Good Corporate Governance Principles in Islamic Banking: A Legal Perspective on the Integration of TARIF Values

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Good Corporate Governance Principles in Islamic Banking: A Legal Perspective on the Integration of TARIF Values

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ABSTRACT

Islamic banking, rooted in the foundational principles of *shiddiq* (honesty), *tabligh*, *amanah* (fulfillment of beliefs), and *fatanah* (intelligence) derived from the teachings of Prophet Muhammad, stands in stark contrast to conventional banking, which is driven by Western-derived concepts encapsulated in Good Corporate Governance (GCG). The latter is characterized by principles such as transparency, accountability, responsibility, independency, and fairness (TARIF). This research investigates the possibilities and implications of applying GCG principles in Islamic banking, examining their impact on Islamic economic law. Utilizing a normative legal study, the research delves into primary and secondary legal materials, employing a deductive analysis with both statutory and conceptual approaches. The integration of GCG principles in Islamic banking signifies a convergence of values that fosters justice, *tawazun* (balance), *mas'uliyah* (accountability), akhlaq (morality), *shiddiq* (honesty), *amanah* (fulfillment of beliefs), *fatanah* (intelligence), and economic equilibrium within the framework of Islamic economic law.

Keywords: Principles of Good Corporate, Islamic Banking, Islamic Economics

INTRODUCTION

As a collector and distributor of public funds, bank must have a high level of believe in the eyes of the community and the business world[1]. Financing is distributing fund to the people who need it either in the form of financing or in islamic bangking terms called "*mudharabah, musyarakah or murabahah*" does not always bring benefits. In other words, the financing carried out is always haunted by risks. Risk is an integral part of life. There is a saying that there is no life without risk[2]. Risks are also faced by companies including banking companies. From the beginning and at the time of running the business, it revealed the possibilities of risks that will be faced, the risk of loss or business failure for instance. Therefore, effort is needed to run a business [3]. Ways or method to overcome or to avoid the risk of

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1 Umar Chapra dan M. Toriq Ullah Khan, *Regulasi Dan Pengawasan Bank Syariah* (Sinar Grafika Office, 2008).

2 H. Misbahul Munir, *Implementasi Prudential Banking Dalam Perbankan Syariah* (Indonesia: UIN-Malang Press, 2009).

3 H. Misbahul Munir.

business loss is to apply the "*Principles of Good Corporate Governance*" in banking activities both in conventional and Islamic banks. Good Corporate Governance principles have been acknowledged as the best company management method [4].

The excution of the concepts of GCG in Islamic banking is urgent for several reasons, are: first of all achieving business continuity (sustainability). [5] Secondly, ensuring trust for the stakeholders [6]. Thirdly, improving company performance by increasing company profits and the value of company shares [7].

Business activity is a mu'amalah feature of Islamic systems since it uses fiqh principles to identify economic transactions, which also employ mu'malah fiqh concepts [8]. Therefore, Islamic banks must fulfil the principles of sharia. Nevertheless, the use of GCG in Islamic banks is anticipated to improve bank operations, investor interest security, adherence to rules and regulations, and upholding universally recognized moral principles [9] Adoption of the concepts of Good Corporate Governance with goal that the purpose of the establishment of Islamic banks can be realised. The goals of Islamic

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[4] Irwan Sugiarto, "The Significance of Good Corporate Governance Principles in The Company Law of 2007," *MIMBAR, Jurnal Sosial Dan Pembangunan* 33, no. 1 (2017): 37, https://doi.org/10.29313/mimbar.v33i1.2067.

[5] Ahmad rojali Rojali, "Analisis Pengaruh Penerapan Good Corporate Governance Terhadap Kinerja Perbankan Syariah Di Kota Medan," *Juripol* 4, no. 1 (2021): 276–84, https://doi.org/10.33395/juripol.v4i1.11038.

[6] Sukirno Carmindah, "Corporate Governance Dan Kinerja Keuangan Bank Syariah Di Indonesia" 17, no. 01 (2021): 1–15.

[7] Syafrudin Arif, "Dampak Good Corporate Governance Terhadap Kinerja Perbankan : Market Risk Sebagai Intervening," *Equity* 23, no. 2 (2011): 167–88, https://doi.org/10.34209/equ.v23i2.2073.

[8] Suryani Suryani et al., "Good Corporate Governance (Gcg) Principle in Sharia Banking: An Islamic Law Perspective," *International Journal of Law Reconstruction* 5, no. 2 (2021): 242–54, https://doi.org/10.26532/ijlr.v5i2.14973.

[9] Akhmad Faozan, "Implementasi Good Corporate Governance Dan Peran Dewan Pengawas Syariah Di Bank Syariah," *La_Riba* 7, no. 1 (2013): 1–14, https://doi.org/10.20885/lariba.vol7.iss1.art1.

banks are: [10]. Firstly, encouraging the economic activities of the *"ummah"* to prevent the use of interest on loans or other types of business or trade that contain elements of fraud. Secondly, creating justice in the economic field. Islamic banks must implement a fair role as the goal of Islamic banks, namely with no one to be vilified, and must not pursue personal gain. Thirdly, maintaining economic and monetary stability. Fourthly, improve people's qualities of living by opening up greater business opportunities. And finally, saving the dependence of the Islamic ummah on non-Islamic banks.

Furthermore, to achieve this goal, Islamic banks has to carry out financing with a direct method based on profits and losses sharing, the financing aims to:[11].

1. Providing a more elastic mechanism for Islamic banks in disbursing various kinds of financing, that can compete with conventional banks, can cover all the needs of industrial projects, trade, and services, and does not violate Islamic law.
2. Re-optimizing the essential understanding of the bank's core role in realizing economic growth through efforts to manage customer-owned assets and generating multiple values derived from its active role in providing capabilities and experiences that can learn, assess and choose which investment is more ideal.
3. Gradually directing the financing system in murabahah (which is the case of buying and selling contracts), into a consumptive financing practice through a special trading company established by the bank together with business people using the musyarakah financing system (sharing profits and losses). That way, the bank can build superior structures and have a strong organization that can carry out its trading activities without the need to burden the bank to carry out activities as a trade mediator, when it does not

[10] Ari Kristin Prasetyoningrum, *Risiko Bank Syariah, Risiko Imbal Hasil, Risiko Investasi, Return Tingkat Dana Pihak Ketiga Dan BI Rate* (Indonesia: Pustaka Pelajar, Yoyakarta., 2015).

[11] Addys Aldizar, *Sains Dalam Perspektif Islam* (Indonesia: Lintas Media, Jakarta, 2017).

have sufficient experience and feasibility to carry out tasks like this effectively.

In the future, the possibility of misconduct in Islamic banks is possible, even though there is a *sharia* supervisory board, because the perpetrators are not angels. Especially now that there are abundant Islamic banks and Islamic bankers. In this regard, the executives and officials of the bank, even including the commissioners, are extra careful in managing Islamic banking institutions that have been considered "sacred", because they are derived from the divine principle. Understandably, religious symbols did not guarantee all institutions to be clean from corrupt behavior, because people are often tempted by the treasures of the world[12].

Problems that often occur in Islamic banks include quality performance. Islamic banks are required to maximize benefits for the community and be responsible for of course all activities carried out with guidelines on sharia principles. The existence of Islamic banking aims are to meet the public's need for the availability of financial transaction services that are in line with Islamic sharia principles, such as being free from ghara, masyir, and also usury [13].

In reality, several things are often done by shareholders (stakeholders) that are contrary to GCG principles. The shareholders' actions including: involved either directly or indirectly in bad faith in utilising the enterprise solely for private profit; involved in an illegal act committed by the firm, and investors involved illegally utilized the firm's wealth, either directly or indirectly, resulting in the corporation's wealth being not enough to pay off the firms debts.

This study will discuss how is the application of GCG concepts in sharia bank while we know that the GCG principles is came from the western values. In Indonesia, it was introduced by the IMF in the

[12] Putri Indar Dewi, "Penerapan Good Corporate Governance (Gcg) Di Lembaga Perbankan Syariah" 3, no. 2 (2020): 1–15, https://doi.org/https://doi.org/10.30863/al-tsarwah.v3i2.1150.

[13] Lucky Rachmawati Tiara Novia Amelinda, "Pengaruh Penerapan Good Corporate Governance Terhadap Kinerja Keuangan Bank Umum Syariah Di Indonesia," *Jurnal Ekonomika Dan Bisnis Islam* 4, no. 1 (2021): 33–44, https://doi.org/https://doi.org/10.26740/jekobi.v4n1.p33-44.

context of economy recovery after crisis [14] The GCG principles are a framework and set of rules that control how different shareholders interact with one another, particularly how shareholders interact with the board of commissioners and the executive board to further company objectives.[15] In addition, GCG principle could be an effective method to increase shariah compliance, due to the lack of people's trust towards shariah banking.

This study aims to contribute to the existing body of knowledge concerning the implementation of Good Corporate Governance (GCG) in Islamic banking. It seeks to address the current gap by meticulously describing and analyzing the principles of Islamic Economic Law in relation to good corporate governance. While numerous studies have explored the implementation of GCG principles in Islamic banking across various disciplines, there remains a notable deficiency in the literature. Existing research has, to a large extent, overlooked the need for a clear and comprehensive depiction of the symmetrical alignment between Islamic Economic Banking law principles and the tenets of good corporate governance within legal discourses. This study endeavors to fill this void and provide a nuanced understanding of the intricate interplay between these two critical domains.

Several studies have explored the intersection of corporate governance and Islamic banking. For instance, Kolsi and Grassa conducted a study titled "Did corporate governance mechanisms affect earning management? Further evidence from GCC Islamic banks," and their research aimed to investigate the impact of corporate governance practices on the earnings management practices of Gulf Cooperation Council (GCC) Islamic banks. Utilizing a novel earnings management model, the authors examined various governance factors and concluded that reinforcing governance

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[14] M.A. Effendi, *The Power of Good Corporate Governance: Teori Dan Implementasi* (Indonesia: Salemba Empat,Jakarta, 2016).

[15] Puji Lestari, Umi Pratiwi, and Permata Ulfah, "Identifikasi Faktor Organisasional Dalam Pengembangan ' E-Governance ' Pada Organisasi Pengelola Zakat" 31, no. 1 (2019): 221–28.

mechanisms, potentially through new legislation or enhanced enforcement, could mitigate the negative effects of earnings management on information openness and financial reporting quality in Islamic banks.[16]

Similarly, Mergaliyev et al, contributed to this field with their study, "Higher Ethical Objective (*Maqasid al Shariah*) Augment Framework for Islamic Bank: Assessing Ethical Performance and Exploring its Determinants," published in the Journal of Business Ethics. This research employed the higher ethical objectives proposed in Islamic moral economy, specifically the *maqasid al shariah* theoretical framework, to evaluate the moral, social, environmental, and financial performance of Islamic banks. The study, encompassing 33 full-fledged Islamic banks from 12 countries over eight years, revealed a positive impact of disclosing *maqasid* performance. However, the study cautioned against proclaiming these practices as best-practices, highlighting intricate and varied relationships between *maqasid* performance, corporate governance practices, and external market circumstances.[17]

Additional studies further contribute to the discourse on corporate governance in Islamic banking. For instance, Suryani et al. explored the "Good Corporate Governance (GCG) Principle in Sharia Banking: An Islamic Law Perspective:. This research highlighted the imperative need for implementing a robust corporate governance system in Indonesian Sharia banking. Emphasizing its potential to enhance financing quality, improve infrastructure and corporate

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16 Mohamed Chakib Kolsi, and Rihab Grassa. "Did corporate governance mechanisms affect earnings management? Further evidence from GCC Islamic banks." *International Journal of Islamic and Middle Eastern Finance and Management* 10, no. 1 (2017): 2-23.

17 Arman Mergaliyev, et al. "Higher ethical objective (Maqasid al-Shari'ah) augmented framework for Islamic banks: Assessing ethical performance and exploring its determinants." *Journal of Business ethics* 170 (2021): 797-834.

decision-making, and act as an early warning system for high-risk business sectors, goods, and services.[18]

In a related study, Septiani et al. (2022) investigated "Good Corporate Governance in Islamic Banking during the Fourth Industrial Revolution Era," and the research identified that the application of GCG in Indonesian Islamic banking was reasonably effective but identified areas for improvement. Notably, the governance mechanism's alignment with Shariah principles needed enhancement, with a particular focus on strengthening the role of the Sharia Supervisory Board.[19]

A noteworthy contribution by Obid and Naysary in their article, "Toward a comprehensive theoretical framework for Shariah governance in Islamic financial institutions," provided a comprehensive review of the theoretical foundations underpinning corporate governance and Shariah governance. Examining three widely used theories—agency theory, stewardship theory, and stakeholder theory—the authors identified five key concepts within the theoretical framework: accountability, disclosure and transparency, competency, confidentiality, and independence among the key functionaries in Shariah governance. These principles were recognized as integral components of effective Shariah governance in Islamic financial institutions.[20]

This research adopts a normative legal study, commonly referred to as doctrinal research. The aim of normative legal studies, also known as doctrinal research, is to hypothesize, correct, and clarify legal rules applicable to a specific field of law by analyzing

[18] Suryani Suryani, et al. "Good Corporate Governance (GCG) Principle in Sharia Banking: An Islamic Law Perspective." *International Journal of Law Reconstruction* 5, no. 2 (2021): 242-254.

[19] Delina Herdian Septiani, et al. "Good Corporate Governance in Islamic Banking during Fourth Industrial Revolution Era." *Islamic Research* 5, no. 1 (2022): 98-107.

[20] Siti Normala Sheikh Obid, and Babak Naysary. "Toward a comprehensive theoretical framework for Shariah governance in Islamic financial institutions." *Journal of Financial Services Marketing* 19 (2014): 304-318.

authentic texts, including primary and secondary legal materials.[21] Beyond the correction and clarification of rules, the doctrinal method involves providing a comprehensive description of the regulations governing a specific legal category. It delves into the analysis of the interconnections among laws, discusses areas of contention, and, potentially, anticipates future developments. In the context of this research, the latter aspect aligns well, as the study explores the possibilities and opportunities for the application of Good Corporate Governance (GCG) principles within Islamic Banking.

The research approaches used were statutory and conceptual approaches. The type of law material includes the primary law material sourced from laws and relevant regulations to the legal problems under study and secondary law material sourced from legal materials [22]. In the form of textbooks, journals, islamic law, and Indonesian national law related to good governance and Islamic Banking. The method of gathering legal resources was conducted by desk study, both through the internet and libraries. Analysis of legal documents was performed using deductive techniques, description and analysis presented from general issues and proceeding to specific issues

ISLAMIC PRINCIPLES *vis a vis* WESTERN VALUES ON BANKING

A. Islamic Principles on Banking

Islamic banking which is widely known as Shariah banking refers to the financial that adhere to Sharia or Islamic principles. There are two core tenets of Islamic banking, are: the sharing of profit and loss and

[21] Dyah Ochtorina Susanti dan A'an Efendi, *Penelitian Hukum (Legal Research)* (Sinar Grafika, Jakarta., 2015).

[22] Muhaimin Muhaimin, *Metode Penelitian Hukum* (Mataram University Press, 2022).

the restriction on interest collection and payment by lenders and investors.[23]

The Prophet Muhammad PBUH is the main role model in Islamic society, therefore moslem activities: personal, business, and spiritual are inspired by the qualities of the Prophet Muhammad.[24] The four qualities of the Prophet Muhammad, are below:

a. *Shiddiq* (Honest)
   Ensure that the management of sharia banks is conducted with the morality that encourages the utmost value of integrity. This value represents that managing public funds will be done by prioritizing ways that introduce (halal) and avoiding ways that are doubtful (*subhat*), especially those that are prohibited (haram).

b. *Tabligh* (Communicate)
   Continuous efforts are made to socialize and inform the general public regarding the principles, goods and services of Islamic banking. Not only does it highlight the compliance of sharia requirements when conducting socialization, but it must also be able of educating the public concerning the merits of using sharia financial services.

c. *Amanah* (Trustable)
   Trust is highly prioritized to be preserved and performed. Trust (*amanah*) is not used as commodity that is only a label but rather a realistic implementation. Maintaining the concept of prudence and honesty in financial institutions, especially in Islamic banks, can be used as a reference to the success in managing funds or money received from shareholders called fund owners (*shahibul maal*) so that by itself will create mutual trust among investors and fund managers (*mudharib*).

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23 Evan Tarver, "Islamic Banking and Finance Definition: History and Example Accessed Through," 2023, https://www.investopedia.com/terms/i/islamicbanking.asp.

24 Yusron Ali Sya'bana, and M. Yasir Nasution. "Bisnis Ala Rasulullah dalam Perspektif Pemasaran." *At-Tijarah: Jurnal Penelitian Keuangan dan Perbankan Syariah* 4, no. 2 (2022): 189-201.

d. *Fathanah* (Intelligent)
Ensuring that the bank's management system is conducted in a very professional and competitive manner to achieve maximum benefit within the risk range set by the bank. This consists of services that are full of meticulousness and civility (*ri'ayah*) and a sense of responsibility (*mas'uliyah*).

B. Western Values on Banking

The principle of conventional banking refers to international and national agreement and is implemented by state regulation. Conventional banks are banks which in their activities, both in collecting funds and in the context of distributing funds, provide and charge compensation in the form of interest or a number of rewards in a certain percentage of the funds for a certain period. This certain percentage is usually set annually[25].

The basic principle of conventional banking is interest payment.[26] The efficiency of conventional banks has been widely studied in the literature to assess banks' experience in achieving their goals. Efficiency is defined as a measure of performance indicating how cautious a bank applies its resources, which produces output. This means better profitability, prices, and quality of services for consumers, and a greater number of financial mediations[27].

To manage savings from the public and pay for bank operational costs, banks distribute these funds in the form of investments, for speculative purposes, and provide large-scale credit to other banks or the government with investments included in the company's activities, thereby obtaining share of profits in the form of dividends,

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[25] Sigit Triandaru and Totok Budisantoso, "Bank Dan Lembaga Keuangan Lain," *Jakarta: Salemba Empat* 200 (2006).

[26] Junaidi Junaidi, et.al., "Determinants to adopt conventional and Islamic banking: evidence from Indonesia", *Journal of Islamic Marketing* 14, no. 3 (2023): 892-909

[27] Allen N Berger, William C Hunter, and Stephen G Timme, "The Efficiency of Financial Institutions: A Review and Preview of Research Past, Present and Future," *Journal of Banking & Finance* 17, no. 2–3 (1993): 221–49.

or interest rates. Whereas bank interest can be understood as compensation given by banks to clients who buy or sell their products based on established principles. Interest for banks can alternatively be seen as the cost that must be borne by customers (who have savings) and the cost that customers (who seek loans) must pay to the bank.

In daily banking activities, there are two types of interest given to customers, that are:

1. Savings interest
   Interest is given as stimulation or compensation for customers who save their money in the bank. Savings interest is the price that the bank must pay to its customers. For example, giro services, savings interest and deposit interest.
2. Loan interest
   Loan interest is the interest given to borrowers or the price that borrowers must pay to the bank. For instance, credit interest.

These two types of interest are the main components of cost factors and income for banks. Savings interest is the cost of funds that must be paid to customers, while loan interest is income received from customers. Both deposit interest and loan interest each influence each other. For example, if savings interest is high, loan interest will automatically increase and vice versa.

THE DEVELOPMENT OF ISLAMIC BANKING IN INDONESIAN LEGAL SYSTEM

A. The Emergence Islamic Banking: Post 1998 Crisis Recovery

The idea of establishing a sharia bank emerged in 1988, since the issuance of government's policy called the October Policy Package (PAKTO) which contained the liberalization of the banking industry in Indonesia. After recommendations from the ulama workshop on bank interest in Cisarua Bogor on 19-22 August 1990. The results of the workshop were discussed in more depth at the IV National Conference of the Indonesian Ulema Council (MUI) which took place on 22-25 August 1990 in Jakarta.

A working group was created to establish a sharia bank in Indonesia, which consist of the government, the Association of Scholars Muslim Indonesia (ICMI), and a few Muslim business-people, as the deed of establishment was signed on the date of 1 November 1991 (Antonio 2001) as the effort of the Council of Indonesia Ulama (MUI). Finally, the Bank Muamalat Indonesia (hereafter called BMI) was the first Islamic banking which were established in 1991. However, Bank Muamalat only started operating on May 1, 1999.[28]

The establishment of Bank Muamalat was a form of acceptance of the new legal system, the Islamic economic legal system entering Indonesia, which was not an Islamic country. Encouragement by the global community with the development of Islamic banking which eliminates the element of usury which is considered haram and replace it with a revenue sharing system permitted by the Qur'an.[29]

There was a shift in law, from Islamic law to state law, as stated by Santilana, that in fact in this case Islamic law in general is very adequate for the legal needs of Muslims, it is not even an exaggeration to say that Islamic law is sufficient for all humanity.[30] The journey from the formation of the first sharia bank to the introduction of the concept of sharia banking was a process of legal transplantation. It could be the whole system or part of it, it could be the legal system

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[28] Zulfadli Nugraha Triyan Putra, and Husni Thamrin. "Problematika dan Dinamika Perbankan Syariah di Era Globalisasi." *Jurnal Tabarru': Islamic Banking and Finance* 5.1 (2022): 34-40.

[29] Siti Aisjah, and Agustian Eko Hadianto. "Performance Based Islamic Performance Index (Study on the Bank Muamalat Indonesia and Bank Syariah Mandiri)." *APMBA (Asia Pacific Management and Business Application)* 2, no. 2 (2015): 98-110.

[30] Abdul Manan, "Acceptance of the implementation of Islamic sharia laws in West Aceh, Indonesia." in *International Conference on Humanities, Education, and Social Sciences, KnE Social Sciences* (2020): 615–627. DOI 10.18502/kss.v4i14.7919

being transferred, it could be an individual or even the community. In the context of Islamic banking in Indonesia, it is adopting the Islamic economic system but not in its entirety.

The acceptance process requires time which is not easy, this is proven by the legal basis for implementing sharia banking, when BMI was formed there was no law that specifically regulated sharia banking.

B. From Law 7 of 1992 to Law 21 of 2008

The implementation of sharia banking in Indonesia, originally referred to the application of banking Law No. 7 of 1992, which created prospects for a bank operating based on sharia principles, is a very fundamental development in the Islamic banking sector.

In responding to several articles in this Law, the Indonesian government finally issued Government Regulation Number 7 of 1992 concerning Banks based on the profit-sharing principle which was promulgated on 30 October 1992. In the Explanation of this regulation, it is emphasized that commercial banks or rural banks whose business activities are solely based on the principle of profit sharing, it is not permitted to carry out business activities that are not based on the principle of profit sharing, and vice versa.

Even this existing legal umbrella is not strong enough as a basis for sharia banking operations, but society has accepted Islamic law as part of state law. BMI continues to grow. It is an extraordinary achievement that the growth of Islamic banks increased and during the 1998 economic crisis, Islamic banks were able to survive this condition. This development is not achieved easily, it requires hard work and government intervention to be able to increase the growth of Islamic banks over time so that they can be fully accepted by the Indonesian people. In 1998, Law No. 7 of 1992 was amended by the Law No. 10 of 1998. The passage of Act No. 10 of 1998 made it possible for banks to switch to sharia banking operations simultaneously or in part by opening sharia bank offices.

The robust growth of Bank Muamalat Indonesia (BMI) has not only spurred the establishment of other sharia-based banks but has also prompted conventional banks to introduce sharia services. Notable examples include Mandiri Syariah, CIMB Niaga Syariah, BRI Syariah, BNI Syariah, and others. This increasing trend signifies a growing demand from the public for a banking system rooted in profit-loss sharing principles. In response to this shift, the government enacted policies governing sharia banking through the issuance of Law Number 21 of 2008, marking a crucial development after 16 years of sharia banks operating in the country.

The observation that the introduction of sharia banking laws doesn't always receive immediate acceptance points to the complexities and challenges involved in implementing such regulatory changes. In the context of Indonesia, this resistance or hesitancy is noteworthy, especially given the context of the 2011 final report. This report indicates that the asset growth of national sharia banks experienced a remarkable surge of 48.1% compared to the previous year, securing a market position of 3.7%. While this percentage might not seem monumental in isolation, it is crucial to consider that this growth represents substantial progress over a span of 19 years, as highlighted by the data from Bank Indonesia in 2012.

On a global scale, the sharia banking sector's monumental reach of 250 billion US dollars, coupled with a growth rate of 15% annually, underscores the increasing prominence and resilience of sharia-based financial services. In 2011, Indonesia marked the presence of 11 Sharia Commercial Banks, 23 Sharia Business Units, and 154 Sharia People's Financing Banks. This proliferation of sharia banking institutions is indicative of a broader acceptance and integration of sharia principles within the financial landscape.

Moreover, the transformation in the financial sector is highlighted by the increasing alignment of financial services offered by sharia banks with those of conventional banks. This includes both fund collection and distribution processes. While the pace of this alignment may not match that of conventional banking systems, the overall trend signifies a notable shift in the financial landscape. This shift is driven by the growing popularity and acceptance of sharia-based banking services, reflecting changing preferences and an evolving understanding of ethical and Sharia-compliant financial practices.

GOOD CORPORATE GOVERNANCE: INTERPRETATION, ADOPTION, & IMPLEMENTATION IN THE ISLAMIC BANKING SYSTEM

A. A Brief Description on Good Corporate Governance

The Indonesian banking industry has at least 3 documents that can be used as a reference in implementing Good Corporate Governance for commercial banks in accordance with the order of publication. These documents are enhancing Corporate Government for Bank Organizations (issued by the Basel committee in 1999, and revised in 2006), guidelines Indonesian banking issued by the KNKG (2004) followed by GCG guidelines, and PBI regarding the implementation of GCG in commercial banks. PBI 2006 point of 3. The document that has legally binding force is PBI-2006 because Bank Indonesia is the bank supervisory authority. The guidelines issued by the Basel committee is morally imperative, because Bank Indonesia is one of the central banks that is part of it. The GCG guidelines have non-binding and non-imperative status, but are useful to be used as a voluntary reference because they are more comprehensive.[31]

In carrying out financial intermediation activities, banks face various risks, from credit risk, market risk, operational risk, to legal

[31] Muhammad Sadi Is, *Hukum Perbankan Syariah Dalam Perspektif Dogmatik Hukum, Teori Hukum, Dan Filsafat Hukum* (Indonesia: Setara Press, Malang, 2022).p. 167

risk and reputation risk. Therefore, Islamic banks must be managed very carefully by management who is not only professional but also has high integrity. This is where, among other things, Good Corporate Governance becomes very important and requires special arrangements.[32]

In accordance with the provisions in Article 34 paragraph (3) of Law Number 21 of 2008, provisions regarding the obligation to implement GCG for Sharia Banks and UUS are regulated by Bank Indonesia regulations as stated in Bank Indonesia Regulation Number 11/33/PBI/2009 concerning Good Implementation Corporate Governance for Sharia Commercial Banks and Sharia Business Units. With the enactment of Bank Indonesia Regulation Number 11/33/PBI/2009, Bank Indonesia Regulation Number 8/4/PBI/2006 concerning the Implementation of Good Corporate Governance for Commercial Banks and its provisions for amendments to Bank Indonesia Regulation Number 8/14/PBI/2006 , is declared not applicable to Sharia Commercial Banks.[33]

As a follow-up to Bank Indonesia Regulation Number 11/33/PBI/2009, Bank Indonesia on April 30 2010 issued Bank Indonesia Circular Letter Number 12/13/DPbS regarding the Implementation of Good Corporate Governance for Sharia Commercial Banks and Sharia Business Units. With the issuance of Circular Letter Number 12/13/DPbS dated 30 April 2010, Circular Letter Number 9/12/DPNP dated 30 May 2007 concerning the Implementation of Good Corporate Governance for Commercial Banks is declared not to apply to UUS as long as the matters regulated in Circular Letter Number 12/13/DPbS dated 30 April 2010 and declared not applicable to Sharia Commercial Banks; and Bank Indonesia Circular Letter Number 8/19/DPbS dated 24 August 2006 concerning Guidelines for Sharia Supervision and Procedures for Reporting Supervision Results for the Sharia Supervisory Board are

[32] Muhammad Sadi Is.
[33] Rachmadi Usman, *Aspek Hukum Perbankan Syariah Di Indonesia* (Sinar Grafika, 2022). pp. 248-249.

declared not applicable to Sharia Commercial Banks and UUS.[34]

From the considerations of Bank Indonesia Regulation Number 11/33/PBI/2009, it can be seen that the implementation of good corporate governance for sharia banking is based on three considerations. First, in order to build a healthy and resilient sharia banking industry, it is necessary to implement good corporate governance for Sharia Commercial Banks and UUS. Along with the development of the sharia banking industry, which is marked, among other things, by the increasing diversity of sharia banking products and the increasing network of sharia banking services, good corporate governance in the sharia banking industry is becoming increasingly important to implement. Second, the implementation of good corporate governance in the sharia banking industry must comply with sharia principles (sharia compliance). Incompatibility of bank governance with sharia principles will potentially give rise to various risks, especially reputation risks for the sharia banking industry. Third, the implementation of good corporate governance is an effort to protect the interests of stakeholders and increase compliance with applicable laws and regulations and applicable ethical values. in general in the sharia banking industry.[35]

There is a fundamental difference in the need to apply sharia principles in enforcing GCG in sharia banking compared to conventional banking, because governance issues in sharia banking are very different from conventional banks. First, Islamic banks have an obligation to comply with sharia principles (syariah compliance) in carrying out their business. Therefore, the Sharia Supervisory Board (DPS) plays an important role in the governance structure of sharia banking. Second, because the potential for information asymmetry is very high for Islamic banking, the problem of agency theory becomes very relevant. This is related to the issue of the level of accountability and transparency in the use of customer and shareholder funds. Therefore, the issue of representation of investment account holders in good corporate governance

34 Rachmadi Usman.

35 Rachmadi Usman., p. 251

mechanisms is a strategic issue that must also receive attention from Islamic banks. Third, from a corporate culture perspective, sharia banking should carry out a cultural transformation in which Islamic business ethical values become an inherent character in sharia banking business practices.

Here are four principles of Good Corporate Governance that can be explained as follows:

a. Transparency
   1) Banks should provide data to stakeholders in a timely, comprehensive, clear, accurate, and comparable way that is easily available and follows their rights.
   2) The information that needs to be revealed contains, but is not restricted to, the vision, mission, company goals, and strategy of the corporate, risk management ,financial health, management proportions and compensation, controlling shareholders, textual management, cross-shareholding , internal supervisory and process control, compliance status, GCG systems and application, and significant events that might impact the state of the bank.
   3) Transparency as a medium or tool to achieve success in a financial institution in this banking. However, the principles of openness applied by the bank do not reduce the obligation to always maintain and fulfill the rules of bank confidentiality according to the relevant laws and rules, private rights and job confidentiality.
   4) Bank policies have to be written and then communicated to investors that have the right to get the information regarding the regulation.

b. Accountability
   1) The Bank has to set clear responsible for every organ of the organisation that is in line with the vision, mission, business goals, and strategy of the enterprise.
   2) The bank has to be convinced that all employees of the bank's organisation have the competence to carry out their

responsibilities and understand their duties in the conduct of GCG..

3) As a company that proactively raises money from the general community in the form of deposits and disburses it to the community in the form of credit or another form in order to raise people's standards of living. As a profit-making institution that seeks profits from the investor capital it generates, bank management must of course establish a systematic and structured check and balance system.
4) Banks would have to have performance measurements at all levels of the organization that are based on agreed-upon measures that are aligned within company's values (firm values), business goals, and bank strategies, as well as a rewards and penalty system [36].

c. Responsibility

1) In order to maintain the viability of their business, banks should adhere to the principle of caution (prudent banking practices) and make sure that all relevant laws are abide.
2) The Bank must act as a true enterprise citizen, which includes caring for the environmental and exercising social responsibility.
3) The Bank must avoid unwarranted dominance by any shareholder, be unaffected by one-sided interests, and be free from interest conflicts.
4) Banks must be objective and devoid of any outside pressure (party) while making decisions [37].

d. Fairness

Fairness and justice in realizing the rights of investors based on agreements and extant rules and regulations applicable statutes and regulations[38], as following:

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[36] Arif, "Dampak Good Corporate Governance Terhadap Kinerja Perbankan : Market Risk Sebagai Intervening."

[37] Arif.

[38] M. A. Sifa and C. Fahruddin, "Implementasi Good Corporate Governance Dalam Meningkatkan Kepercayaan Pada Perbankan Syariah," *Journal of Islamic Banking* 2, no. 1 (2021): 55–77.

1) Banks always should pay attention the needs of all parties involved (shareholders) in accordance with the concepts of equality and justice (equal treatment).
2) Banks have to give opportunities for all partners to provide feedback and share ideas that will benefit the bank. They must also provide access to information or data In compliance with the openness concept[39]

In Islamic teachings, these points become important principles in the activities and life of a Muslim. Islam intensely teaches the application of the principles of justice, mas'uliyah (accountability), shiddiq (honesty), tawazun (balance), akhlaq (moral), fathanah (intelligence), amanah (fulfillment of beliefs), tabligh (transparency, openness), hurriyah (independence and responsible freedom), ihsan (professional), wasatan (reasonableness), raqabah (supervision), Ijarah (management), ghirah (sharia militancy), caliphate (leadership), aqidah (faith), ijabiyah (positivity), qira'ah and islah, (firms that are always enhancing and learning). Given what has been said this far, it is obvious that Islam predated GCG, which later emerged as a standard for good corporate governance around the world. These guidelines should make it possible for Islamic financial and economic institutions to be managed professionally and for social, commercial, and economic relations to follow ethical standards.[40]

As an intermediary and trust organisation, in performing its business practices, the bank should uphold the concepts of transparency, have performance evaluation of all levels of the bank in accordance with the firms values, have business goal and strategic plan as a representation of the bank's accountability, adhere to prudent banking practises and ensure the application of applicable policies as a manifestation of the bank's responsibilities, be impartial and independent from any external pressure in decision-making, and

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[39] Sifa and Fahruddin.

[40] Arif, "Dampak Good Corporate Governance Terhadap Kinerja Perbankan : Market Risk Sebagai Intervening."

always think the interests of all shareholders on the basis of the concepts of neutrality and justice (fairness) [41]

He explained that GCG is enforced above the principles of company management. There are many versions of opinions regarding the number of principles of management of that company. However, here is explained an opinion that is easy to follow, namely that GCG is enforced with five key elements, which include transparency, accountability, responsibility, independence, and fairness, which are designed to safeguard the interests of all interested parties (shaherholders). Top management and "*all levels of the organization*" must commit to the regulation and execution of GCG. Its execution begins with the creation of fundamental rules (strategic policy) and moral standards that "*all parties in the firm*" must abide by. The foundation for adopting GCG for Indonesian banks is conformity with the code of ethics, which is only expressed in words and deeds.

The application of the principles of enterprise govenance is a necessity for an agency, including Islamic banks. This is further indicated by the availability of community accountability in relation to the business operations of the bank which is required to adhere to the regulations as outlined in positive laws such as Law No. 40 of 2007 on Limited Companies in Indonesian and Law No. 10 of 1998 on the Amendment of Law No. 7 of 1992 regarding Banking, along with its implementing regulations, and specifically for Islamic banks must comply with Law No. 21 of 2008 about Islamic banking.

Regarding the review of GCG implementation, this management side is focused on the boards of directors. As regulated in the Company Law, the board of directors is required to be an organ of the corporation that is wholly liable for the management of the Company for the benefit and objectives of the PT both inside and out of court. Furthermore, the Company Law regulates the obligation for each group of the board of directors and commissioners in accordance with good intentions and fully responsible for performing their tasks for the interests and the business of the organization. For both of them,

[41] Arif.

they can also be sued in the district court if based on their mistakes and negligence cause losses to the Limited Company (PT). For an amount of the board of directors, there is an additional provision that for such errors or omissions, he/she may be held fully personally liable. Likewise, in the instance of insolvency occurring owing to such errors or omissions, every board of directors membership is liable within the range of liability for the loss in question.

Thus, the execution of GCG concepts is very important to be applied in company operations. Moreover, companies are engaged in the banking sector because in bank operations the bank is required to always implement the prudential principle in providing financial services to the public. This is very possible considering that the bank is an institution that has been regulated in such a complex way (the most regulative industry in the world) bank Indonesia have to be capable to assess and enforce the application of the Bank's GCG.

THE URGENCY OF GCG WITHIN ISLAMIC BANKING IN INDONESIA

In order to prevent misconduct, it is essential to apply Good Corporate Governance (GCG) standards in Indonesian sharia banking. GCG is a notion that governs the corporation and gives it direction in order to create a balance between the firm's power and authority and its duty to its shareholders.[42]

GCG determines the company's ability to safeguard to the interests of shareholders. According to Islamic economists, the interests of stakeholders are not only financial but can reach ethics, religion, and other noble values. Sharia firm governance, which

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[42] Efrizal Syofyan, *Good Corporate Governance (GCG)*. (Malang: Unisma Press, 2021). *See also* Stijn Claessens, "Corporate governance and development." *The World bank research observer* 21, no. 1 (2006): 91-122; Peter Cornelius, "Good corporate practices in poor corporate governance systems: Some evidence from the Global Competitiveness Report." *Corporate Governance: The International Journal of Business in Society* 5, no. 3 (2005): 12-23.

derives from Islamic ethical concepts, encompasses all economic agents in firms, embracing the spiritual and material demands of the Islamic community. Nonetheless, research on sharia governance practices has mainly ignored the significance of Islamic moral economy in essentializing enterprise governance mechanisms [43]. Concerning Islamic financial institutions, stakeholders certainly expect what the company does to meet sharia principles.

Therefore, a company structure that can implement good governance through *sharia*-compliant operational activities is important for the stability and efficiency of Islamic financial services.[44] Since sharia banking is an intermediary organization that needs the confidence of the general public or other stakeholders, implementing the GCG system is extremely crucial. Furthermore, it is highlighted that sharia banks benefit from the application of Good Corporate Governance (GCG), which will enhance their infrastructure, business decision-making quality, accuracy of bank assessments, and early detection of high-risk business sectors, goods, and services.

The existence of stakeholder values is important for Islamic banking (and other Islamic financial institutions), and in average practice, they put them into the formulation of their vision and mission. Grais and Pellegrini studies [45] showed that the characteristics of the mission of Islamic banks focus on two major objectives 1). Compliance with sharia principles, 2). Providing the best service.

Sharia compliance is embodied in three important categories. The first and most widely understood is to maintain the conduct of the financial business so as not to violate the prohibition of usury and *gharar*. The second is efforts to reach Islamic social goals, especially in

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[43] Muhammad Rizky Prima Sakti, Mohammad Ali Tareq, and Hajime Kamiyama, "Corporate Governance from an Islamic Moral Economy Perspective: The Dimensions and Analysis," *Signifikan: Jurnal Ilmu Ekonomi* 10, no. 2 (2021): 359–78, https://doi.org/10.15408/sjie.v10i2.21511.

[44] Mal An Abdullah, *Corporate Governance Perbankan Syariah Di Indonesia* (Jakarta: Ar-Ruzz Media, 2010).

[45] Grais, Wafik, and Matteo Pellegrini. "Corporate governance in institutions offering Islamic financial services: issues and options." *World Bank Policy Research Working Paper* 5046 (2006).

promoting social policies. The third is sincerity to develop an integrated Islamic financial system. As for what is included in the purpose of giving the finest service is a). The service to the community as a Comprehensive, in particular (but not exclusively) the Muslim society *(ummah)* itself: b) advancing the interests of relevant parties, including shareholders, depositors, and employees; and c). development of ethnic and professional qualities on the part of management and staff[46].

Among the most important concepts of sharia are to stay away from usury transactions and prohibited contracts, distribute all profits under the agreement without exploiting the needs of people in need, help borrowers who need funds, and invite them to return to Islam both in the economic and social fields [47].

Implementation of good corporate governance and in accordance with applicable regulations will make investors respond positively to the company's performance and the company's market value. The definition of performance is a description of the achievement of implementing an activity or program or policy in realizing the goals, objectives, mission and vision of the organization. Company performance is influenced by several factors, including whether ownership is concentrated or not, profit manipulation, and financial report disclosure.[48]

When compared with conventional bankers, sharia bankers should be superior and at the forefront in implementing GCG in banking institutions, considering that sharia banking institutions bring the name of religion into business institutions. Strictly speaking, sharia bankers must play their role as pioneers in enforcing GCG in banking institutions. If sharia bankers commit deviations and moral hazards, this not only has implications for the institution but also for the image of sharia. Even though the public knows that it is the fault

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46 Grais.

47 Wahbah Az-Zuhaili, *Fiqih Islam Wa Adillatuhu* (Indonesia: Gema Insani, Jakarta, 2007).

48 Andi Irfan, "Hubungan Antara Penerapan Model Prinsip-Prinsip Good Governance Syari'ah Dengan Kinerja Lembaga Keuangan Syariah," 2014. p. 281

of certain individuals. But people will quickly judge that even sharia institutions carry out moral hazard, let alone conventional institutions.[49]

The implementation of GCG in sharia banking is in order to make sharia banks more sharia because its application in the sharia banking industry must comply with sharia principles. Sharia banking operations must truly be carried out based on sharia principles. On the other hand, the direction of sharia banking development and regulation is to ensure compliance with sharia principles (sharia compliance) in its operations by implementing fatwas that have been issued by the National Sharia Council (DSN) of the Indonesian Ulema Council (MUI).[50]

The implementation of the GCG system in sharia banking is expected to increase added value for all interested parties (stakeholders) through the following objectives:[51]

a. Increasing the efficiency, effectiveness and sustainability of an organization which contributes to the creation of the welfare of shareholders, employees and other stakeholders and is an elegant solution in facing future organizational challenges;
b. Increasing the legitimacy of organizations that are managed in an open, fair and accountable manner;
c. Recognize and protect the rights and obligations of stakeholders;
d. An integrated approach based on democratic principles, legitimate organizational management and participation;
e. Controlling conflicts of interest that may arise between principals and agents;
f. Minimize capital costs by providing positive signals to capital providers. Increasing company value resulting from lower capital

[49] Irfan.

[50] Faozan, "Implementasi Good Corporate Governance Dan Peran Dewan Pengawas Syariah Di Bank Syariah." p. 2

[51] Putri Indar Dewi, "Penerapan Good Corporate Governance (Gcg) Di Lembaga Perbankan Syariah," *Jurnal Ilmiah Al-Tsarwah; Vol 3, No 2 (2020)DO - 10.30863/Al-Tsarwah.V3i2.1150* , December 30, 2020, https://jurnal.iain-bone.ac.id/index.php/altsarwah/article/view/1150.

costs, improving financial performance and better perceptions from stakeholders regarding future company performance.

Thus, through the above objectives, it is hoped that the implementation of GCG in sharia banks will increase public trust in sharia banks, the growth of the Islamic financial services industry and the stability of the financial system as a whole will always be maintained, and the success of the Islamic financial services industry in implementing GCG will put Islamic financial institutions in a better position. in line with other international financial institutions. A number of basic tools required for the establishment of GCG in Islamic banks include: internal control system, risk management, bank transparency, accounting system, sharia purification and audit, and external audit.

GCG' ADOPTION IN INDONESIAN SHARIA BANK LAW

A. Bank Indonesia Regulation Number: 11/33/PBI/2009 on Good Governance for Sharia Commercial Banks and Sharia Business Units

In this regard, GCG in sharia commercial banks and sharia business units are governed by Bank Indonesia Regulation Number: 11/33/PBI/2009 on Good Governance for Sharia Commercial Banks and Sharia Business Units, which states that Good Corporate Governance is bank governance that adheres to the concepts of transparency, accountability, professionalism, and fairness.

In the public description chapter of PBI Number: 11/33/PBI/2009, it is stated that first. In addition to being transparent in the decision-making system, transparency is also defined as being openness in the provision of information and relevance. Second, accountability, namely the clarification of the functions and responsibilities of bank organs in order to ensure effective management. Third, accountability refers to bank management's compliance within relevant laws and regulations, as well as the concepts of sound bank management. Fourth, Professionals are people who are competent, operate honestly and objectively, and are unaffected by outside pressure (independent) and possess a great dedication to support the development of Islamic finance. Fifth, Justice is fairness and equal fulfilment of shareholders' rights arising from contracts and prevailing laws and policies (Muhaimin, 2022). Therefore, these values are aligned with the Islamic concept on banking management, as it follows the four qualities of the Prophet Muhammad S.A.W, are *shiddiq*, *tabligh*, *amanah* (communicate), and *fathanah* (intelligent).

In regulation of Article 2 paragraph (1) of Bank Indonesia Regulations No: 11/33/PBI/2009 pertaining the application of GCG for Sharia Commercial Banks and Sharia Business Units, it is mentioned that the bank is obliged to comply with the concepts The implementation of guiding principles by banks is divided into two groups, namely Sharia Commercial Banks and Sharia business units in the application of GCG for BUS which at least should be embodied in [52]

1) Execution of the board of commissioners and directors' tasks and responsibilities;
2) Complete and put into practice the committee and labor unit responsibilities for Sharia Commercial Banks' internal control;
3) Implementation of duties and responsibilities in supervision;
4) Implementing compliance functions for internal and external audits;
5) On the maximum disbursement of funds; and
6) Financial and non-financial circumstances on buses are transparent.

Furthermore, the implementation of GCG for Sharia core business have to be at least be realized in:[53]

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[52] Wahbah Az-Zuhaili, *Fiqih Islam Wa Adillatuhu*.

[53] Wahbah Az-Zuhaili.

1) Performing the duties and responsibility of the Sharia Business Unit (SBU) director.
2) Application of tasks and responsibilities of the Sharia supervisory board.
3) Disbursement of funds to key financing clients and deposit of money by key depositors as well as transparent financial and non-financial condition of UUS.

B. Opportunities on Implement Good Corporate Governance Principles in Sharia Banking

To prove how GCG is implemented in sharia banking, the results of research conducted by Sri Endah Wahyuningsih with the title Analysis of GCG Implementation in Sharia Commercial Banks will be shown as follows:

Bank Muamalat is run through devotion and obedience to Allah SWT. This spirit is the basis for business management, activities and business at Bank Muamalat. With high commitment, Bank Muamalat strives to always be consistent in implementing and improving GCG implementation. Like Muamalat Spirit which is an inseparable part of the implementation of GCG, the transformation steps carried out by Bank Management since 2009 are an effort to further spur the implementation of better corporate governance at Bank Muamalat, in addition to continuing to develop a culture of compliance and increasing awareness of the risks involved. faced.

Bank Muamalat has carried out the obligation to carry out and submit GCG reports to Bank Indonesia on an ongoing basis with increasingly better implementation. This is a manifestation of Bank Muamalat's commitment to implementing Bank Indonesia Regulation (PBI) No.11/33/PBI/2009 dated 7 December 2009 and BI Circular Letter (SE) No.12/13/DPbS dated 30 April 2010 concerning Implementation of Good Corporate Governance for Sharia Commercial Banks (BUS) and Sharia Business Units (UUS), especially Article 62 and Article 63 regarding the Bank's obligation to submit a GCG Implementation Report to Bank Indonesia (BI) and other stakeholders. In implementing GCG, Bank Muamalat is not only guided by the rules and regulations governing the implementation of GCG as mentioned above, but is also guided by internal provisions and other applicable laws and regulations.

In addition, the implementation of Good Corporate Governance in BNI and BRI Sharia and its disclosures, it can be seen that BRI Syariah has implemented a "GOOD" GCG, although there are several items or disclosure indicators that are not included in the Good Corporate Governance report. Based on the outcomes of Good Corporate Governance execution and disclosure, particularly in the two Sharia Commercial Banks, BRI Syariah, BNI Syariah, and Good Corporate Governance application in the future must run more successfully and, of course, have a high GCG score or rating. To meet these expectations, companies in Indonesia are required to:

1. Professional management of the company and no affiliation between the owners, supervisors and directors of the company and the board of commissioners.
2. Create of a symmetrical relationship so that minority shareholders can participate in the company's decision making.
3. Provide legal protection for minority shareholders.
4. Increase the score/rating of openness.[54]

In addition, the implementation of GCG in Indonesia sharia bank based on the Indonesia Sharia Bank 2021 Annual Report, GCG has been implemented by the management of Indonesia Shariah Bank (BSI) with the "Good" category in general. It can be shown in the 11 indicators' proper implementation of good corporate governance. Although there are certain flaws in the way GCG is being implemented, they are not serious issues and can be fixed with the usual bank management remedies (PT. Bank Syariah Indonesia TBK, n.d.) This application reveals the positive trends in implementing GCG principles within Shariah Bank in Indonesia that may become best practice that can be replicated in any Shariah bank in all of Indonesia areas.

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[54] Resti Ardhanareswari, "Pelaksanaan dan pengungkapan good corporate governance pada bank umum syariah." *Law and Justice* 2, no.1 (2017): 66-78.

GCG determines the company's ability to safeguard to the interests of shareholders. According to Islamic economists, the interests of stakeholders are not only financial but can reach ethics, religion, and other noble values. Sharia firm governance, which derives from Islamic ethical concepts, encompasses all economic agents in firms, embracing the spiritual and material demands of the Islamic community. Nonetheless, research on Sharia governance practices has mainly ignored the significance of the Islamic moral economy in essentializing enterprise governance mechanisms. [55] Concerning Islamic financial institutions, stakeholders certainly expect what the company does to meet Sharia principles.

Therefore, a company structure that can implement good governance through Sharia-compliant operational activities is important for the stability and efficiency of Islamic financial services (Mal an Abdullah, 2010). Since Sharia banking is an intermediary organization that needs the confidence of the general public or other stakeholders, implementing the GCG system is extremely crucial. As well as, a study shows that, due to the recent and rapid growth of sharia banking, Good Corporate Governance (GCG) practices must be implemented immediately in banking management to ensure the maximum level of protection for all parties interested in the stakeholders, particularly consumers and depositors.[56]

The existence of stakeholder values is important for Islamic banking (and other Islamic financial institutions), and in average practice, they put them into the formulation of their vision and mission. Grais and Pellegrini studies showed that the characteristics of the mission of Islamic banks focus on two major objectives 1). Compliance with sharia principles, 2). Providing the best service. Sharia compliance is embodied in three important categories. The first and most widely understood is to maintain the conduct of the

[55] Sutan Emir Hidayat, Muhammad Rizky Prima Sakti, and Raqiya Ali Abdullah Al-Balushi. "Risk, efficiency and financial performance in the GCC banking industry: Islamic versus conventional banks." *Journal of Islamic Accounting and Business Research* 12, no. 4 (2021): 564-592.

[56] Suryani et al., "Good Corporate Governance (Gcg) Principle in Sharia Banking: An Islamic Law Perspective,"

financial business so as not to violate the prohibition of usury and *gharar*. The second is efforts to reach Islamic social goals, especially in promoting social policies. The third is sincerity to develop an integrated Islamic financial system. As for what is included in the purpose of giving the finest service is a). The service to the community as a Comprehensive, in particular (but not exclusively) the Muslim society (ummah) itself: b) advancing the interests of relevant parties, including shareholders, depositors, and employees; and c). development of ethnic and professional qualities on the part of management and staff.[57]

Among the most important concepts among the concepts of sharia are to stay away from usury transactions and prohibited contracts, distribute all profits under the agreement without exploiting the needs of people in need, help borrowers who need funds, and invite them to return to Islam both in the economic and social fields.[58]

As an intermediary and trust organization, in performing its business practices, the bank should uphold the concepts of transparency, have performance evaluation of all levels of the bank in accordance with the firms values, have business goal and strategic plan as a representation of the bank's accountability, adhere to prudent banking practices and ensure the application of applicable policies as a manifestation of the bank's responsibilities, be impartial and independent from any external pressure in decision-making, and always think the interests of all shareholders on the basis of the concepts of neutrality and justice (fairness).[59]

Furthermore, it is emphasized that Good Corporate Governance (GCC) supersedes the principles of company management. While there exist diverse perspectives on the number of

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[57] Wafik Grais, and Matteo Pellegrini. "Corporate governance in institutions offering Islamic financial services: issues and options." *World Bank Policy Research Working Paper* 5046 (2006).

[58] Wahbah Az-Zuhaili. *Fiqh al-islam wa adillatuhu*. (Damaskus: Dar al-fikr, 2007).

[59] Muhammad Al Arif, et al. "The Islamic banking spin-off: Lessons from Indonesian Islamic banking experiences." *Journal of King Abdulaziz University: Islamic Economics* 30, no. 2 (2017).

principles governing company management, a simplified interpretation is presented here. GCG is asserted to be governed by five fundamental elements—transparency, accountability, responsibility, independence, and fairness. These elements are meticulously designed to protect the interests of all stakeholders, particularly shareholders. The commitment to GCG extends across top management and permeates "*all levels of the organization*." Its effective implementation commences with the establishment of foundational rules (strategic policy) and moral standards that every participant within the firm must adhere to. For Indonesian banks, the adoption of GCG is anchored in compliance with a code of ethics, a commitment that should be reflected both in words and actions. Emphasizing transparency, accountability, responsibility, and fairness, these GCG principles hold significant relevance in the activities and life of a Muslim.

Islam intensely teaches the application of the principles of justice, mas'uliyah (accountability), *shiddiq* (honesty), *tawazun* (balance), *akhlaq* (moral), *fathanah* (intelligence), *amanah* (fulfillment of beliefs), *tabligh* (transparency, openness), *hurriyah* (independence and responsible freedom), *ihsan* (professional), wasatan (reasonableness), *raqabah* (supervision), *Ijarah* (management), *ghirah* (sharia militancy), caliphate (leadership), aqidah (faith), ijabiyah (positivity), qira'ah and islah, (firms that are always enhancing and learning). Given what has been said thus far, it is obvious that Islam predated GCG, which later emerged as a standard for good corporate governance around the world. These guidelines should make it possible for Islamic financial and economic institutions to be managed professionally and for social, commercial, and economic relations to follow ethical standards.[60]

The application of the principles of enterprise governance is a necessity for an agency, including Islamic banks. This is further indicated by the availability of community accountability in relation

[60] Muhamad Arifin. "The Influence of Islamic Law and Economic Principles on Banking Industry in Indonesia." *Journal of Legal, Ethical and Regulatory Issues* 24 (2021): 1-11.

to the business operations of the bank which is required to adhere to the regulations as outlined in positive laws such as Law No. 40 of 2007 on Limited Companies or "Perseroan Terbatas" in Indonesian and Law No. 10 of 1998 on to the Amendment of Law No. 7 of 1992 regarding Banking, along with its implementing regulations, and specifically for Islamic banks must comply with Law No. 21 of 2008 about Islamic banking.

Juridically, Islamic banks are responsible to many parties (stakeholders), namely depositor customers, shareholders, bond investors, correspondent banks, regulators, company employees, suppliers, the society and the environmental so the application of GCG is a requirement for all Islamic banks. The realization of GCG is a way for Islamic banks to be accountable to the general public that an Islamic bank is being well managed, professional, and prudent while still attempting to enhance its stakeholders' value without neglecting other stakeholders.

Regarding the review of GCG implementation, this management side is focused on the boards of directors. As regulated in the Company Law, the board of directors is required to be an organ of the corporation that is wholly liable for the management of the Company for the benefit and objectives of the PT both inside and out of court. Furthermore, the Company Law regulates the obligation for each group of the board of directors and commissioners in accordance with good intention and fully responsible for performing their tasks for the interests and the business of the organization. For both of them, they can also be sued in the district court if based on their mistakes and negligence cause losses to the Limited Company (PT). For an amount of the board of directors, there is an additional provision that for such errors or omissions, he/she may be held fully personally liable. Likewise, in the instance of insolvency occurring owing to such errors or omissions, every board of director membership is liable within the range of liability for the loss in question.

Hence, the implementation of Good Corporate Governance (GCG) concepts is of utmost significance in company operations, particularly for entities operating in the banking sector. In banking operations, the adherence to the prudential principle is imperative, given the inherent responsibility of banks to consistently uphold this principle while providing financial services to the public. The complexity of regulations governing the banking industry, making it one of the most regulated sectors globally, underscores the necessity for Bank Indonesia to effectively evaluate and enforce the application of GCG within the banking institution.

CONCLUSION

Finally, this study concluded and highlighted that the application of Good Corporate Governance (GCG) principles in Sharia aligns seamlessly with the established GCG framework, encompassing key elements such as accountability, transparency, independence, responsibility, and fairness. Rooted in the principles exemplified by the Prophet Muhammad SAW, namely *shiddiq*, *tabligh*, *amanah*, and *fathanah*, these GCG elements are designed to protect the interests of all shareholders. Moreover, the convergence of GCG concepts with Islamic economic principles, including *al-a'dl* (justice), *tawazun* (balance), *mas'uliyah* (accountability), *akhlaq* (morality), *shiddiq* (honesty), *amanah* (fulfillment of beliefs), and *fatanah* (intelligence), underscores their relevance in the Islamic financial landscape. Furthermore, the concept of *hurriyah* (independence and conscientious freedom) within GCG reflects the belief that humans are creations of God endowed with responsible freedom. For Islamic banking, ensuring freedom from undue dominance, preemptive interests, conflicts of interest, external pressures, and embracing principles such as *Ikhsan* (professionalism), *Wasathan* (reasonability), *Ghirah* (spirit), *Idarah* (management), and *Khalifah* (Leadership) is essential. This holistic approach emphasizes the need for Islamic banking to operate independently, purposefully, and ethically, guided by a commitment to professionalism, reasonability, spiritedness, effective management, and principled leadership.

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