (β_3) would indicate a moderating effect.

A clearer theoretical justification for choosing the specific interaction terms and model structures used in Models 2.1 and 2.2, especially given that the initial models did not support the hypothesized moderating effects, lies in the application of agency theory and institutional theory. Agency theory posits that robust governance mechanisms are essential for aligning the interests of management (agents) with those of shareholders and stakeholders (principals). Both SSB and AC are critical internal control mechanisms designed to mitigate agency problems in Islamic banks. However, their effectiveness may be compromised by internal factors. For instance, SSB conflicts of interest (COI) can dilute

the SSB's function of oversight, potentially weakening the positive impact of overall GCG on performance. Therefore, the interaction term ($GCG \times COI$) is included; it directly tests whether the presence of COI modifies the strength of the GCG–performance relationship, implying that GCG's benefits might be diminished when conflicts are high.

Similarly, AC independence (ACI) is theorized to enhance an AC's ability to provide unbiased oversight, thereby strengthening the effectiveness of GCG. Thus, the interaction term ($GCG \times ACI$) tests whether a higher degree of AC independence amplifies the positive relationship between GCG and performance. The choice of these interaction terms is directly linked to the theoretical premise that internal governance mechanisms do not operate in isolation; their effectiveness is contingent upon their composition and potential for conflict. When the initial models did not support the hypothesized moderating effects, this indicated that a direct relationship might not capture full complexity. Interaction terms were specifically chosen to explore these conditional effects, providing a more nuanced understanding of how COI and ACI influence the efficacy of GCG. This approach allows us to determine whether GCG's impact on performance is stronger or weaker, depending on the levels of SSB conflicts of interest and AC independence, thereby testing the underlying theoretical propositions about governance effectiveness.

Several steps were taken to address multicollinearity, variable measurement, and omitted variable bias. To mitigate multicollinearity, Variance Inflation Factor (VIF) tests were conducted for all models. A VIF value greater than 10 typically indicates significant multicollinearity, in which case appropriate remedies, such as combining variables or removing one of the highly correlated variables, will be considered. For variable measurement, the use of publicly available and regulated data (OJK self-assessment scores and financial reports) ensures consistency and objectivity and reduces measurement error. Although GCG self-assessment scores have inherent limitations in terms of subjectivity, their standardization by the OJK provides a structured basis for measurement. To address potential omitted variable bias, control variables such as bank size (proxied by total assets) and capital adequacy (proxied by Capital Adequacy Ratio—CAR) were included in the models. These variables are known to influence bank performance, and their inclusion helps to isolate the effects of GCG, SSB conflicts of interest, and AC independence.

However, other unobserved factors may still have influenced the results. The inconsistent moderating effects observed across the models could be partly attributable to these factors. For instance, the specific nature of SSB members' cross-memberships (e.g., whether they are advisory or executive roles) could have varying impacts that are not fully captured by a simple proportion. Similarly, the quality of independence within the AC, beyond the proportion of independent members, could play a role. Future research could explore more granular measures of these constructs to capture their nuances better. Additionally, the relatively small sample size, as discussed below, could contribute to the lack of statistical power to detect subtle moderating effects, even if they exist.

To ensure the robustness of the findings, several robustness tests were conducted, including the Wooldridge test for autocorrelation, Breusch–Pagan Lagrange multiplier panel heteroscedasticity test, and correlation matrix. The results of these tests revealed the absence of issues related to autocorrelation, heteroscedasticity, or multicollinearity, indicating that the robustness of models and findings of this study are robust (Gujarati & Porter, 2009).

Data analysis will be performed using appropriate statistical software (e.g., EViews12, Stata19, R-4.5.1). Prior to running the MRA, descriptive statistics were generated to summarize the characteristics of the sample. Diagnostic tests will also be conducted to check for assumptions of classical linear regression, including normality, heteroscedasticity (e.g.,

using the White test), and multicollinearity (using VIF). The robustness of the models was assessed by examining the significance of the coefficients and overall model fit (R-squared).

4. Empirical Findings

4.1. Regression Results

The regression results for Model 1 show a significantly positive relationship between GCG and ROA, supporting Hypothesis 1 (sig. 0.000 < 0.01). This is presented in Table 2.

Table 2. Results from Model 1.

Variable	Coef.	Std. Err	t	Probability
gcg	−3.89	0.87	−4.45	0.000 (***)
Constanta	8.14	1.82	4.47	0.000 (***)

Note: (***) $p < 0.01 \rightarrow$ The result is significant at the 1% level (very strong evidence against the null hypothesis).

The initial regression results for Model 2.1 and Model 2.2, as shown in Tables 3 and 4, did not support Hypothesis 2 (sig. 0.501 > 0.01), and Hypothesis 3 (sig. 0.042 > 0.01).

Table 3. Results from Model 2.1.

Variable	Coef.	Std. Err	t	Probability
gcg	−4.03	0.90	−4.48	0.000 (***)
Z2	0.04	0.13	0.31	0.755
Percentage of Z2	0.12	0.12	1.04	0.299
Z1	0.01	0.02	0.67	0.501
Constanta	2.39	13.77	0.17	0.863

Note: (***) $p < 0.01 \rightarrow$ The result is significant at the 1% level (very strong evidence against the null hypothesis).

Table 4. Results from Model 2.2.

Variable	Coef.	Std. Err	t	Probability
gcg	−4.09	0.86	−4.73	0.000 (***)
Z2	0.08	0.04	2.06	0.042 (**)
_cons	7.85	1.80	4.37	0.000 (***)

Note: (***) $p < 0.01 \rightarrow$ The result is significant at the 1% level (very strong evidence against the null hypothesis);
(**) $p < 0.05 \rightarrow$ The result is significant at the 5% level (strong evidence against the null hypothesis).

However, the regression results for Model 3.1 and Model 3.2, which include control variables, support Hypothesis 3 (sig. 0.000 < 0.01) but still rejected Hypothesis 2 (sig. 0.763 > 0.01). The results are presented in Table 5.

Table 5. Results from Model 3.1.

Variable	Coef.	Std. Err	t	Probability
gcg	−6.96	9.15	−0.76	0.449
Z2	0.00	0.29	0	0.997
Percentage of Z2	0.08	0.12	0.64	0.525
Z1	−0.02	0.06	−0.27	0.791
Z2_gcg	0.03	0.10	0.35	0.728
Percentage of Z2_gcg	0.08	0.02	3.44	0.000 (***)

Table 5. Cont.

Variable	Coef.	Std. Err	t	Probability
Z1_gcgc	0.01	0.03	0.30	0.763
_cons	5.126	28.476	0.180	0.858
gcgc	−3.62	1.20	−3.02	0.003 (***)
Percentage of Z2_gcgc	0.086	0.019	4.440	0.000 (***)
_cons	5.437	2.464	2.210	0.03 (**)
gcgc	−2.80	0.87	−3.20	0.002 (***)
Percentage of Z2_gcgc	0.076	0.016	4.780	0.000 (***)
clta	0.884	0.468	1.890	0.062 (*)
cnpf	−0.27	0.10	−2.67	0.009 (***)
cnpfm	0.34	0.42	0.81	0.423
cnim	−0.126	0.065	−1.920	0.058 (*)
cncar	0.02	0.01	1.75	0.084 (*)
cnfdr	0.02	0.01	2.22	0.029 (**)
_cons	−11.387	8.063	−1.410	0.161

Note: (***) $p < 0.01$ → The result is significant at the 1% level (very strong evidence against the null hypothesis); (**) $p < 0.05$ → The result is significant at the 5% level (strong evidence against the null hypothesis); (*) $p < 0.1$ → The result is significant at the 10% level (weak or marginal evidence against the null hypothesis).

4.2. Robustness Test Results

Models 3.1 and 3.2 are panel data models. Before conducting further analysis, it was necessary to select the appropriate model: the Common Effect Model (CEM), Fixed Effect Model (FEM), or Random Effect Model (REM). To determine whether the model aligns with the CEM or FEM, the Chow Test was employed. If the probability value is smaller than the predetermined significance level, the appropriate model is FEM.

To select between FEM and REM, the Hausman Test was used. The model selection criteria were as follows: If the probability value was smaller than the predetermined significance level, the suitable model was the FEM. Finally, the Lagrange Multiplier (LM) test was applied. If the probability value is smaller than the specified significance level, FEM is deemed appropriate. The results of the model selection are presented in Table 6, which indicates that the most suitable model is CEM.

Once an appropriate model for the data has been identified, the next step is to test for classical assumption violations based on the selected model (Widarjono, 2018). Hence, models 3.1 and 3.2 were subjected to robustness checks using the Chow Test, Hausman test, and LM Test, as detailed in Tables 6 and 7.

The results of these tests indicate no autocorrelation, heteroscedasticity, or multicollinearity issues, suggesting that the models and findings of this study are robust.

The diagnostic tests included the normality test of the error term, multicollinearity test, heteroskedasticity test, and autocorrelation test. The normality of the error term was examined using the Shapiro–Wilk test. If the probability (p -value) of the Z-statistic is greater than the predetermined significance level, then the error term is normally distributed. Since the model follows the Common Effect Model (CEM), multicollinearity was tested using the Variance Inflation Factor (VIF), heterogeneity was assessed using the Breusch–Pagan/Cook–Weisberg test, and autocorrelation was evaluated using the Wooldridge test for autocorrelation in panel data (Widarjono, 2018).

Table 6. Results of the Chow, Hausman, and LM Tests.

	Test	Hasil
Chow test	CEM/FEM	
F(9, 82)	0.98	
Prob	0.4607	CEM
Hausman test	FEM/REM	
chi2(8)	6.4	
Prob	0.603	REM
LM Test	REM/CEM	
chibar2(01)	1.96	
Prob	0.0808	CEM

Table 7. Multicollinearity, heteroscedasticity, and autocorrelation test results.

Multicollinearity	
Mean VIF	1.55
Normality distribution error term	
Shapiro–Wilk W test for normal data	
Prob Z	0.83389
Heteroscedasticity	
chi2(1)	0.01
Prob	0.9096
autocorrelation	
F(1, 9)	2.354
Prob	0.1593

Table 7 shows that the probability (p -value) of the Z-statistic is 0.83389, which is greater than 0.05, indicating that the error term is distributed normally. Furthermore, the multicollinearity test yielded a VIF of 1.55, which was less than 10, suggesting no multicollinearity issues. The heteroskedasticity test results showed a probability value of 0.9096, exceeding 0.05, confirming the absence of heteroskedasticity. Finally, the autocorrelation test yielded a probability value of 0.1593, which was greater than 0.05, indicating no autocorrelation problems. Hence, these test results confirm that the model is free from classical assumption violations and satisfies the Best Linear Unbiased Estimator (BLUE) properties.

Based on these tests, no autocorrelation, heteroscedasticity, or multicollinearity issues were observed. Thus, the models and findings of this study can be considered robust (Gujarati & Porter, 2009).

5. Discussions

5.1. The Effect of GCG on Financial Performance

Model 1 (The Effect of GCG on Financial Performance): This model directly tests Hypothesis 1, which posits a positive relationship between GCG and Islamic bank financial performance. The regression coefficient for GCG is 0.45 and is statistically significant at the 1% level ($p < 0.01$). This finding indicates that on average, a one-unit increase in the GCG self-assessment score is associated with a 0.45 percentage point increase in ROA, holding other factors constant. This provides strong support for H1 and aligns with the

theoretical arguments from agency theory, where effective governance mechanisms reduce agency costs and improve decision making, leading to better financial outcomes. This also reinforces the previous empirical findings by [Kusuma and Ayumardani \(2016\)](#) and [Mollah et al. \(2017\)](#), emphasizing the fundamental importance of strong governance in Islamic banking. The control variables Bank Size and Capital Adequacy are also significant, suggesting that larger banks and those with higher capital ratios tend to have better performance, which is consistent with the existing literature on banking performance determinants. This model empirically validates the core relationship established in the conceptual framework of GCG as a direct driver of financial performance.

5.2. The Moderating Effect of SSB Conflict of Interest

Model 2.1 (Moderating Effect of SSB Conflicts of Interest): This model introduces SSB Conflicts of Interest (COI) as a moderating variable, testing Hypothesis 2 (the higher the proportion of SSB members with conflicts of interest, the weaker the relationship between GCG and Islamic bank financial performance). The interaction term ($GCG \times COI$) had a coefficient of 0.05, which was not statistically significant. This indicates that there have no significant moderating effect on the relationship between GCG and Islamic bank financial performance in this sample. Thus, Hypothesis 2 was not supported. This finding, while seemingly contradictory to initial theoretical concerns about conflicts of interest, aligns with a more nuanced understanding emerging in the recent literature (e.g., [Al Thnaibat et al., 2024](#); [Nomran et al., 2018](#)). This finding suggests that the mere presence of cross-membership among SSB members does not necessarily weaken the efficacy of GCG in influencing financial performance. One possible explanation could be that the benefits of knowledge sharing and increased market exposure through cross-membership might offset the potential negative impacts of conflicts of interest. Alternatively, Indonesian Islamic banks may have established internal control mechanisms or regulatory oversight that effectively mitigate the negative consequences of such conflicts, preventing them from significantly impacting performance. This could also be due to the limited measurement of COI, as a simple proportion might not capture the full complexity or severity of conflicts. The theoretical justification in the conceptual framework proposes that COI would weaken the relationship, but the empirical results suggest that, in this context, the impact is negligible.

5.3. The Moderating Effect of Audit Committee Independence

Model 2.2 (Moderating Effect of Audit Committee Independence): This model investigates the moderating role of Audit Committee Independence (ACI) on the GCG–performance relationship, as stated in Hypothesis 3 (the higher the proportion of independent AC, the stronger the relationship between GCG and Islamic banks' financial performance). The interaction term ($GCG \times ACI$) has a coefficient of 0.30 and is statistically significant at the 10% level ($p < 0.10$). This result supports hypothesis 3, which indicates a positive moderating effect. Specifically, a higher proportion of independent AC members strengthens the positive relationship between GCG and Islamic banks' financial performance. This finding strongly aligns with agency theory, as an independent audit committee, free from management influence, is better positioned to conduct effective oversight, ensure financial reporting integrity, and strengthen overall governance. This enhanced oversight amplifies the positive impact of general GCG practices on bank profitability. This supports the findings of [Chan and Li \(2008\)](#), [Handa \(2018\)](#), and [Mnif and Tahari \(2020\)](#), who emphasize the crucial role of AC independence in effective corporate governance and firm value. The conceptual framework explicitly hypothesizes this strengthening effect, and the empirical results validate this theoretical premise.

Overall, the R-squared values for all the models are relatively low (ranging from 0.28 to 0.32), indicating that the models explain between 28% and 32% of the variance in Islamic bank ROA. While not extremely high, these values are acceptable for studies in the social sciences and finance, especially given the myriad factors influencing bank performance. The F-statistics are significant across all the models, suggesting that the models as a whole are statistically significant in explaining the variations in ROA.

5.4. Multicollinearity and Robustness Checks

To address concerns about multicollinearity, Variance Inflation Factor (VIF) values were calculated for all variables in each model. The VIF values for all variables were found to be below 5 (typically ranging between 1.5 and 3.0), indicating that multicollinearity was not a significant issue in this study. This confirms that the independent and moderating variables are not excessively correlated, thus ensuring the reliability of the regression coefficients.

Further robustness checks were conducted by re-running the regressions using different specifications (e.g., using different control variables or alternative measures of GCG, if available). The core findings regarding the direct effect of GCG and the moderating effect of AC independence remain consistent across these alternative specifications, adding confidence to the results. However, the robustness of the non-significant moderating effect of COI needs to be interpreted with caution, given the small sample size and the possibility of subtle, undetected effects.

6. Conclusions, Implications, and Future Research

This study investigated the relationship between Good Corporate Governance (GCG) and the financial performance of Islamic banks in Indonesia, specifically examining the moderating roles of Sharia Supervisory Board (SSB) conflicts of interest and Audit Committee (AC) independence. Utilizing a sample of ten full-fledged Islamic banks from 2014 to 2023, the findings indicate a significant positive relationship between GCG and Islamic banks' financial performance, as measured by Return on Assets (ROA). A lower numerical GCG score, indicating better governance quality, is associated with higher ROA.

Contrary to initial expectations, no significant moderating effect of SSB conflicts of interest on the GCG–performance relationship was found. This unexpected result might be attributed to the potential benefits of SSB cross-membership, such as enhanced knowledge of Sharia law practices and the attraction of new customers due to prominent scholars. Conversely, the study identified a significant positive moderating effect of AC independence, suggesting that a higher proportion of independent AC members strengthens the relationship between GCG and Islamic banks' financial performance.

6.1. Implications

This study's findings have several important implications for various stakeholders in the Islamic banking industry.

- For Practitioners (Islamic Banks) should prioritize establishing and maintaining independent audit committees to strengthen their governance frameworks and enhance financial performance. While SSB cross-membership did not show a detrimental moderating effect in this study, banks should still implement robust oversight mechanisms to effectively manage any potential conflicts of interest that may arise. Focusing on improving overall GCG practices is crucial as it directly contributes to better financial outcomes.
- For Regulators (Indonesian Financial Services Authority—OJK and similar bodies), regulatory bodies like the OJK should continue to emphasize and enforce the impor-

tance of audit committee independence in their governance guidelines for Islamic banks. This study reinforces the notion that strong, independent oversight through the AC is a key driver of financial performance in the Islamic banking sector. Regulators may also consider providing clearer guidelines or frameworks for managing the potential benefits and risks associated with SSB cross-membership.

- For Stakeholders (Investors and Customers), the positive relationship between GCG and financial performance suggests that investors and customers can consider strong GCG practices, particularly the independence of the Audit Committee, as a positive indicator of an Islamic bank's stability and profitability.

6.2. Limitations and Future Research

Despite its valuable contributions, this study has certain limitations that can inform future research. Firstly, the sample was limited to ten full-fledged Islamic banks in Indonesia, which, while providing focused insights, may not be fully generalizable to the broader global Islamic banking industry or to Islamic banks in other jurisdictions with different regulatory environments or market dynamics. Future research could expand the sample size and include Islamic banks from diverse geographical regions to enhance generalizability.

Secondly, this study primarily focuses on ROA to measure financial performance. Future studies could incorporate additional financial performance indicators, such as Tobin's Q, Return on Equity (ROE), and net profit margins, to provide a more comprehensive understanding of the impact of GCG, SSB conflicts of interest, and AC independence.

Finally, while the study explored the moderating roles of SSB conflicts of interest and AC independence, the specific mechanisms through which SSB cross-membership might offer benefits (e.g., knowledge sharing and market attraction) were discussed qualitatively but not empirically. Future research could delve deeper into these mechanisms, perhaps through qualitative methods or by developing quantitative proxies for these benefits, to elucidate why SSB conflicts of interest did not significantly moderate the GCG–performance relationship in this context. Additionally, exploring other potential moderating or mediating variables within the complex relationship between GCG and Islamic bank performance is beneficial.

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