Analysis of the Effect of Sharia Compliance and Islamic Corporate Governance on Fraud in Islamic Banks in Indonesia 2017-2019

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ABSTRACT
This study aims to analyze the factors that influence the occurrence of fraud in Islamic banks in Indonesia. Measurement of fraud in Islamic banks is based on the number of internal frauds that occur in the financial year. The population in this study is Islamic banks in Indonesia for the period 2017-2019. The sample is selected using purposive sampling method and the number of samples obtained is 24 samples. The data used in this study are secondary data in the form of financial reports and corporate governance reports. Data analysis is performed using classical assumption tests and regression analysis. The results of this study indicate that Islamic corporate governance has a significant effect on internal fraud in Islamic banks in Indonesia. Meanwhile, partially the profit sharing ratio and Islamic investment ratio do not have a significant effect on internal fraud in Islamic banks in Indonesia. Islamic banking must comply with accounting standards and Auditing Organizations for Islamic Financial Institutions (AAOIFI) to minimize fraud in operations.

Keyword: Sharia Compliance, Islamic Corporate Governance, Islamic Banking, and Fraud

1. INTRODUCTION
At this time Sharia banking continues to develop. Developments occur not only in the number of Sharia Commercial Banks and Sharia Business Units but also in the total assets of sharia banking from year to year as shown by the following data (Figure 1).

The development of Islamic banking can be seen not only from the number of banks, the number of assets, or the number of offices in Indonesia but also from the awards or achievements obtained, such as in the 2019 Global Islamic Finance Report (GIFR). The National Committee for Sharia Finance (KNKS) states that GIFR is an annual report on Islamic banking and finance that issued in 2010, it is measured using the Islamic Financial Country Index (IFCI). At last year’s IFCI, Indonesia earned 81.93 points so that it was ranked first after consistently getting only 15-25 points since the initial IFCI assessment. This significant development is a manifestation of the 2017-2019 Islamic finance development roadmap (OJK, 2017).

The financial and banking industries are the industries most affected by fraud (ACFE Indonesia Chapter, 2019). In Islamic banks, there were several cases of fraud that harmed the bank, such as in the fictitious credit case that occurred at Bank BJB Syariah in 2018. This case involved the BJB Managing Director at the time, namely
Figure 1. The Development of the Number of Banks, the Number of Assets, and the Number of Offices in Indonesia 2016 - April 2020

Source: Islamic Banking Statistics, Financial Services Authority of the Republic of Indonesia (OJK), April 2020

Yocie Gusman. Islamic banks are banks that implement Islamic corporate governance (ICG). Where in its application there are principles of Good Corporate Governance (GCG) and sharia compliance. However, this cannot guarantee that Islamic banks will be free from fraud. Therefore, this research is needed to analyze the effect of sharia compliance and ICG on fraud in Islamic banks in Indonesia in 2017-2019, so it is hoped that this research can contribute indirectly to reducing fraud in Islamic banking.

Research on the factors that influence the occurrence of fraud in Islamic banking in Indonesia has been conducted by several researchers. In this research, sharia compliance is represented by Profit Sharing Ratio (PSR) and Islamic Investment Ratio (IIR) which are included in the Islamicity Disclosure Index developed by Hameed et al (2004). Research conducted by Muhammad et al (2019) using the Islamic Investment Ratio as a proxy for sharia compliance concludes that the Islamic Investment Ratio has a significant negative effect on fraud that occurs in Islamic banks. This contrasts with research conducted by Raharjanti and Muharrami (2020) and Haifa Najib and Rini (2016) that Islamic Investment Ratio does not have a significant effect on fraud in Islamic banking.

Based on the description above, it can be seen that the results of some of the studies are still mixed. Therefore, this study is conducted to review the factors that influence fraud in Islamic banking.
The difference from previous research is that the variables chosen are a comparison of the results of previous studies that have an effect and do not have an effect on the occurrence of fraud in Islamic banks. In addition, the sample period used in this study is also different from previous studies, from 2017 to 2019.

2. LITERATURE REVIEW AND HYPOTHESIS

Fraud
Fraud is an act that is deliberately committed to cheat or manipulate stakeholders both bank and customer, which occurs within the bank, like using bank facilities so as to cause the stakeholders to suffer losses and the perpetrator of fraud obtains financial benefits, either directly or indirectly (Bank Indonesia, 2011). According to Irianto & Novianti (2019), fraud has very serious implications that go beyond calculations from the financial aspect, because it involves moral and integrity issues in the midst of social life, national life and state.

Basically, every action that is taken has a basis for a specific reason, including fraud. In this case, these reasons are generally used as a defense for fraud. This phenomenon attracts the attention of researchers to reveal the reasons for someone to commit fraud, which then gives birth to various theories. Based on the Fraud Pentagon Theory developed by Marks (2012), there are five factors that cause a person to carry out fraud: arrogance, competence, opportunity, pressure, and rationalization.

The Association of Certified Fraud Examiners (ACFE) classifies fraud into three: asset misappropriation, corruption, and fraudulent financial report. Based on the results of a survey conducted by ACFE Indonesia Chapter (2019), the most prevalent fraud in Indonesia is corruption with a percentage of 64.4%, the second position is occupied by asset misappropriation with a percentage of 28.9%, and the last one is financial statement manipulation. Based on the data above, this study focuses on occupational fraud, or commonly referred to as internal fraud.

Sharia Compliance
Shariah compliance is a form of preventive action to ensure that all policies,
procedures, and operational activities carried out by banks are in accordance with bank Indonesia regulations, laws, and sharia principles (Bank Indonesia, 2012). These sharia principles are one of the distinguishing factors between Islamic banks and conventional banks. Therefore, Islamic banks are expected to always operate in accordance with sharia principles. One of the very hot legal issues in the sharia economy is sharia compliance of Islamic financial institutions. Sharia compliance is very important in the operation of sharia contracts because it determines whether a practice in Islamic financial services is in accordance with sharia principles (Manan, 2019). In this study, sharia compliance is represented by the Profit Sharing Ratio (PSR) and the Islamic Investment Ratio (IIR) which are included in the Islamicity Disclosure Index developed by Hameed et al. (2004).

**Profit Sharing Ratio (PSR)**
According to Hameed et al. (2004), the main objective in Islamic banking is to avoid interest by using a profit sharing system. This ratio is used to determine the extent to which Islamic banks achieve these goals.

**Islamic Investment Ratio (IIR)**
Hameed et al. (2004) explain that Islamic principles prohibit transactions involving usury, gharar, and gambling. Simultaneously, Islamic principles encourage halal trade. Thus, Islamic banks need to disclose honestly any investment that is considered halal and haram.

**Islamic Corporate Governance (ICG)**
According to Abdullah (2010), the implementation of effective corporate governance is needed to protect the rights of all stakeholders to uphold fairness, honesty, and protection of human needs in accordance with *maqashid* sharia. In the context of Islamic banking, the interests of stakeholders, other than financial, are sharia compliance where banks are expected to always operate in accordance with sharia principles. Therefore, Law no. 21 of 2008, concerning Islamic Banking, requires Islamic banks and sharia business units to establish a Sharia Supervisory Board (Indonesia: Dewan Pengawas Shariah / DPS). To fully fulfill the interests of stakeholders, Islamic banks must integrate the implementation of modern GCG principles into the framework of Islamic banking.

**FRAMEWORK AND HYPOTHESIS FORMULATION**

The Effect of Profit Sharing Ratio on Fraud
Based on research conducted by Fadhistri & Triyanto (2019) and Najib & Rini (2016), PSR has a negative effect on the occurrence of fraud. Other results are shown by research conducted by Muhammad, et al., (2019) that PSR has a positive effect on fraud. This indicates that the higher the profit sharing ratio, the higher the fraud that occurs. Mudharabah contracts have a high risk, which can lead to asymmetric information. Asymmetric information can lead to fraud in its implementation. This is in line with the results of research conducted by Muhammad, et al., (2019). Based on the description above, the first hypothesis can be formulated as follows:

\[ H_1: \text{Profit Sharing Ratio has a positive effect on fraud.} \]

The Effect of Islamic Investment Ratio (IIR) on Fraud
The results of research conducted by Muhammad, et al., (2019) show that Islamic investment ratio (IIR) has a negative effect on fraud. This indicates that the higher the Islamic investment ratio, the less the possibility of fraud in Islamic banks. High Islamic investment ratios are the result of transparent management by management. Based on the description above, the second hypothesis can be formulated as follows:

\[ H_2: \text{Islamic Investment Ratio has a negative effect on fraud.} \]
The Effect of Islamic Corporate Governance (ICG) on Fraud
The results of studies conducted by Raharjanti & Muharrami (2020), and Fadhistri & Triyanto (2019), show that Islamic corporate governance (ICG) has a positive effect on fraud. This indicates that the lower the ICG self-assessment score, the less the possibility of fraud in Islamic banks. It should be noted, however, that the smaller the self-assessment score, the better the ICG's performance is. The implementation of ICG, consisting of the principles of accountability, transparency, accountability, independence, fairness, and sharia compliance, will help prevent fraud. Based on the theory and results of previous research explained above, the third hypothesis can be formulated as follows:

\[ H_3: \text{Islamic Corporate Governance has a positive effect on fraud} \]

3. METHODS
This study uses the causal method because there is a causal relationship between the dependent variable and the independent variables. The population in this study Islamic Commercial Banks in Indonesia for the period 2017-2019. This study uses purposive sampling technique to determine the sample based on certain considerations. The sample used in this study is Islamic Commercial Banks that were registered with the Financial Services Authority of the Republic of Indonesia (OJK) for the period 2017-2019 and published a complete annual financial report and GCG implementation report for the period 2017-2019. The data used in this study is secondary data in the form of GCG report listed in the Islamic Commercial Banks' annual report obtained through the respective Islamic Commercial Banks website. The data analysis technique used in this study is the classical assumption test and multiple-linear regression test using SPSS version 24.

Measurement and Operational Definition of Variables Dependent Variable (Y)
The dependent variable in this study is fraud. Fraud in this research is measured using the number of occurrences of internal fraud in Islamic banks in the GCG implementation report of each Islamic bank. The number of internal frauds is used because this research is limited to the occupational fraud or internal fraud only.

Variabel Independen (X)
The independent variables in this study are sharia compliance and Islamic corporate governance (ICG). Sharia compliance in this study is proxied by the profit sharing ratio and the Islamic investment ratio developed by Hameed et al. (2004).

Profit Sharing Ratio (PSR)
Profit sharing ratio (PSR) is a measurement ratio that describes the ratio between the amount of mudharabah and musyarakah financing and the total financing.
The formula for the PSR is as follows:
\[
\text{PSR} = \frac{\text{Mudharabah} + \text{Musyarakah}}{\text{Total Financing}}
\]

**Islamic Investment Ratio (IIR)**

Islamic Investment Ratio (IIR) is the ratio of halal income to total income, both halal and non-halal.

The formula for the IIR is as follows:
\[
\text{IIR} = \frac{\text{Halal Investment}}{\text{Halal and Non-Halal Investment}}
\]

Islamic Corporate Governance (ICG) in this study is measured using the composite value of the self-assessment results of Islamic bank GCG which is disclosed in the report on the implementation of Islamic bank GCG.

**4. RESULT AND DISCUSSION**

The results of the analysis in this study are obtained by conducting several tests, such as the classical assumption test (normality test, multicollinearity test, heteroscedasticity test, and autocorrelation test), and hypothesis test (the coefficient of determination \( R^2 \) test, simultaneous \( F \) test, and partial \( t \) test).

**Classical Assumption Test Normality Test**

![Normality Test Results](Image)

Source: Data Processed by the Author

The results of the normality test using the Kolmogorov-Smirnov parametric test method can be seen in Figure 4 above. The normality test results show the value of asymp. sig. (2tailed) is 0.2 > 0.05. This means that standardized residual data are normally distributed.

**Multicollinearity Test Results**

![Multicollinearity Test Results](Image)

Source: Data Processed by the Author
Multicollinearity Test
The test results in Figure 5, above show that the tolerance values of PSR, IIR, and ICG variables are respectively 0.979; 0.976; and 0.992. Meanwhile, the VIF value of PSR, IIR, and ICG variables are respectively 1.022; 1.025; and 1.008. By looking at the test results of the three variables, none of which indicates that the VIF value is greater than 10 and the resulting tolerance value is also more than 0.10, so it can be concluded that the data tested did not detect multicollinearity symptoms.

Heteroscedasticity Test
Heteroscedasticity in this study is tested using the Glejser method. The results show that the IIR variable has a significant value for the absolute residual value of 1.000 > 0.05, the PSR variable for the absolute residual value is 1.000 > 0.05, while the ICG variable for the absolute residual value is 1.000 > 0.05. This indicates that there is no systematic relationship between explaining variables and the absolute residual value. So it can be concluded that the data obtained does not contain heteroscedasticity.

Autocorrelation Test
Based on the test results of the autocorrelation test in Figure 7 above, the Durbin-Watson value is 1.613, which means that the dw value is between the dL value ≤ d ≤ dU, which is 1.1010 ≤ 1.613 ≤ 1.6565, so there is no positive autocorrelation, or it can be interpreted that there is no relationship between one data with another data.

Hypothesis Test Coefficient of Determination (R²) Test
Based on the test results the coefficient of determination (R²), the value of R or multiple R is 0.585, which means that the multiple correlation between IIR, PSR, and ICG is 0.585. Meanwhile, the value of the coefficient of determination (R²) is 0.343, which means that the IIR, PSR, and ICG variables have an effect on fraud by 34.3%, while the remaining 65.7% is influenced by other factors that have not been examined by...
researcher. The adjusted R² value is 0.244, which means that the variation in IIR, PSR, and ICG has an effect on fraud by 24.4%. In addition, the value of std. error of the estimate is 8.0355061, which means that the deviation between the regression equation and the real dependent value is 8.0355061 units of the dependent variable.

Simultaneous F Test
Based on the results of the simultaneous F test in Figure 9 above, the F significance value is 0.035 < 0.05, so it can be concluded that PSR, IIR, and ICG simultaneously have an effect on fraud.

Partial t test
The partial t test in this study uses a significance level of 0.05. The t test is used to test the effect of the independent variable on the dependent variable partially. The first hypothesis states that PSR as a proxy for sharia compliance has an effect on fraud in Islamic banks. The results of the regression analysis show that the PSR variable has a significance value of 0.968 which is greater than 0.05. Based on the results above, it can be concluded that sharia compliance proxied by PSR has no effect on fraud, so that the first hypothesis is rejected. Based on the results of an interview with the manager of the financing department at one of the Sharia Banks, Emeraldo (2019), Islamic Bank financing products help the existence of a Profit Sharing Ratio in the operation of Islamic banking products, even though in the application of these products in Indonesia there are more mudarib who apply for financing with a murabahah contract than mudharabah and musyarakah.

Mudharabah contract products are still slightly applied because of the lack of trust between shahibulmaal and mudarib, and vice versa. There are still mudarib who cannot be transparent in reporting the financial statements of their business results and profit sharing received from the business they run, even though Islamic banks have given full confidence to mudarib by providing business capital in accordance with what is needed by the mudarib to help and expand their business in obtaining maximum profits. Especially in the current situation and conditions of Figure 8.

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Figure 8. Coefficient of Determination (R²) Test Results

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.585^a</td>
<td>.343</td>
<td>.244</td>
<td>8.0355061</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), ICG, IIR, PSR

Source: Data Processed by the Author

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Figure 9. Simultaneous F Test Results

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>673,571</td>
<td>3</td>
<td>224,524</td>
<td>3.477</td>
<td>.035b</td>
</tr>
<tr>
<td>Residual</td>
<td>1291,387</td>
<td>20</td>
<td>64,569</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1964,958</td>
<td>23</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: Fraud
b. Predictors: (Constant), ICG, IIR, PSR

Source: Data Processed by the Author
Covid-19 pandemic, many businesses have decreased due to a decrease in business operational activities and restrictions on carrying out activities to minimize the spread of Covid-19. This results in a decrease in the profit sharing obtained by Islamic Banks. Covid19 pandemic has an impact not only on economic conditions, but also on Islamic banking activities. Thus, it will affect PSR so that Islamic Corporate Governance (ICG) must be able to make a positive contribution to the situation at hand.

The second hypothesis states that IIR as a proxy for sharia compliance has a significant effect on fraud in Islamic banks. The results of the regression analysis show that the IIR variable has a significance value of 0.605. Therefore, it can be concluded that the sharia compliance proxied by IIR has no effect on fraud, so the second hypothesis is rejected. Although the average IIR value is close to one hundred percent, which means that investment has been dominated by investments that comply with sharia principles, there are still frauds in Islamic banks. So, Islamic investments owned by Islamic banks have no effect on fraud. Based on the calculations that have been done, of the two proxies used to assess sharia compliance, there is not one that has an effect on fraud. In addition, the non-effect is caused by the limited data used in this study.

The third hypothesis states that ICG has an effect on fraud in Islamic banks. This means that even though the financing and investment activities of Islamic banks have been carried out or dominated by sharia activities and in accordance with Shari a standards of Bank Indonesia Regulations, there is still fraud that occurs. So, financing and investment activities that are in accordance with sharia principles have an influence on cases of fraud that occur. The results of the regression analysis show that the ICG variable has a significance value and a coefficient value of 0.004 and 0.582, which indicates that the ICG variable has a positive effect on fraud. This indicates that the smaller (better) the results of self-assessment of bank governance, the lower the number of frauds in Islamic banks.

5. CONCLUSION

The results of t test analysis (partial) in this study show that the profit sharing ratio and the Islamic investment ratio have no effect on fraud at Islamic Commercial Banks that meet the sample criteria, which means that sharia compliance, which is proxied by the profit sharing ratio and the Islamic investment ratio, does not have a significant effect on fraud. Meanwhile, Islamic corporate governance has a positive effect on fraud. The results of this study strengthen the results of research conducted by Raharjanti and Muharrani (2020) where PSR has no positive effect on fraud, IIR has not significant effect on fraud, and ICG has a positive effect on fraud.
The results of this study indicate that simultaneously sharia compliance and Islamic corporate governance have a significant influence on fraud. Partially, sharia compliance, which is proxied by the profit sharing ratio and the Islamic investment ratio, does not have a significant effect on fraud, while the Islamic corporate governance variable has a significant effect on fraud that occurs in Islamic Banks.

The implication of this research is that the stability of Islamic corporate governance and sharia compliance must be maintained by Islamic Commercial Banks because the stability of Islamic corporate governance can minimize the occurrence of fraud in financial reporting and activities in Islamic Banks. By maintaining the stability of Islamic corporate governance, it will increase the understanding of perspectives in the operational activities of Islamic banks. Furthermore, it will have an effect on effective and efficient performance and reduce the occurrence of fraud. However, the role of sharia compliance is also very important in the operations of Islamic Banks. Even though the results are not significant, sharia compliance still has an influence in minimizing fraud that occurs in Islamic Banks. Thus, every Islamic Bank is expected to be able to execute the principles of Islamic Good Corporate Governance (GCG) in the form of transparency, accountability, responsibility, independence, fairness and sharia compliance.

Based on the results of the research analysis, it is necessary to have an understanding of literacy related to sharia compliance and Islamic corporate governance for all Sharia Bank Board of Directors, Sharia Supervisory Board, financial managers, and those involved in Islamic Bank financial reporting. The transparency of financial statements is one of the important factors that can influence decision making to determine the success or failure of the Islamic Bank operations. Thus, training on literacy related to Islamic corporate governance is needed to prevent fraud in Islamic Banks. By understanding Islamic values in the operational activities of the company, accounting standards, and Auditing Organizations for Islamic Financial Institutions (AAOIFI) and participating in training related to the dangers of fraud, a person will get the knowledge that the audit carried out must be accountable not only to the interests of the company and stakeholders but also to Allah SWT in the hereafter.

It is expected that further research expand the observation period and add or use other variables that may affect the large number of frauds in Islamic Banks. Due to the difficulty of detecting fraud through financial reports, further research may consider the use of non-financial proxies from sharia compliance.

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