

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

This chapter reviews the previous studies on governance practice and performance of firms, specifically in Islamic banks, to identify the gaps in the existing literature on Shariah governance. This chapter synthesizes the Shariah governance mechanisms and Maqasid Shariah and the mediator's function to indicate the impact on the Islamic banks' performance. The review in this chapter has led to providing the guidelines regarding the theoretical standpoint, research design, and research hypotheses.

This chapter is divided as follows:

Section 2.2 discusses the corporate governance overview that defines corporate governance and its roles in an organization.

Section 2.3 discusses Shariah governance practices by IFIs in Malaysian, in terms of the guidelines, rules, and regulations of Shariah governance in Malaysian IFIs. This section contains three sub-sections, which are 2.3.1 Shariah governance practice in Malaysian IFIs—highlighting the regulation, framework, and guidelines, such as the Shariah governance framework by the BNM, Islamic financial service Act 2013, and IFSB guidelines. Subsection 2.3.2 is on Shariah governance and performance of Islamic banks, and subsection 2.3.3 summarises the Shariah governance literature. Section 2.4 is on Maqasid Shariah overview, which discusses the Maqasid Shariah and Islamic

banks' performance and also the integration between CSR elements and Maqasid Shariah.

Section 2.5 discusses the Board of Directors and performance of Islamic banks, while 2.6 discusses prior studies on the financial performance and measurements. Section 2.7 summarises the gap. Section 2.8 contains the underpinning theories, namely, the Intellectual Capital model related to the current study, and the supported theory of the theoretical framework. The present study identified four theoretical frameworks: The stewardship theory, stakeholders' theory, and legitimacy theory. Section 2.9 presents the hypotheses of study, while section 2.10 presents the research framework based on the literatures and theories. Section 2.11 summarises this chapter.

2.2 Corporate Governance Overview

Corporate governance is the system by which companies are directed and controlled. Scholars give varied definitions of corporate governance. However, corporate governance has been widely used in an organization to govern the entire organization. Corporate governance is how the corporation is directed, administrated, and controlled, of which these affect the company's goals and direction.

The origin of the term "governance" was derived from the Greek word "kyberman", which means to steer, guide or govern, and this word in Latin means "governor" and the old French "governor." However, the definition of this word has been defined in different ways by different organizations (Tapanjeh, 2009).

OECD (2004) defines corporate governance as:

"The system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders, and other stakeholders. It spells out the rules and procedures for making decisions on corporate affairs. Doing

this also provides the structure through which the company's objectives are set and so are the means of attaining those objectives and monitoring performance"

Meanwhile, the Malaysian Code on Corporate Governance (MCCG) (2021) defines Corporate Governance as:

"The process and structure used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability with the ultimate objective of realizing long-term shareholder value while taking into account the interest of other stakeholders".

Corporate governance is also known as a system where the company has been directed, administrated, and controlled based on the policy and laws played by the major players of corporate governance, shareholders, the BODs, and the managers. These groups play their roles in determining the corporate direction, administering the daily operation, and controlling all its activities. Corporate governance covers the duties, obligations, and rights of control, and directs the corporation. The primary function of corporate governance is to distribute the duty to the participants involved in the corporation, including BOD, shareholders, managers, and other stakeholders. It specifies the distribution of rights and responsibilities among different participants in the corporation, such as the BOD, managers, shareholders, and other stakeholders. It spells out the rules and procedures for making decisions on corporate affairs (Wanjau et al., 2018). Corporate governance allows the participants to communicate amongst the members in discharging their responsibilities. Usually, the participants of corporate governance in a corporation consist of shareholders, management and the BOD, the regulators, employees, suppliers, partners, customers, constituents, and the general community. The participants will support each other towards the business corporation to grab the opportunities and interest.

Corporate governance initially addresses the conflict of interest between management and shareholders (Jensen & Meckling, 1976). However, corporate governance has a broader scope to ensure a corporation's sustainability and plays different roles to ensure a company's success (Abu-Tapanjeh, 2009). A robust governance system can withstand the economic crisis. It is due to corporate governance principles benefitting from the economic ups and downs without the dissolution of the existing corporation (Wajeeh, 2012). Moreover, it plays a significant role in macroeconomic stability and provides the appropriate resources for economic growth and social welfare (Haddad et al., 2011).

Numerous studies discuss corporate failure that involved giant companies, such as WorldCom, Enron, Parmalat, Bank of Credit, and Commerce International in the UK and US revealed the scandals, collapse, and frauds that led to the worldwide corporate governance issues. These corporate issues can be attributed to a lack of transparency and inadequate disclosure of the company's results (Khanifah et al., 2020).

The crucial objective of corporate governance is to ensure corporate accountability and transparency for those involved in the policy implementation of organizations through mechanisms that will reduce principal-agent conflict. Corporate governance is the system for those involved in the policy implementation of organizations through mechanisms that will reduce principal-agent conflicts (Wanjau et al., 2018).

2.2.1 Disclosure and Transparency

The academic and market regulators broadly recognise corporate transparency as the crucial element resulting in the numerous rules and regulations introduced overtime to ensure timely and reliable disclosure of

financial information, creating standards to which companies must adhere (Wanjau et al., 2018).

Disclosure and transparency are the significant elements emphasised by Islam. Allah SWT mentions this as in the following verse:

"Not upon the Messenger is [responsibility] except [for] notification. And Allah knows whatever you reveal and whatever you conceal" (Al-Qur'an, Al-Maidah 5: 99)²

Transparency is defined as disclosing the information in revealing the relevant company's information (Nur'ainy et al., 2013). Disclosure of the information, such as the company's activities, operations, and transactions, allows the public to obtain the essential information for decision making (Fung, 2014). Enhancing corporate governance disclosure could mitigate the information asymmetry between shareholders and managers (Darmadi, 2011a). For instance, the stakeholders, shareholders, and the public are always concerned about the correct and timely information concerning a company's investment decisions (Haqqi, 2014). The banks that disclose the information and transparent in business deals will attract the people and gain the trust and confidence of Muslim consumers towards Islamic banking institutions (Haqqi, 2014).

Furthermore, the disclosure may lead to the business activities conducted with justice and honesty (Bukhari et al., 2013). It would also enable the firm to avoid fraud or dispute after the transaction is executed. Reporting all activities in the annual report allows the customers to review and evaluate the level of assurance in the bank's operation. The study of performance conducted by Bijalwan and Madan (2013) shows that the transparency and disclosure level contribute to better corporate governance and

² Al-Qur'an. Al-Maidah 5: 99.

performance. This study shows a significant relationship between transparency and shareholders' rights and firm performance.

Disclosure and transparency reflect the level of confidence and influence the firm's performance through financial performance. In the context of corporate social responsibility, disclosure plays a crucial role in ensuring corporate transparency, developing corporate image, and providing helpful information in deciding for investment purposes (Aribi & Gao, 2010; Gray et al., 1988; Harun et al., 2020; Patten, 1990). Strengthening the disclosure in reporting on the corporate governance might eliminate the business failure that signals the stakeholders, especially regulators, regarding the status of the firm, and may also help to reduce information asymmetry between outsiders and insiders, and between institutional shareholders and minority shareholders (Haat et al., 2008).

Hassan (2010) states that there are limitations on transparency in several aspects: the IFIs in disclosing the Shariah information, the right to access the document, and the necessary information and the publication. A similar study conducted by Amalina et al. (2013) on the extent of the Shariah governance reporting on the disclosure, where they found that only about 57 percent of the Islamic banks disclose their annual report activities. This study also indicates that only 30 percent of banks confirmed that the review process is based on valid and reliable information against the Shariah review standard developed by AAIOFI since this standard is not being applied in Malaysia and Indonesia.

Al-Tamimi (2012) revealed that the effects of corporate governance on performance and financial distress have a significant positive relationship between corporate governance practices of UAE national banks and disclosure and transparency.

This result has proven that the UAE banks are aware of disclosure and transparency.

However, this result indicates an insignificant positive relationship between the corporate governance practices of the UAE national banks and the level of performance. Another study conducted by Bijalwan and Madan (2013) shows that the transparency and disclosure level contribute to better corporate governance and performance. This study shows a significant relationship between transparency and shareholders' rights, and firm performance. Hassan (2011) found that Islamic financial institutions' disclosure and transparency practice is still low, and the institution needs to improve to maintain credibility and accountability. Hassan (2011) also argued that, there is a need for the Shariah board to enhance the technical and legality of Islamic financial products, especially in Islamic values, ethics, and the value-added on Islamic finance practices. The need to improve the internal code of conduct for the Shariah board will enable the firm to strengthen Shariah's compliance aspects and finally enhance the performance and credibility of the IFIs. Moreover, transparency and disclosure are essential parts of the Shariah governance framework; it constantly impacts the cost of capital, reputation, investors' decisions, and stock prices. Stakeholders, shareholders, and the general public are always concerned over the correct and timely information about a company for their investment decisions (Haqqi, 2014).

In IFIs, the BOD and SC disclose the Shariah governance policy and practices in the annual report. The elements of Shariah governance are required to be disclosed by the board on its oversight, accountability for Shariah governance implementation, and the IFI's overall compliance with Shariah. Furthermore, the disclosure required by the SC is related to their responsibilities towards Shariah governance and their opinion on the state of the IFI's Shariah compliance. (BNM, 2019). Consistent with the legitimacy theory, disclosure is considered as a critical element to gain public confidence, which is aligned with the aim of Islamic banks to provide services and products based on

Shariah, which is in line with Muslims' need to fill the obligation of Muslims (Ahmed, 2011). Knowing that most Islamic banks' customers are Muslims, Shariah compliance in the bank's operations, activities, and transactions are critical to ensure the Islamic banks genuinely serve them in alignment with the Shariah principles.

On the other hand, the information concerning the Shariah contract, the reporting of non-permissible activities income or source, and the zakat contribution or other corporate social responsibility (CSR) program conducted by the company are also significant to attract the customers. Reporting the bank's activities in the annual report allows the customers to review and evaluate the level of assurance. It clarifies the importance of the banking sector in convincing the stakeholders towards the capability of the institution.

The legitimacy theory explains that Islamic banks need to depend on society and the public to realize their business goals (Zain & Abdullah, 2019). In this effort, a business organisation focuses on the public to be aware of their business and attract them, where the demand arises and utilises the resources, such as natural, human, supply, and demand. Hence, it is crucial to consider the needs and interests of the community to ensure they feel acknowledged in supporting the business of an organisation. Disclosing the information related to activities, particularly community activities, provides evidence to the public that shows the appreciation and the welfare of an organization. In return, it will strengthen the transparency policy, improve the reputation, and meet the needs and interests of the community. However, the challenge is that failure to meet society's expectations of its propensity can trigger unforeseen actions against the operations and cause restrictions on its resources and demand (Yusoff & Alhaji, 2012).

2.2.2 Accountability

In Islam, accountability is related to the Divine law, Shariah, as stated in the Holy Quran. Accountability has been repeated several times as *hisab*, referring to Muslims' obligation to perform their responsibilities and duties in fairness and justice. They will be held accountable and responsible for each action performed.

In business activities, Islam teaches its believers to conduct the business following Shariah principles such as honesty in every conduct and avoiding fraud. The verse in *Al-Muthaffifin* from the holy Quran mentions the cheating in the scale that Allah SWT curses the traders who reduce the scale. In addition, any activity regarded as usury is prohibited, as clearly narrated in the Quran:

“Those who consume interest cannot stand [on the Day of Resurrection] except as one stands who is being beaten by Satan into insanity. That is because they say, “Trade is [just] like interest. So whoever has received an admonition from his Lord and desists may have what is past, and his affair rests with Allah. But whoever returns [to dealing in interest or usury]- those are the companions of the Fire: they will abide eternally therein”. (Al-Qur’an. Al-Baqarah 2: 275)³

Accountability in business dealing is to avoid any doubt, injustice, and deception. In this regard, the business activities must be guided by the concept of *tauhid*, *ihsan*, and *tawakkal* (Lewis, 2006). Besides that, the Holy Quran signifies that accountability is crucial to be practised in the transaction when dealing with people. As narrated in the Quran:

“O you who have believed. When you contract a debt for a specific term, write it down. And let a scribe write (it) between you in justice. Let no scribe refuse to write as Allah has taught him. SO let him write and let the one who has the obligations dictate. And let him fear Allah, his Loard, and not leave anything out of it”. (Al-Qur’an. Al-Baqarah: 282)⁴

³ Al-Qur’an. Al-Baqarah 2: 275.

⁴ Al-Qur’an. Al-Baqarah 2: 282.

and

“To Allah belongs whatever in the heavens and whatever is in the earth. Whether you show what is within yourselves or conceal it, Allah will bring you to account for it. Then He will forgive whom He wills and punish whom He wills, and Allah is over all things competent”. (Al-Qur’an. Al-Baqarah 2:284)⁵

They contend that the accountability in IFIs has profound implications for corporate governance. Accountability in an organisation is the mechanism and the business process that ensure all the managers can conduct their duties and make decisions accountable (Magalhaes & Al-Saad, 2013). Thus, IFIs must ensure that management, reporting, and the entire business activities must be consistent and helpful in assessing the level of accountability and ensuring compliance with the bank’s activities following Shariah requirements, thereby increasing the community’s confidence level in IFIs.

2.3 Shariah Governance

Shariah is defined as ‘the road to the watering place’ or ‘the straight path’. Technically, it is defined as ‘the laws that God revealed to Prophet Muhammad (PBUH) in the Quran and Sunnah (Muhammad, 1414) (Hilmy & Hassan, 2019). Shariah governance refers to the structure and process to ensure compliance with Shariah rules and principles Mizushima (2014). It refers to a set of institutional and organisational arrangements and the monitoring aspects of Shariah compliance in IFIs (IFSB, 2009). A proper Shariah governance framework is crucial to differentiate between corporate governance in Islamic institutions and conventional institutions, besides enhancing the confidence of stakeholders, mainly Muslim stakeholders.

⁵ Al-Qur’an. Al-Baqarah 2:284

Hasan (2012) emphasises that corporate governance in the Islamic perspective is faith-based rationalism, which consists of *akidah*, Shariah, and *akhlak* as episteme and the welfare of people as a corporate goal. Choudhury and Nurul Alam (2013) define corporate governance by combining the epistemological foundation and the functional ontology of the Islamic worldview of *tauhid* that is,

“...immersed with corporate social responsibility in the light of the moral law of *tauhid* and its continuous recalling in the processed functional ontology of the evolutionary learning system in the unity of knowledge involving a decision-making by the medium of the share driven by *tasbih*; that is the discourse induced by moral consciousness”.

Shariah governance embeds the Islamic values and emphasises equality and justice. Shariah governance includes the additional layer regarding Muslims’ belief as the highest level related to the faith towards the Creator (Allah SWT) as a symbol of worship. This spiritual aspect leads the people to be more responsible, accountable, transparent, honest, fair, and just in performing their duties. It also motivates people to work harder to accomplish the goal in life and seek pleasure from God and happiness in Hereafter.

Shariah compliance in Islamic banks is the key feature of Shariah governance (Mollah & Zaman, 2015), emphasising the Islamic principles and its values in a business transaction, such as the prohibition of the unlawful source. These principles provide legitimacy to Islamic banking practices, which Islamic banking needs to abide by the Shariah principles in the entire organisation (Chowdhury & Shaker, 2015). Lacking in defining the Shariah non-compliant elements can jeopardise the existence of the institution and expose to the risk such as fiduciary and reputational risk (Chowdhury & Shaker, 2015).

Shariah governance promotes high ethical conduct, high accountability, transparency, fairness, and responsibility towards the oneness of Allah. The oneness of Allah or *tauhid* posits that the human activities and actions are united with religion, whereby humans are responsible and will be accounted for their effort. Muslims believe that God will account for every action, and this belief encourages people to produce better performances when such a belief is implemented in the Shariah governance (Obid & Naysary, 2014). The concept of *tauhid* urges Muslims to conduct their business activities ethically and responsible on their duties in line with the Islamic teaching (Kasim et al., 2013).

This principle is consistent with the stewardship theory, introducing the *tauhid*, *Khalifah*, and brotherhood concepts. *Khalifah* refers to the board member carrying out the duty as a steward by recognising that corporate governance requires disclosure and addressing accountability as an obligation to God (Maliah et al., 2015). Stewardship theory encourages the manager to act as stewards. A steward should know and understand their responsibility and play their roles to enhance organisational performance.

In Malaysia, IFIs are required to implement Shariah governance. The Shariah governance has been guided by the issuance of the Shariah Governance Framework (SGF) 2010 and later the Shariah Governance Policy Document (SGPD) 2019 by the BNM. The SGF provides a comprehensive guideline for IFIs towards the implementation of Shariah governance. The SGF emphasises the roles of the Board, SC, and the management concerning Shariah matters. According to the SGF 2010, IFIs should have at least three SCs to function effectively. In addition, Abu Samah and Hassan (2014) state that there are three critical features of Shariah governance practice:

Institutional/organisational arrangement, effective independent oversight (supervision) on Shariah-compliant, and Shariah pronouncement, dissemination, and Shariah review.

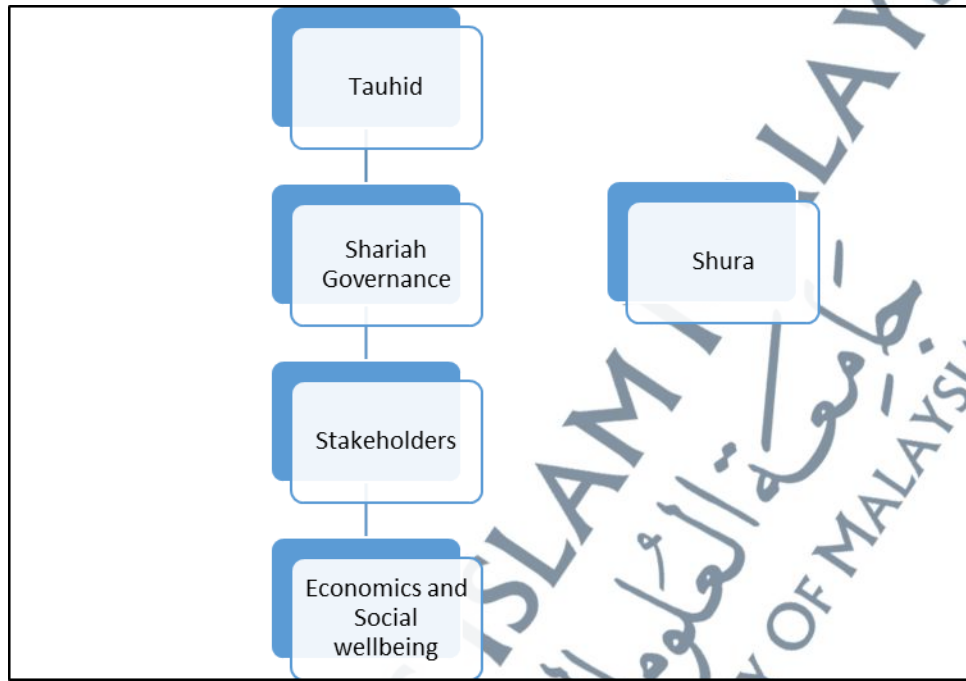


Figure 2.1: Shariah Governance Structure

Figure 2.1 shows corporate governance from an Islamic perspective derived from *tauhid* as a spiritual value. *Tauhid* is the highest component in establishing Shariah governance (Md Zain & Shafii, 2018), while *shura* is the system in corporate governance to decide and to achieve a mutual agreement. *Tauhid* refers to Allah's SWT Oneness as the foundation of Islam about the faith of Muslims, guiding the Muslims through the Divine law. *Tauhid* leads the Muslims to understand and believe in the existence of the ultimate judge, which is Allah SWT rather than a human judge. The supreme judgment is the day of judgments (*Yaumul Qiyamah*) in Islam. Belief on the Judgment Day is one of the pillars of Islam; Muslims believe that, during the Judgment Day, humans will be held accountable for their actions, and it will be decided whether

they are to be rewarded or punished according to their practices (*'amal*) during their lifetime (Md Zain & Shafii, 2018). This belief guides human to avoid evil and to do good deeds in daily life. This value also encourages people to prevent unethical behaviours and leads them to seek forgiveness for the mistakes that they have committed. Such value leads them to perform their duties with honesty and trustworthiness in organisational practice.

The concept of *tauhid* in Shariah governance practice has led the people toward high ethical conduct as Islam provides the code of conduct for all humankind. This code of conduct follows Shariah or Islamic law. As derived from the holy Quran and Hadith, Shariah law contains all prohibitions and encouragement in all matters. In the business environment, ethical conduct is of utmost importance (Abu-Tapanjeh, 2009). According to history, unethical behaviours cause the collapse of several companies.

Islam encourages and motivates people to work harder to achieve success and emphasises a high work ethic in conducting business (Bhatti et al, 2016). A proper governance system is influenced by high moral and ethical practice in the organisation, as Muslims believe every human action is rewarded according to their deeds. Allah SWT mentions in the Holy Qur'an:

“And for all are degrees [i.e., positions resulting] from what they have done. And your Lord is not unaware of what they do” (Al-Quran. Al-An'am 6: 132)⁶

Muslims must carry out their duties correctly be highly responsible, honest, and transparent in all activities. The proper conduct in an organisation can be related to high performance in the business environment.

⁶ Al-Quran. Al-An'am 6: 132.

On the other hand, *shura* is the system introduced since the prophet Muhammad SAW chose the *khalifah* (leader) to lead the country. The concept of *shura* in Islam allows the members to select the best leader to lead the organisation. This system is based on a consensus among the members in making the decision, which is based on the discussion and approval. *Shura* has been implemented and applied as one of the pillars in Shariah governance. The *Shura* system is represented by scholars who are the Islamic thinker and experts in Islamic principle (Bukhari et al., 2013). This expertise is crucial that has been highlighted in the Shariah governance framework, where the appointment of SCs among the scholars will ensure all bank's activities follow the Shariah.

In Malaysia, IFIs are required to implement Shariah governance practice based on the Shariah Governance Framework (SGF) 2010 and later the Shariah Governance Policy Document (SGPD) 2019 by the BNM. The SGF provides a comprehensive guideline for IFIs towards the implementation of Shariah governance. The SGF emphasises the roles of the Board, SC, and the management concerning Shariah matters. According to the SGF 2010, IFIs should have at least three SCs to function effectively. In addition, there are three critical features of Shariah governance practice namely institutional or organisational arrangement, effective independent oversight on Shariah-compliant, and Shariah pronouncement, dissemination, and Shariah review (Abu Samah & Hassan, 2014).

2.3.1 Shariah Governance Practices in Malaysian IFIs

The establishment of IFIs has fulfilled the Muslim's needs towards a religious requirement by providing Shariah-complaint's products and services. To enhance the credibility and consistency of IFIs towards Shariah practices, the SGF has been

developed by the BNM as the guidelines for IFIs as Shariah requirement. This guideline provided for the IFIs, is to ensure that all Islamic bank's transactions and activities follow the Shariah. This guideline allows the institutions to prevent the Shariah risk embedded in the transaction or in any part of business activities that deal with a prohibited element, such as *riba* (interest), *maisir* (gambling), and *gharar* (uncertainty). It is also to prevent unethical issues or conduct in an organisation (Satkunasingam & Shanmugam, 2004). The Shariah governance in IFIs, comprised of the SSB as stated in the SGF, has differentiated between conventional and Shariah governance. Shariah scholars represent the SSB to advise and oversee Shariah matters independently. The governorship of the Shariah board is to control the bank's transaction based on the Islamic law (Ghayad, 2008). The members of the Shariah board are entrusted to carry out their duties of directing, reviewing, and supervising the activities in Islamic banks to ensure the transaction follows the Shariah principles.

In Malaysia, the SGF is required for IFIs to ensure that the proper Shariah governance is implemented in IFIs. The implementation of the SGF in Malaysia is based on a centralised model developed by the BNM, which enforces IFIs to set up their own SC according to the rules formed by the Shariah Advisory Council (SAC) of BNM. The SAC of BNM is the highest authoritative body serving Shariah matters related to Islamic finance in Malaysia (BNM, 2022). This mandate has been given to ascertain the Shariah-compliant matter, including Islamic banks, Takaful, Islamic financial businesses, or other financial institutions that apply the Shariah principles (Miskam & Nasrul, 2013).

The BNM has established the framework and act particularly to enhance and strengthen Shariah governance; namely, i) the current policy document SGPD 2019, ii) the SGF 2010 issued as comprehensive guidelines for IFIs towards Shariah-compliant,

iii) the act provides the regulation and supervision of IFIs, payment system, and other related entities IFSA 2013, iv) the guiding principle requirement in corporate governance for the Islamic financial services IFSB and GP8-I, and the guidelines for Islamic Bank licensed under the Islamic Banking Act 1983 that focused on providing the basis for presentation disclosure of reports and financial statements of Islamic banks.

Corporate governance frameworks are provided to achieve the effectiveness of the management and ensure the level of accountability in the organisation to protect the interest of shareholders specifically and stakeholders (Alexakis & Tsikouras, 2009). However, as corporate governance mechanisms monitor the corporation and ensure that good corporate conduct are practised, the lack of a governance system may generally reflect the firm. Therefore, the organisation's failure directly reflects the lack of governance practice.

Thus, the financial institutions' corporate governance needs to emphasise that these institutions deal with many funds managed by different banks belonging to other account holders and investors (Bukhari et al., 2013). In addition, the corporate governance code of conduct has been practised by other international Islamic banks, mainly in Islamic countries. This code provides the guidelines to protect the stakeholder's interests and rights. This is similar to the State Bank of Pakistan (SBP), which provides the corporate governance code of conduct to establish financial institutions and provides comprehensive guidelines to the BOD and the management (Bukhari et al., 2013).

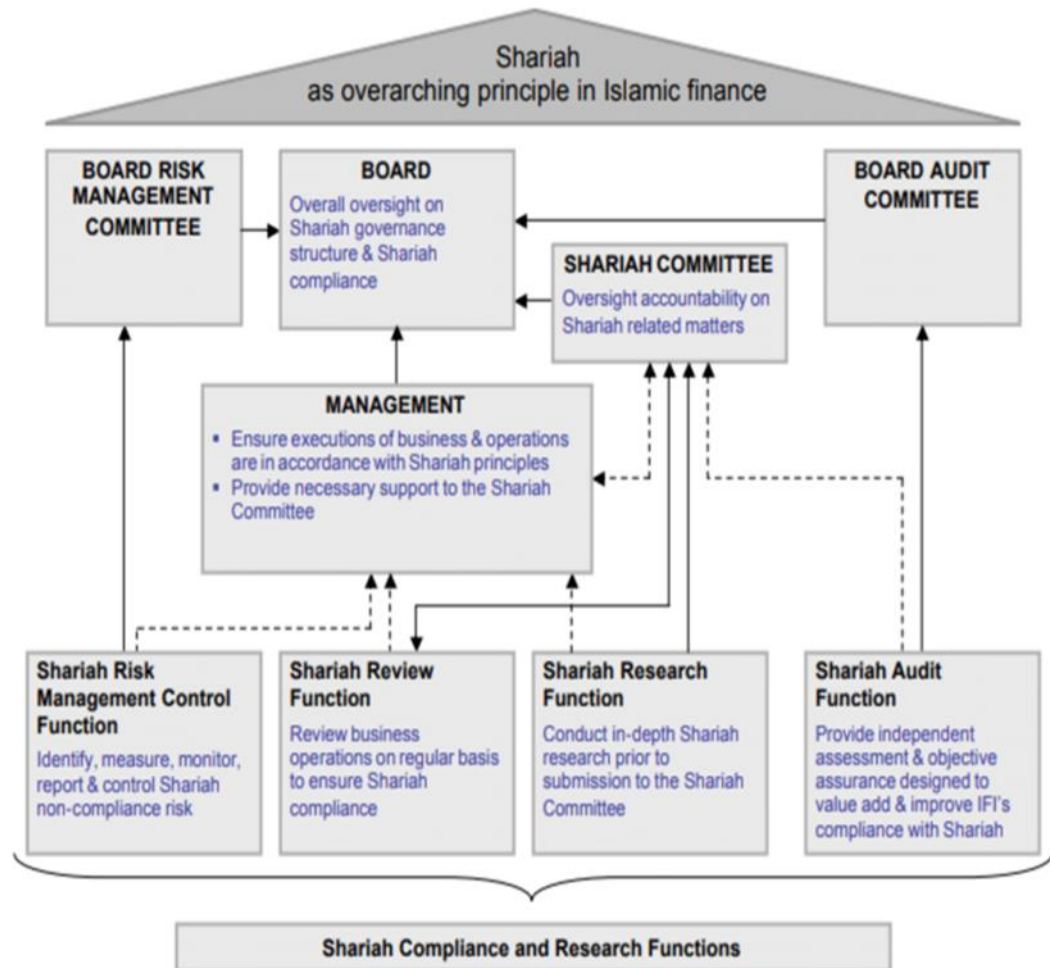
2.3.1.1 Shariah Governance Policy Document and Shariah Governance Framework (SGF) by Bank Negara Malaysia (BNM)

In Malaysia, Shariah governance practices in IFIs has been guided by SGF 2010 and currently has been superseded by SGPD 2019. Shariah governance guidelines provided to ensure the entire business operation complies with the Shariah. Likewise, a manager in Islamic organisations extend the responsibility towards the Shariah principles rather than maximise the shareholders' profit as the motivation (Bukhari et al., 2013). However, Shariah governance practice is essential to ensure all the right of stakeholders are protected that can maximise the shareholders' value of wealth by protecting the interest and rights (Hasan, 2009c).

Recently, the Shariah governance in Malaysia has shown positive developments that are reacted by the BNM. BNM, as the regulatory body, continuously enhances and strengthens the Shariah governance system through its policy to ensure strong Shariah practices in IFIs. This enhancement of Shariah governance was proven by the BNM through the implementation of SGF 2010. SGF provide a sound and robust Shariah governance that requires the IFIs to adopt this framework as a guideline. The Shariah board is mandated to monitor the implementation of the SGF; this function is to control the Islamic banks' transactions and the entire operation operated based on Islamic law (Ghayad, 2008). The Shariah board members are entrusted to ensure all the transaction conducted complying with the Shariah by directing, reviewing, and supervising the activities of Islamic banks (BNM, 2011).

Following that, the BNM's initiative is continuously presented according to the issuance of the Islamic Financial Service Act (IFSA) in 2013. This act was enacted under Malaysian law to provide regulation and supervision. Meanwhile, in 2019, the BNM is again enhancing the Shariah governance position as an essential element in IFIs

by introducing a new policy document known as the Shariah Governance Policy Document, effective in 2020.



Source: BNM (2010)

Figure 2.2: Shariah Governance Framework

The SGF for IFIs was designed and established to meet three main objectives:

1. Sets out the bank's expectations on an IFI's Shariah governance structures, processes, and arrangements to ensure that its operations and business activities follow the Shariah.

2. Provides comprehensive guidance to the BOD, SC, and management of the IFI in discharging its duties in matters relating to the Shariah.
3. Outlines the functions related to the Shariah review, Shariah audit, Shariah risk management, and Shariah research.

In addition, the BNM emphasises that the SC members and Shariah function to enhance sound and robust Shariah governance. Based on the Shariah Governance Framework model, there are four Shariah governance functions under the Shariah-compliant and research function. These functions are:

1. Shariah risk management and control function:

Shariah risk management is “a function to identify systematically, measure, monitor, and control Shariah non-compliance risks to mitigate any possible non-compliance events”.

“The systematic approach of managing Shariah non-compliance risks will enable the IFI to continue its operations and activities effectively without exposing the IFI to unacceptable levels of risk”.

2. Shariah review function:

“The Shariah review function refers to a regular assessment of Shariah compliance in the activities and operations of the IFI by qualified a Shariah officer(s) to ensure that the activities and operations carried out by the IFI do not contravene with the Shariah”. The function involves examining and evaluating the IFI’s level of compliance to the Shariah, remedial rectification measures to resolve non-compliances, and control mechanisms to avoid recurrences.

3. Shariah research function:

The Shariah research function “refers to performing in-depth research and studies on Shariah issues, including providing a day-to-day Shariah advice and consultancy to relevant parties, including those involved in the product development process(es)”.

4. Shariah Audit function:

“The Shariah audit refers to the periodical assessment conducted from time to time to provide an independent assessment and objective assurance. It is designed to add value and improve the degree of compliance concerning the IFI’s business operations, with the primary objective of ensuring a sound and effective internal control system for Shariah compliance”.

Therefore, the implementation of the SGF by the BNM affects the IFIs by guiding this institution towards the Shariah governance.

In 2019, the BNM issued a new policy document of Shariah governance named Shariah Governance Policy Document (SGPD) 2019, replacing the SGF issued in October 2010. Unlike the SGF, the SGPD 2019 provides more precise and detailed guidelines and direction than the SGF 2010 to strengthen the Shariah governance (Kamaruddin et. al. 2019). Specifically, the policy document enhances oversight accountabilities on the BOD, SC, and other important organs in Shariah governance. Another element relates to the SC's objectivity in order to support sound decision-making and robust internal control systems for effective management of Shariah non-compliance risks (SGPD, 2019). This policy document also emphasises the need for IFIs to demonstrate that the Shariah governance arrangements operate effectively and appropriately to their size, nature of business, and complexity of activities and structure.

2.3.1.2 Islamic Financial Service Act 2013

Malaysia has placed the IFIs in significant roles in the country. The recent development of IFIs shows a remarkable achievement through their business activities, such as providing their services to individuals or corporations. The establishment of IFIs is also to fulfil the need and obligations of Muslims. The existence of Islamic banks has contributed to the economic development in Malaysia and to balance the social economy. The legal framework has supported the implementation of IFIs to ensure the operations are following Shariah in all aspects.

The Pre-2013 Malaysia legal provision is based on the Central Banks of Malaysia Act 2009 (Act 701). This Act stipulates the need to establish the Shariah Advisory Council and the roles of the Shariah Advisory Council to carry out their functions to ascertain the banks' compliance with the Shariah. Before that, the legal provision was based on the Central Banks of Malaysia Act 1958 (Act 509). This act was amended in 2003 by enhancing the position of the Shariah Advisory Council under the supervision of the BNM. The amended Act provides the new provision with the establishment of the Advisory Council in section 16B. The acts were established as the authoritative body towards the Islamic law for Islamic banking business, *takaful* business, Islamic financial business, Islamic development financial business, or any other business meant for Shariah principles.

The Malaysian legal system has enacted the Act, specifically for the institutions providing Islamic financial service (IFSA), which came into force on 30 June 2013. The IFSA has placed IFIs as a platform for empowering Islamic economic systems in Malaysia towards the sound Shariah compliant system, encompassing the banking system, *takaful* sector, financial market and payment system, and other financial intermediaries. The provision was enacted to promote financial stability and Shariah

compliance for IFIs. The rules related to the Shariah governance in this provision under Sections 30 until 36 of IFSA 2013 highlight the requirement for the establishment of SC, the appointment of SC, duties and responsibilities, and the cessation of members of the SC.

The IFSA focuses on transparency, accountability, and governance in the management and operation of Islamic banking in Malaysia. This current legal provision has regulated the SC's specific requirement, highlighted the SC's criteria, and enhanced the roles and position of the SC as one of the integral parts of the company (Miskam & Nasrul, 2013). This regulation has increased the responsibility of the SC to be at the same level as the BODs and the Senior Management (Muhamad Sori & Mohd Rashid, 2015). In addition, this Act has enhanced Shariah governance by codifying the Shariah-compliant requirements and enforcing the penalties for non-compliant (Hassan, 2016). In addition, this current rule has placed more significant roles on the BNM in regulating and supervising financial institutions, payment systems, and other relevant entities, including monetary and money market surveillance to promote financial stability and the Shariah compliance system (Thajudeen, 2014).

In Sections 27 to 39, the Act allocates the Shariah-compliant matters. These sections interpret the Shariah-compliant requirement and specify the matters related to business activities, while the specific Shariah Governance rule has been allocated in Sections 30 to 36. The Shariah governance provision emphasises a strict requirement of the SC that needs to meet the requirement as stipulated in the SAC, whereby the SAC is the highest authority for IFIs in Malaysia. Section 30 in this act has provided more specific requirements that require the institution to apply directly to the Central Bank to establish the SC. This Section will enable the Central Bank to have the information and ascertain the proper supervision towards the activities conducted by the institutions.

Concerning the SC members, this act highlights the requirement of the appointment of the SC under Section 31 with a cross-reference to subparagraph 29(2)(a)(ii), stipulates that the SC should meet the requirements to be qualified as SC members. Meanwhile, Section 32 highlights the functions and duties of the SC concerning the ascertainment of Islamic law. This provision emphasises the responsibility and role by exercising the Shariah governance structure, which binds with the functions and duties of the BODs and senior officers with Shariah compliance.

In Sections 33 and 34, the Act stresses the cessation of members of the SC. This Act emphasises a critical requirement for SC members, namely, any SC member who does not meet the requirement is subject to cessation as a member. In addition, the provision under Section 35 is related to the institution's responsibility, directors, managers, or officers to provide an accurate and complete document. This information is required to ensure that the SCs perform their duties effectively. Finally, Section 36 gives the SCs a mandate to perform their duties, emphasise the confidentiality matters between members and the banks, and the SC should conduct their commitment in good faith.

2.3.2 Shariah Governance and the Performance of Islamic banks

A substantial volume of literature concerning Shariah governance has become available. These studies reveal that Shariah governance plays a significant role to determine the performance of a firm (Kausar et al. 2021; Ben Abdallah & Bahloul, 2021). Likewise, in IFIs, a corporate governance function is placed substantially to ensure the management and business operation work properly. The Shariah governance reflects a few elements: Integrity, transparency, accountability, and responsibility with the Islamic principles to preserve *maslahah* for all stakeholders (Ahmad & Ishak, 2020).

The literature has proven the importance of Shariah governance, which states that the implementation of Shariah governance to the firm performance shows a positive relationship between the SSB and the performance of Islamic banks. A study by Ghayad (2008) on corporate governance and global performance of Islamic banks show that the Shariah board's roles in the performance of Islamic banks include the governorship of Shariah board and Shariah board profit. The governorship of the Shariah board controls the bank's transactions based on Islamic law. They are entrusted with directing, reviewing, and supervising the Islamic bank activities to ensure they always comply with the Shariah principles.

In addition, IFIs have additional roles regarding the Islamic principles that need to respond by implementing a Shariah-compliant system to conduct their business activities following the Islamic principles (Md Amin, et. al, 2021). Shariah governance provides comprehensive Islamic principles to conduct the entire business operation, differentiating between Islamic and conventional practices (Wasiuzzaman, 2013), unlike the conventional principles based on self-interest without considering the sources of income and how the operation is conducted.

Concerning the corporate governance system, it is noted that proper governance mechanisms integrate the interests of owners, managers, and dependents in the corporation and enable the securing of long-term capital, retention of confidence of financiers, and using the capital effectively (Musibah et al., 2014). Ho (2005) explains that good corporate governance could increase competitiveness and enhance financial performance. The literature has also proven a positive relationship between corporate governance and corporate performance, consistent with the prior studies (Haddad et al., 2011).

On the other hand, a study on Islamic banks and the Islamic bank window conducted by Bukhari et al. (2013) revealed that the most significant dimension affecting corporate governance in Islamic banks is the BOD and SSB. Likewise, Ghayad (2008) conducted a study on corporate governance and the global performance in Islamic Bank. This study analysed the SSB and the performance of Islamic banks whereby it was found that the existence of the Shariah board in the Islamic bank with their role is significant to ensure the profit is complying with the Islamic law and indirectly influences the financial performance. Other than the SSB, this study discusses other Shariah governance mechanisms, namely, Shariah audit and Shariah risk. These mechanisms are highlighted in the previous guideline (SGF 2010) and the new policy document (SGPD 2019). Thus, in this Shariah governance section, the Shariah governance mechanisms were identified for this study. The following subsection will explain each of the Shariah mechanisms identified for this study.

2.3.2.1 Shariah Committee Disclosure and Performance

Corporate governance disclosure is an essential factor for Islamic banks. It could maximize the banks' value guided by a set of rules and regulations that provide transparency and accountability (Abdallah & Bahloul, 2021). In Shariah governance, the term “SC”, which is also used as the “SSB”, is an independent committee to observe the business operation and ensure the stakeholders conducting the business for the SSB are independent boards to investigate, audit, and provide Islamic banks with Shariah principles at ex-ante and ex-post for all financial transactions using a standard policy (Quttainah, 2012).

The SSB was selected based on the qualification and knowledge in Shariah. The Shariah background is significant to monitor and lead the Islamic banks towards Islamic

governorship to ensure the bank's activities comply with Islamic laws and that they build the Islamic values in the organisation. In the Shariah governance practice in Islamic banks, the institution must implement the Shariah requirement stipulated by the BNM for IFIs. Therefore, the SSB plays a significant role in ensuring that the entire operation is Shariah-compliant. Also, the Shariah supervisions under the SSB present various objectives, including providing legitimate solutions for barriers and conflicts and improvements for the future (Garas & Pierce, 2010).

Recently, numerous studies emphasised the function of the SSB as an essential mechanism in Islamic banks to ensure the activities of Islamic banks comply with Shariah. It is considered one of Shariah governance's significant components of IFIs (Grassa, 2013). The primary function of the SSB is to ensure the transaction in Islamic banks follows Islamic principles. Failure to ensure the Islamic banking operates on Shariah compliance would cause most people to lose confidence in the Islamic banking system, especially the Muslim community (Alnasser, 2012).

In addition, Amalina et al. (2013) state that the role of the SSB is also to assure the Shariah compliance that could influence the Shariah is related to disclosure in the annual report in Islamic banks. The study by Ghayad (2008) on the corporate governance and the global performance of Islamic Banks state that the roles of the SSB on Islamic banks' performance include the governorship of Shariah board and Shariah board and profit. The governorship of the Shariah board oversees the bank transaction based on Islamic law. They are entrusted with directing, reviewing, and supervising the Islamic bank activities to ensure that they always comply with the Shariah principles. In a study, Bukhari et al. (2013) also argue that the SSB allows the financial activities based on *fatwas* and will review whether the transaction follows the Shariah. In addition, the execution of the SSB by Islamic financial institutions deals with the

transaction in the business activities towards Shariah issues in financial transactions to ensure compliance with the Shariah requirements.

A recent study reveals that SSB has a positive and significant impact on ROA and ROE (Abdallah & Bahloul, 2021), which indicates that good governance had a significant association with higher performance in MENASA Islamic banks. A study by Mollah and Zaman (2015) investigated the impact of Shariah supervision, including the supervisory or advisory role of SSB, on performance. This study found that the effect of SSB on accounting-based performance is positive when the Shariah boards have a supervisory role. In contrast, the effect is negative when the Shariah boards have an advisory role, such as Mohammed and Muhammed (2017) describe the SSB as one of the critical stakeholders affecting the financial performance of Islamic banks. Masruki et al. (2018) revealed that the empirical result of the prior study on SSB and performance are a mix. However, most studies found a positive association between SSB and financial performance. In addition, a study's findings on corporate governance disclosure practices in Islamic banks have given the evidence on the SSB as positively significant with the ROA and ROE in the same study. This result concludes that the function of SSB plays an integral role in the performance of Islamic Banking. Mollah and Zaman (2015) found a positive and significant impact for SSB supervision on the Islamic banks' performance during the financial crisis. This result indicates that the SSBs slightly enhanced Islamic banks' performance during the financial crisis (Srairi, 2015). In contrast, a finding in a study conducted by Khanifah et al. (2020) reveals that the financial performance of ROE is not significantly related to the disclosure of Shariah governance. Even though the regression results provide evidence that Islamic banks with a higher level of corporate governance disclosure reported a high operating

performance measured by ROA, they conclude that the insignificant result is due to the small data and observation of the study.

However, it could strengthen the Shariah governance in Islamic banks. Based on the literature on the SSB and performance, most of the studies show a significant association with the performance of Islamic banks. However, the function of the SSB as an independent body specialising in *Fiqh* and *Muamalat* is not influenced by management, board, or shareholders (Nienhaus, 2007). They are primarily responsible for ensuring investments, business activities, services, and other financial transactions comply with the Shariah principle (Tawfeeq & Alabdullah, 2017).

2.3.2.2 Shariah Audit Disclosure and Performance

Shariah audit refers to the periodical assessment to provide independent assessment and improve compliance in IFIs (Bahari & Baharudin, 2016). Shariah audit concerns the auditing process of the Shariah-compliant practices of IFIs on financial reporting, Shariah-compliant matters, and other related documents (Haniffa, 2010). According to the BNM (2019), the Shariah audit function “provides an independent assessment on the quality and effectiveness of the IFI’s internal control, risk management systems, governance processes, and the overall compliance of the IFI’s operations, business, affairs, and activities with Shariah”.

In this regard, Khalid et al. (2018) contend that the SSB’s independence and experience could enhance the internal Shariah audit’s effective essence and experience due to the position of the SSB as the ultimate oversight organ in the IFIs, the SSB could influence the internal Shariah audit’s effectiveness in IFIs. Meanwhile, a study conducted by Kasim et al. (2009) examined the expectations and actual practice of Shariah audit function in Malaysia's Islamic financial institutions (IFIs). It highlights

several issues in Shariah auditing, namely, in framework and scope qualification and the independence's issue. The discussion of the issues reveals that the actual desire for auditing does not coincide with the actual practice, indicating that the Shariah audit in IFIs was not conducted properly (Bahari & Baharudin, 2016; Nawal Kasim et al., 2009). Meanwhile, Yahya, and Mahzan (2012) reported that the Shariah practices of IFIs in Malaysia are still minimal, and therefore, it is necessary for regulators to promote a Shariah audit.

On internal Shariah audit's effectiveness, Khalid et al. (2018) examined the role of the SSB in Islamic financial institutions (IFIs) in Bahrain. Through reviewing the literature and structured interview conducted with SSB and the Head of the internal Shariah audit department, they argue that the SSB, independence and experience could enhance internal Shariah audit effective essence and experience. Due to the position of the SSB as the ultimate oversight organ in the IFIs, the SSB could influence the internal Shariah audit's effectiveness in IFIs.

On the other hand, internal audit efficiency is essential because it is often associated with financial reporting by showing its performance progress (Bett, 2014). Concerning Shariah auditing in Islamic banks, there has been a noticeable improvement in the significance of Shariah audits, which includes consulting with IFIs on their Shariah compliance (Khalid, 2020). Moreover, Shariah auditing is crucial since it is one of the instruments for enhancing Shariah governance and, as a result, reduces violations or risks, which can be either internal or external. However, the absence of Shariah regulations and a supervisory structure might make Islamic banks less effective, which could make these banks appear less Shariah-compliant (Algabry et al., 2020). Through the internal audit, the company can monitor the operations and increase the organisation's value through systematic risk management. Several studies argue that

audits in an organisation could improve the firm's performance. Alaswad and Staniši (2016) found a relationship between audit function and a firm's performance, and this correlation plays a significant role in the performance of financial institutions. Another study conducted by Awdat (2015) reveals that the importance of the internal audit function had positively impacted a firm's financial performance. Therefore, this study concludes that a practical internal audit function positively affects financial performance. However, this is contrary to a study conducted by Masruki et al. (2018) where they found no association between Shariah audit disclosure with ROA and gearing. They argue that this result is due to the lack of Shariah practice on the internal control system and opine that this area is still at the infancy level in Malaysia.

Shariah audit also essential to ensure the IFIs comply with Shariah in all organisation-related aspects. The audit activities require the auditor to examine the status of financial treatment and advise on whether the transactions made by the company are following Shariah guidelines (Lahsasna et al., 2013). The disclosure of the information may lead to business activities conducted with justice and honesty (Bukhari et al., 2013). This role has a mandate to the external auditors concerning the disclosure practices to enhance transparency to all stakeholders that points out a positive influence on a solid firm on corporate disclosure (Salem et al., 2019). Khlif and Souissi (2010) point out a positive influence on a solid firm on corporate disclosure and reveal that the appropriate information might reflect an excellent signal to investors. Otherwise, the potential investors may have the wrong signal reflected, which may negatively affect their investment decisions (Salem et al., 2019).

2.3.2.3 Shariah Risk Disclosure and Performance

The function of Shariah risk is to identify non-Shariah compliance risks that may arise from the business transaction, which is to identify the possible risk, measure the level of risk, monitor and facilitate effective risk management, and control the recurrences of non-compliance risk. Risk ultimately cannot be avoided, but the function of Shariah risk management is to deal with and mitigate the risk. Thus, the proper guidelines shall be developed to facilitate and assist the committee in managing the risk (BNM, 2011). Shariah non-compliant matters as regulated under the IFSA 2013 emphasise the Shariah matters by providing the rigorous requirement to SC and implementing Shariah compliant system in an organisation. In IFIs, stringent requirements and regulations towards the Shariah matters become the legal risk of the Shariah non-compliant identified in any business activities. In addition, adequate internal controls, risk management, accounting and external audit, and transparency might build confidence in the system in corporate governance (Chapra & Ahmed, 2002).

As discussed above, the significant risk in IFIs is the Shariah non-compliant risk. The IFSA 2013 clearly states that the failure to apply the Shariah compliance in the transaction will be fined under section 28 (5). Likewise, the IFSA 2013 emphasises that any Shariah non-compliant element in business activities is an offence under the laws. The Act provides imprisonment for a term not exceeding eight years or fine not exceeding twenty-five million Ringgit or both (Chik, 2012).

The finding of a study conducted by Grassa et al. (2020) reveals that Islamic banks seem to be more secretive about material risk than their conventional counterparts. In the same study by Grassa et al. (2020), multiple tests were conducted to determine the relationship between ROA and risk-related disclosure (RRD). Different results were

obtained, of which the coefficient on ROA in (RRD) equation remains positive and significant. On the other hand, the coefficient on RRD in the financial performance equation is statistically insignificant. Another study conducted by Rosli et al. (2017) examined the determinants of voluntary risk disclosures of Shariah-compliant companies in Malaysia, focusing on the religiosity factor and the ownership structure. The study's findings reveal that the average voluntary risk disclosures in Malaysia's Shariah-compliant companies is not more than sixty percent. The finding suggests the importance of risk management information in the annual reports of Malaysia's Shariah-compliant companies as Malaysia is growing as a leading country in the Islamic economy. Khlif and Souissi (2010) revealed that corporate governance has a relationship with the level of risk disclosure.

Meanwhile, Salem et al. (2019) found that the risk disclosure quality is significantly associated with the institutions. The result is consistent with the empirical findings, revealing that the risk disclosure quality is positively and significantly associated with the directors' institutional independence. In contrast, a study conducted by Abdel Razek (2014) found an insignificant negative relationship between risk disclosure and performance. Likewise, Masruki et al. (2018) found no association between Shariah risk disclosure with ROA and gearing. They argue that it lacks Shariah practice in the internal control system and opine that this area is still at the infancy level in Malaysia.

2.3.2.4 Shariah Governance Measurement

As discussed above, this study employed three Shariah governance mechanisms, namely, the SSB, Shariah Audit, and Shariah risk. Prior studies have widely empirically examined the SSB and performance. However, the empirical studies on Shariah audit

and Shariah risk are still limited based on the literature analysis, especially by measuring based on the disclosure method. A recent study by Sencal and Asutay (2020) employed the Shariah governance disclosure, consisting of the age of Shariah-compliant activities that have started, the number of Shariah scholars, the average level of education, and the popularity of the Shariah board as the indicators of Shariah governance disclosure. Other studies by Islam and Bhuiyan (2021) and Khalid (2020) measured the compliance level of Shariah disclosure using a disclosure index developed based on the BNM and AAOIFI guidelines for mandatory and voluntary disclosure. Likewise, Zain and Abdullah (2019) proposed the Shariah governance disclosure as a mediating role in their study between CG mechanisms and firm performance.

Meanwhile, in the study of corporate governance, Bijalwan and Madan (2013) constructed four corporate governance factors as independent variables: Transparency, disclosure, shareholders' rights, and corporate governance policy and practice. On the other hand, Al-Baidhani (2014) constructed corporate governance mechanisms, including ownership structure, board structure, audit function, and other control variables, such as bank size, age, and type of banks.

Researchers used various measurement scales in their studies to measure variables based on the method of the research. For example, Haniffa and Hudaib (2007) produced the Shariah mechanisms in their analysis of the ethical identity of Islamic banks. Their study used disclosure items to measure the independent variable, and it can be measured using the scoring method or ratio-based performance or index. For instance, Ramli et al. (2015) studied the Shariah governance disclosure to assess Shariah governance compliance. The SGF provides comprehensive Shariah matters to be applied by IFIs, which can be used as the Shariah governance mechanisms. Likewise, Shahwan (2015) used the corporate governance index to identify corporate governance mechanisms,

consisting of four corporate governance mechanisms to assess the quality of corporate governance practice. These four mechanisms are disclosure and transparency, the characteristics of the BODs, shareholders' rights and relationship with the investor, and ownership and control structure.

2.3.3 Summary of Prior Studies on Shariah Governance

Based on the literature analysis of studies on Shariah governance, Table 2.1 was generated that summarises the prior studies on Shariah governance.

Table 2.1: Summary of Prior Studies on Shariah Governance

	Authors/years	Elements	DI	SSB	SA	SR
1	Md Amin et al. (2021)	The study measured the compliance level of Shariah disclosure using a disclosure index developed from BNM and AAOIFI guidelines for mandatory and voluntary disclosure, respectively.	/	/	/	
2	Abdallah & Bahloul (2021)	Investigating the impact of the disclosure and the Shariah governance on the financial performance in MENASA		/		
3	Muhammad et al. (2021)	This study aimed to analyze the effect of intellectual capital, independent directors, academic directors, and Shariah supervisory boards on the financial performance of Islamic banks.		/		
3	Islam & Bhuiyan (2021)	The study determined the factors that influence the effectiveness of the Shariah-based audit system.			/	
4	Khalid (2020)	The study explored the Audit and Governance Committee (AGC) role for internal Shariah auditing's effectiveness in Bahrain's Islamic banks.	/		/	
5	Abd Rahman et al. (2020)	The study is on Islamic legal maxim for Shariah audit in Islamic banks looking at how the Islamic legal maxims (ILM) could provide a basis for Shariah audit practices in assisting the institution's managerial practice to achieve Maqasid al-Shariah (MS).			/	
6	Khan & Zahid (2020)	This study aimed to investigate the impact of Shariah and corporate governance on Islamic banks' performance in Asia.	/	/		
7	Ridwan & Mayapada (2020)	This study aimed to investigate the effect of sharia governance to corporate social responsibility disclosure in Indonesia Islamic banks.		/	/	
8	Norman & Haron (2020)	This study aimed to examine the impact of the Shariah governance mechanism on the	/	/		/

Table 2.1 Cont.

		performance of Islamic banks (Islamic banks) during the financial crisis of 2008.				
9	Al-Sartawi & al Musleh (2020)	This study aimed to shed light on the relationship between Shariah disclosure and the performance (social performance and firm value) of listed Islamic financial institutions in the Gulf Cooperation Council (GCC) countries.	/	/	/	/
11	Alam et al. (2021)	This Qualitative study examined the influence of SG mechanisms on Islamic banks.		/		
13	Shivaani (2020)	Developed risk disclosure index to capture both quality and quantity of risk disclosures.	/			/
14	Mansoor et al. (2020)	This study aimed to investigate the association between corporate governance characteristics, Shariah governance characteristics, and the credit rating of Asian Islamic banks.		/		
15	Hasan et al. (2020)	The purpose of this paper was to explore the Shariah governance practices of Islamic fund management companies (IFMCs) in Malaysia.			/	/
17	Khanifah et al. (2020)	This study aimed to examine the effect of corporate governance disclosure on bank performance by building a corporate governance disclosure index (CGDI) for 10 Islamic banks operating in Iran, Saudi Arabia, and Malaysia.	/	/		/
18	Omaliko et al. (2020)	This study empirically investigated the effect of Non-Financial Disclosures on the performance of non-financial firms in Nigeria.	/			
19	Hanefah et al. (2020)	The purpose of this paper was to identify issues related to governance and internal control of SNCI in selected IFIs in Malaysia.		/	/	/
20	Ab Ghani et al. (2019)	This paper examined the measurement of effective internal Shariah audit function in IFIs.			/	
21	Rosli et al. (2017)	Examined the determinants of voluntary risk disclosures of Shariah-compliant companies (ShCCs) in Malaysia, focusing on the religiosity factor and the ownership structure.				/
22	Bukair & Abdul Rahman (2013)	Empirically examined the influence of the SSB and its characteristics on the level of corporate social responsibility (CSR) disclosure.	/	/		
23	M. Hassan et al. (2017)	Identified the impact of Corporate Governance determinants on Islamic banks performance. The study analyzed the effect of BOD size, Board independence and Shariah Advisory Board on Islamic banks performance in Pakistan.		/		

Table 2.1 Cont.

24	Ahmad & Ishak (2020)	This study explored how far the element of maqasid al-Shariah is realized through the practice of Shariah governance in Malaysia.			
25	Grassa et al. (2020)	The study examined and compared the relationship between risk disclosure and corporate attributes in Islamic and conventional banks. Using a comprehensive risk disclosure index.	/		/
26	Md. Zain et al. (2020)	The study explores the reporting of Shariah governance in Islamic banks by developing the Shariah governance disclosure items.	/	/	/ /
27	Sencal & Asutay (2020)	This study aimed to determine the ethical disclosure in SARs to identify how close the Shariah disclosure is to the standards set by AAOIFI and the substantive morality of Islam. The research also aimed to examine the factors determining disclosure performance.	/	/	
28	Aslam & Haron (2020)	The purpose of this study was to examine the impact of corporate governance (CG) on intellectual capital efficiency (ICE) in Islamic banks (Islamic banks) of Organisation of Islamic Cooperation (OIC) countries.	SSB	/	/
29	Muzammil & Siddiqui (2020)	The study assessed the Shariah audit in regularities of Islamic banks in Pakistan using an exploratory study design. Qualitative interviews were conducted using a semi-structured and content analysis approach.			/
30	Zain & Abdullah (2019)	This study discusses the potential influence and relationship between the CG mechanism and firm performance of the Islamic banking sector and the mediating role of Shariah governance disclosure.		/	
31	Iryani et al. (2019)	This research aimed to assess the effect of financial performance on Maqasid Shariah performance with Shariah governance as a moderating variable		/	
32	Salem et al. (2019)	This study investigated the potential influence of corporate governance mechanisms on risk disclosure quality in Tunisia. Using the content analysis method to measure the risk disclosure quality. Examined 152 annual reports of Tunisian non-financial-listed firms	/		/
33	Khalid et al. (2018)	The study examined the role of SSB on internal Shariah audit effectiveness in Islamic financial institutions (IFIs) in Bahrain by reviewing the literature and structured interview with the SSB and Head of internal Shariah audit departments.		/	/
34	Rusyadianan & Al-Parisi (2016)	Measurement of Islamic banks' performance using the Maqasid index and profitability.		/	
35	Mukhibad (2016)	The research was conducted to prove whether the corporate Governance, Sharia		/	

Table 2.1 Cont.

		Supervisory Boards (SSB) (DV), and Corporate Ethics.		
36	Musibah & Alfattani (2014)	The objective of this study was to determine the influence of SSB Effectiveness (SSBE) and Intellectual Capital (IC) on Corporate Social Responsibility (CSR).	/	
37	Wan Abdullah et al. (2013)	The study aimed to examine the extent of disclosure on the Shariah Supervisory Board (SSB) and the content of the Board's report in the annual reports of 23 Islamic banks in Malaysia and Indonesia. The study also investigated the disclosures about zakat.	/	/

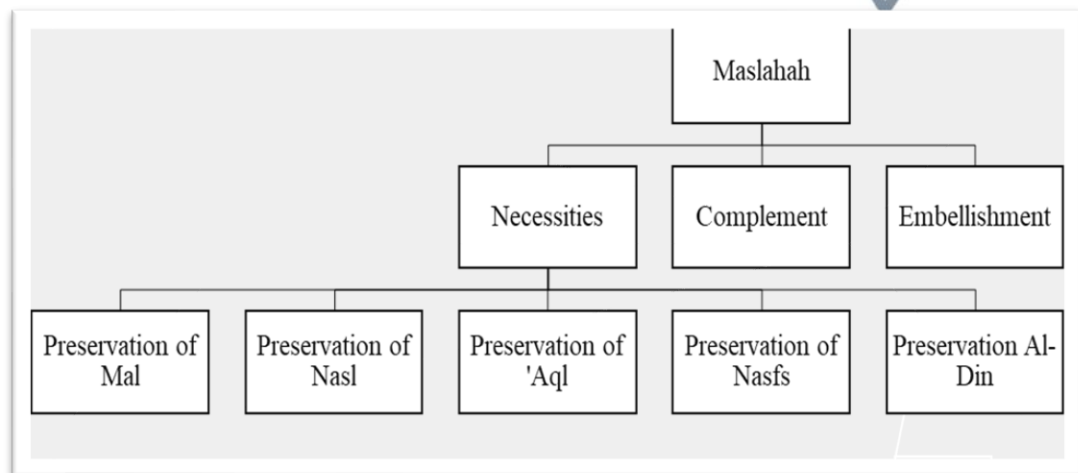
Note: DI= Disclosure Index, SSB= Shariah Supervisory Board, SA=Shariah Audit, SR= Shariah Risk

2.4 Maqasid Shariah Overview

Maqasid Shariah is well-known by many researchers as the Al-Ghazali's theory. Maqasid-cum-Masalih has been related to human life, interpreted as human well-being (Mergaliyev et al., 2019). Scholars classified *masalih* into three categories, namely, *daruriyat* (necessities), *hajiyyat* (complement), and *tahsiniyat* (embellishment). *Daruriyat* is broken into five essential elements: Daruriyat al khams or Maqasid Shariah, enumerated as preservation of din, preservation of 'aql, preservation of *nasfs*, preservation of preservation *nasl*, and preservation of *mal*.

Necessities are the absolute necessity for the individual's survival and spiritual well-being, whereby their destruction or collapse will lead to chaos in the society. For instance, theft, adultery, and alcoholic beverages are punishable as they violate and threaten the rights of others, the well-being of the family, and human intellectual integrity. Thus, the role of Shariah is to adopt the values and identify necessary measures for their preservation, improvement, and development.

Complements are defined as the benefit that facilitates human life. These complements are given to humans to manage their life in hardship without neglecting their obligation to Allah SWT. For instance, Shariah guides people in performing ibadah in hardship and complex situations, for example, Muslims can shorten their prayers.



Source: Adopted from Mohammed et al. (2015)

Figure 2.3: Theoretical Framework of Al-Ghazali's Maqasid Al-Shariah

Principally, Maqasid Shariah refers to the human being. It translates into human life regarding the need of humans to ensure the well-being of humankind without compromising the welfare and rights of others. However, the al-Ghazali's theory is well applied in the related studies and translated into institutional practice. To match this study, the scholars use Ibn Ashur's reinterpretation to translate the Maqasid theory of al- Ghazali as adapted by Mohammed et al. (2015).

The history of the development of Maqasid Shariah has a long discussion and story that involve many scholars. This development of Maqasid Shariah has contributed to the knowledge as the mechanism that may influence the performance of Islamic banks. It seems significant for the business organisation, of which currently the prior studies found that the Maqasid measurement has been developed for the financial

industry (Rahman et al., 2017). Similarly, to meet the study's objective, the current study adapted the application of al-Ghazali theory to examine the performance of Islamic banks.

2.4.1 Maqasid Shariah and the Performance of Islamic Banks

Maqasid Shariah's concept has been applied in the industry, and numerous studies were conducted to observe Maqasid Shariah's achievement. Align with the contemporary scholars' effort, the Maqasid Shariah subject has acquired more attention in academic and industrial practices and, as such, has yielded a positive Maqasid Shariah standard, application, methods, challenges, and relevance in the society (Shinfaki et al., 2017). The Maqasid Shariah is recommended in Islamic banking institutions because of the significant relationship between Maqasid Shariah and the objectives of business transactions where wealth must be protected to prevent incoming hardships from occurring in the society (Abd Rahman et. al, 2020). Mergaliyev et al. (2020) interpret the Maqasid Shariah as "achieving social good as a consequence in addition to well-being and, hence, it goes beyond traditional (voluntary) social responsibility". The literature has shown the growth and development of the Maqasid Shariah as current knowledge. However, Lesmana and Haron (2019) argue that the Islamic banks still do not fully apply Maqasid Shariah as an indicator and in their practices due to the lack of attention of Islamic Banks' managers.

Recently, numerous studies have been conducted concerning the Maqasid Shariah, including in the Islamic banking industry; however, it is still lacking (Ahmad & Ishak, 2020; Rahman et al., 2017; Razali et al., 2021). The Maqasid Shariah's achievements disclosure through social activities becomes the attention of stakeholders.

The disclosure of the Maqasid Shariah guides the Islamic banks' stakeholders to believe

that the banks are more concerned with their social welfare goals than with their commercial purposes (Iryani et al., 2019). Through the Maqasid Shariah disclosure, Islamic banks have revealed their responsibility towards the interest of stakeholders that may extend beyond the financial interest. It includes ethical, religious, and other welfare, even though ensuring the protection of the stakeholders requires a moral consciousness and commitment by many players in the market (Hasan et al., 2020).

Several studies were conducted on the Maqasid Shariah-based performance (Amaroh & Maturin, 2018; Arini et al., 2020; Asutay & Harningtyas, 2015; Iryani et al., 2019; Mohammed et al., 2008, 2015). Prior studies show that the Maqasid Shariah was applied to measure the performance of banks through its implementation and achievement. Accordingly, most researchers used the disclosure index in their studies of Maqasid Shariah to see the extent of its achievement. The elements of Maqasid Shariah in the IFIs are also frequently used to achieve a firm based on disclosure, which indicates an organisation that is committed towards the community. A study conducted by Said et al. (2016) examined the extent of Maqasid Shariah CSR disclosure in public listed companies. However, this study reveals that the Maqasid Shariah CSR disclosure index is generally low.

The Maqasid Shariah measurements were conducted based on the Maqasid Shariah index, which has been developed specifically for the financial industry (Rahman et al., 2017). For instance, a study by Mohammed and Tarique (2015) developed a Maqasid Based Performance Evaluation Model (MPEM) to measure the performance of Islamic banks. Syafii et al. (2012) applied the Maqasid Index approach as a measurement to indicate the performance of Islamic banking. Likewise, Asutay and Harningtyas (2015) also developed a Maqasid Shariah index to evaluate the social

performance of Islamic banks, while Mohammed et al. (2008) have proposed using the Maqasid Shariah to measure the performance of Islamic banks.

Meanwhile, the Maqasid Shariah disclosure in this study was developed to examine whether the achievement is associated with Islamic banks' performance. Hence, this study integrated the elements of CSR based on prior research that has formally discussed the Western perspective consistent with an investigation by Said et al. (2018) in a study of corporate social responsibility disclosure index of Malaysian Shariah-compliant companies. Likewise, Arshad et al. (2012) examined the effect of Islamic corporate social responsibility (ICSR) disclosure on corporate reputations and firm performance. The result of this study reveals that the ICSR disclosure is significantly positively associated with corporate reputations and firm performance.

Azmi et al. (2020) examined the effect of the Islamic social reporting index on Maqasid Shariah of Islamic banks through the annual report disclosure. They emphasised the stewardship theory as the bank's commitment to providing the best service to their customers and community to achieve the Maqasid Shariah. Concerning the ethical, social, and environmental dimensions, many studies also explored the determinant of social and ethical reporting of IB (Mergaliyev et al., 2019). In addition, a recent study examined the CSR based on Maqasid Shariah, providing a significant insight into the amount and nature of CSR among Islamic banks across sectors (Razali et al., 2021). Other studies explored the element of Maqasid Shariah through the Shariah governance practices and has revealed that the Maqasid have been realized through the practice of Shariah governance in Malaysia in two elements, namely, ensuring the viability of Islamic banking institutions and promoting transparency (Ahmad & Ishak, 2020).

Furthermore, Ahmad and Ishak (2020) explored Maqasid Shariah's elements via practising Shariah governance. The study on Maqasid Shariah by Arsad et al. (2015) assessed four corporate social responsibility mechanisms (CSR): Workplace, environment, community, and marketplace Shariah-compliant companies are in line with the objectives of Shariah. The author argues that organisations must show their accountability to the public even though CSR is only part of voluntary disclosure. The implementation of CSR is an obligation to Muslims as a Khalifah of Ummah. Many studies relate the Maqasid Shariah with CSR. CSR in an organisation addresses a firm's responsibility towards the community and environment, aligning with the Maqasid Shariah's concept. The environment and the community are interrelated in human life. Maqasid Shariah with regards the Al-Shatibi, views the *maslahah* as an essential element of human life by exercising the livelihood, development of emotional, intellectual, and practical life (Ahmad & Ishak, 2020).

Lesmana and Haron (2019) state that Islamic banks' performance has evaluated their social responsibilities in an Islamic framework. Through implementing a CSR program, the company can maximise the firm trustworthiness, and thus, support the relationship between stakeholders (Aguilera et al., 2007). However, some empirical studies support a negative relationship between CSR and financial performance by arguing that CSR projects raise administrative costs and cause financial burdens to corporations (Platonova et al., 2018). This argument is contrary to the Islamic view, where the Maqasid Shariah concept emphasises that humans need to support each other towards good deeds. Moreover, by understanding the concept of giving and sharing sustenance, Allah SWT will reward and replace what we spend with something better.

2.4.2 Harmonising the Corporate Social Responsibility's Elements with the Principles of Maqasid Shariah

Islamic banks play a significant part in the development of the national economy. Islamic Banks can empower employees, shareholders, and business partners by focusing on sustainable economic wealth. In addition, it can also contribute to the sustainability of state treasuries through the social development and increase the shareholder's and the entrepreneur's wealth where the economic contribution of Islamic banks can be seen in its contribution to general economic development and benefit the customers and society (Abdul Aris et al., 2013).

Islamic concept emphasises equality and justice in every aspect of life and requires Muslims to be good in their actions. Interest and personal gain is not the ultimate goal in the business transaction. Islam encourages good conduct in line with the faith because Islam promotes good deeds and directs humans to avoid harm. In practice, encouraging good deeds and avoid harm is consistent with the principles of Islam in achieving the Maqasid Shariah (Arsad et al., 2015; Esen, 2015; Haq & Wahab, 2019). The Maqasid Shariah has been discussed in many perspectives by researchers as a crucial element that always relates to human life. It includes the minor level of the individual, organisation, community, and universe.

The Maqasid Shariah, from an organisation perspective, particularly in Islamic banking, is widely discussed and studied at the academic and industrial levels. Many studies were conducted on the achievement of Maqasid Shariah by Islamic banks (Ahmad & Ishak, 2020). In line with optimising the Shariah-based system, the Maqasid Shariah aims to meet the needs of Muslims and promote human well-being by organising the activities and programs and emphasising all stakeholders, such as employees, customers or users of Islamic banks and the community.

Islamic banks have provided a Shariah-compliant system, encompassing a general understanding of usury elimination, trade, and efficiency incentives. It also emphasises social objectives, such as social justice and environmentally friendly monetary policy, thus, advancing a human-oriented approach that encourages public participation and the state and private sectors (Sairally, 2013). These understandings and values aim to meet all parties' expectations in the context of Shariah to encourage a more excellent vision in promoting human well-being based on the Maqasid Shariah achievement that potentially serves the social interests better (Dusuki & Abdullah, 2007). In addition, the religious factor guides the philosophy and principles of Islamic finance (Sairally, 2013). The Islamic finance paradigm is identified by the Maqasid Shariah achievement. It leads to a comprehensive Islamic view and positive response to the IFIs through the CSR programs and an effort to achieve Maqasid Shariah. Moreover, Islam covers the elements of *aqidah*, *akhlak*, and *fiqh*, which is the fundamental that is unlikely to change according to the current situation and developments, which is in contrast to worldly related activities that require changes and flexibilities depending on current developments (Dusuki & Abdullah, 2007; Kamali, 1989).

In general, CSR was born out of an organization's concern for the impact of its actions on the society's well-being (Carroll & Buchholtz, 2006). Through the CSR program, the companies can gain an advantage from the activities and the program organised by the company. This advantage can be obtained depending on the ability to communicate and deliver information regarding the company's achievement and performance to the public (Mamun et al., 2017). Thus, CSR activities become a subject to be highlighted by the company in their corporate report as part of its program. The concept of CSR embeds the ethical and values practices in assisting the social or the environment for human sustainability as part of a firm's responsibility. CSR in an

organisation is an obligation beyond the law requirement to portray their commitment in contributing their roles to meet the interest of the public and all stakeholders (Arsad et al., 2015). In addition to the compliance with the governmental policies and reforms, Islam also necessitates the welfare of the individuals, society, environment, and universal creatures compatible with the Islamic teaching (Rehman et al., 2020). Even though CSR is a voluntary program, it is an integral part of a firm's activities in contributing to social and environmental awareness.

In addition, a theoretical perspective has examined the roles of CSR and the importance of disclosure to the firm's performance. It is one of the primary obligations of Islamic banks as a form of Islamic banks accountable to God and human beings (Ridwan & Mayapada, 2020). The CSR and its disclosure are considered as a firm being accountable for managing its activities to acknowledge the society and the environment where it operates (Ahmed & El-belihy, 2017). This effort will benefit the firm to increase confidence, build reputation, and improve competitiveness in the business field. Consistently revealing the CSR activities in the company's report is a way to promote a firm's business that illustrates the positive contribution to society. However, in Malaysia, Bursa Malaysia has made it mandatory for the publicly listed company to disclose CSR activities in their annual reports. Disclosing the activities in the annual report as a medium of communication represents the company's accountability to the public, strengthens its reputation, and increases the connection in government and other private organisations as they show the responsibility to the society (Baba, 2017). Thus, CSR becomes an obligation of every organisation to show their accountability toward the society (Arsad et al., 2015).

Besides CSR, an organisation's commitment can be translated as sustainability development, which relates to the company's responsibility towards society and

environmental awareness. Schaltegger and Wagner (2006) addressed sustainability performance management's social, environmental, and economic aspects related to three management frameworks: Connecting environmental and social management with competitive strategy and management as well as integrating the environmental and social information with financial business information and sustainability reporting.

Therefore, the concept of CSR that embeds ethics and values is aligned with the requirement of Islam. Islam encourages its followers to help each other with good things and not support evil. The value of society in safeguarding the rights of these individuals has been translated into the concept of Maqasid Shariah in safeguarding universal well-being. The CSR activities focus on the welfare of the society at large that serve the objectives of Shariah (Tarique et al., 2017). Arini et al. (2020) transformed the elements of sustainability into the Islamic perspective, which is translated as Maqasid Shariah achievements. Meanwhile, Said et al. (2018) argue that the concept of CSR fixes the Maqasid Shariah spirit. From an Islamic perspective, CSR is a set of operation-based activities aiming to achieve Maqasid Shariah. Therefore, all the activities, transactions, and programs provided will contribute to the human well-being that act as worship, of which Allah SWT will count.

In line with the objective of SCR, the principles of Maqasid Shariah benefit the interest of the individual and community towards the improvement of life and protection as a duty of Muslims (Arsad et al., 2015). In this regard, realising and understanding the concept of Maqasid Shariah by the individual or the organisation has mirrored the idea of *ta'awwun* among Muslims; it is consistent with the principles of CSR, which implementation has framed the business ethics by addressing morally right and wrong in the business context (Ahmed & El-belihy, 2017). Furthermore, this argument has been theorising that CSR can be defined as a firm being accountable for managing its

activities by acknowledging society and the environment in which it operates (Ahmed & El-belihy, 2017).

Moreover, several researchers argue that the theory promotes social commitment by emphasising socioeconomic goals, such as social justice, equity, cooperation, poverty alleviation and human well-being that inevitably have recourse to the Maqasid Shariah (Sairally, 2013). Furthermore, the dimension of CSR is consistent with the concept of Islamic teaching to achieve Maqasid Shariah based on the Quran and sunnah (Arsad et al., 2015), which is also stated in a study by Mohammed Shamim and Md. Nesarul (2011).

Table 2.2: Reinterpretation of Ibn Ashur and Maqasid Dimensions

Al-Ghazali Maqasid Dimensions	Ibn Ashur's Interpretation	Traditional non-financial dimensions	
Preservation of faith	Freedom of faith	Shariah-complaint Product/service	
Preservation of life	Preservation of human dignity Protection of human rights	Employee's welfare	Maslahah (Arsad et al., 2015; Ahmad & Ishak, 2020)
Preservation of intellect	Propagation of scientific thinking Avoidance of brain drain	Employee's development, knowledge, e.g., training for employees	
Preservation of Progeny	Care of family/ stakeholders	Stakeholder's right (privacy)	
Preservation of wealth	Wellbeing of society Minimising income and wealth disparity Source of income Environmental awareness	Utilising the wealth - Community/Social responsibility	

Source: Adapted from Mohammed et al. (2015)

Therefore, the discussion of CSR is more advanced than Maqasid Shariah in its implementation and achievement within the organisation's scope. Nevertheless, the essential function of CSR implementation in Islam is Shariah. Shariah applies values and ethics in all aspects of human life, such as individual, social, political, economic,

and intellectual (Tariq et al., 2017). In addition, Zinkin (2007) contends that Shariah is a legal framework inculcated with values and morals different from secular views, in which ethics and law are separated. The meaning of justice is the core of Islam that strengthens the relationship between business activities and justice that occurs in Islam as an essential element for equitable distribution of wealth between the rich to the needy (Graafland et al., 2006). Hence, Islamic financial institutions should promote Maqasid Shariah in order to establish justice, equity, and equality in society. This is following the Maqasid Shariah elements discussed in the scope of IFIs related to the interest of Islamic banks' stakeholders, the Muslims, the society, and the environmental sustainability.

2.4.1.1 Product and Service

In Islamic banks, providing the Shariah-compliant products and services is a core Islamic banking business. The Shariah-compliant system is fundamental in IFIs to serve the Muslims with the Shariah-compliant products, avoiding uncertainty, and protecting the consumers from the interest in the transaction. Islam strictly prohibits the elements of non-halal sources from being consumed by Muslims. Any consumption from prohibited elements will affect the worship of Allah SWT. Therefore, abidance with the relevant legal maxims to develop rulings related to financial products can be related to the Maqasid Shariah achievement at the transaction level that binding under the legal requirement (Ahmed, 2011).

Moreover, it is essential to develop products to achieve the goals of Shariah, and at the same time, meet the economic needs of society (Al-Salem, 2009). It is adhering to the principle of Islam by executing all the commands and leave all the prohibitions.

This Shariah-based practice implies divine rules by avoiding elements of usury (*riba*),

uncertainty (*gharar*), gambling (*maisir*) and the things that are categorized as forbidden in Islam, such as alcohol and pork (Rosly, 2010; Siddiqui, 2008). Thus, this institution promotes the Islamic-based system to fulfil the Muslim community's needs to avoid oppression and injustice. This facility might preserve the Muslims from dealing with Shariah non-compliant elements and other prohibited matters in Islam and allowed them to practice according to their religion.

From an Islamic banking perspective, creating Islamic-based products to fulfil the need of Muslims is a commitment to achieve the Maqasid Shariah. The Maqasid Shariah achievement can be seen through the product development by emphasising the Shariah-compliant product and services. Shariah-compliant products and services bind with the contract as a legal requirement to serve the Muslims' needs (Ahmed, 2011). Thus, the Islamic finance products as guided in the *Fiqh Muamalah* must be based on prudential principles, in which that the products should comply with Shariah principles (Qoyum, 2018). The Shariah contract between seller and buyer is a prerequisite to the two parties' validity as part of the legal requirement. In addition, the contract (*'aqd*) needs to be emphasised and conducted in the transaction. Therefore, the status of Shariah complaint is only recognised when the organisation has fully complied with the contract's requirement at hand (Rosly, 2010).

Regarding Maqasid Shariah, Ahmed (2011) identified three types of Islamic financial products; i) A Shariah-based product fulfils both the legal and social requirements, ii) A Shariah-compliant product would be one fulfilling the legal requirements, but not the social requirements, iii) A pseudo-Islamic product fulfils the form but not the substance of Islamic law. Hence, it is significant for IFIs to determine the right product to ensure that the Maqasid Shariah is achieved at the contract level, according to Shariah.

However, the effort in developing products compliant with Shariah has become a significant challenge for the industry. It is aligned with Al-Salem's (2009) opinion that the Shariah-compliant products need to be maintained in the market. The product and services are developed continuously by focusing on the quality and diversity of products and services by Islamic financial.

2.4.1.2 Employee's Welfare

A welfare scheme is an initiative that needs to be provided by an organization to increase the healthcare, comfort, and safety of employees. This initiative can improve employees' loyalty and productivity in performing tasks. Augustus-Daddie et al. (2018) classify employee welfare schemes into two categories, namely, statutory, and non-statutory. The statutory scheme refers to a mandatory scheme to be provided by an organization based on employee health and safety laws. In contrast, non-statutory schemes differ between one organization, as well as one industry with another.

In the Maqasid Shariah of an organisation in this study, welfare refers to preserving life, protecting people and humanity (Esen, 2015). Preserving life can be achieved by serving the individual with the basic needs. The basic needs or necessities include food, health, clothes, and home. This basic need can be interpreted as the employer's commitment concerns towards the employees in an organisation. It is not a single study explored and discussed empirically or conceptually in academic research concerning the employees' welfare. It has been discussed broadly in CSR studies and in this subject (Aribi & Gao, 2010; Haniffa & Hudaib, 2007; Platonova et al., 2018). The former was studied by Haniffa and Hudaib (2007) in their study titled "Ethical Identity of Islamic Banks via Communication in Annual Reports" where they developed the ethical identity index.

The welfare provided by the employer, such as health care, insurance, retirement program, workplace condition, and safety as Esen (2015), Md Zain and Shafii (2020), and Razali et al. (2021) classify the healthcare as a protection scheme, security, and emphasising safety. This welfare will encourage the employees to perform and motivate them to feel secure at the workplace (Md Zain & Shafii, 2020). In an organisation, the employees' welfare is essential because it helps keep the workers' morale and motivation to enjoy the working environment. The welfare of employees includes psychological, economic, moral, cultural, and intellectual development, making them good workers, good citizens, and good family members. In line of this notion, the finding from a study by Tep (2015) reveals that incentives are significant in encouraging and motivating employees to work harder, perform better, and effectively achieve organizational goals. However, Tep (2015) also argues that job-related support and organizational support are preferred as incentives to increase public employees' interest in their work and workplace.

Furthermore, the welfare in this prior study relates to certain facilities provided by an organisation, including the housing, transportation, medical, knowledge accessibility, and wellness program. Several studies examined the relationship between employee's performance and employee welfare benefits and services. For instance, a study reveals that poor employee benefits, including healthcare, transportation, education, and the workplace, caused reduction and low worker productivity (Waititu et al., 2017). Moreover, Agusioma et al. (2019) opine that the staff welfare is consistent with the human capital theory to ensure a proper human resources practice and optimum work performance.

2.4.1.3 Employee's Development (Knowledge and Training)

Maqasid Shariah plays an essential role in enhancing intellectual reform's social abilities and qualities and civilization renewal (Monzur-E-Elahi as cited in Qoyum, 2018). Knowledge is essential for individuals to preserve their minds and direct them to act rationally, especially in making decisions. Shariah also encourages people to seek knowledge for intellectual development. Seeking knowledge is crucial in Islam as Allah SWT raises humans' status who pursue knowledge.

In Islamic banking, Shariah matters become the main feature to serve the need of Muslims. Knowledge and experience are essential in ensuring that the Islamic policies held by Islamic banking are always based on the Shariah. Thus, the employees' development is a program that can enhance employees' knowledge and experience to perform in Islamic banking institutions. The institution is responsible for providing its employees with knowledge (Asutay & Harningtyas, 2015). The knowledge, such as training and development program will expose the employees to new information and enhance their thinking level. The knowledge exposure may also lead the employees to work independently and create the ability for decision making. For instance, in IFIs, the SC is selected based on knowledge and experience in a related field. They are also provided with the training to enhance their knowledge, especially in banking and finance. The Shariah knowledge and experience of SC are critical elements due to the responsibility and duty that determine the progress of Shariah-compliant matters.

In addition, besides formal knowledge, skills are also essential in a workplace. Kum et al. (2014) argue that training should be implemented to improve individual performance and enhance productivity, affecting the quality of work and corporate image. The efforts towards knowledge enhancement are the basis of the development of an organization that will benefit the organisation's effectiveness. An organisation

often implements this effort to improve work effectiveness, learning, and support technologies that facilitate knowledge (Abuazoum et al., 2013).

2.4.1.4 Stakeholder's Right

An individual or a party who deals with a company can be classified as a stakeholder. The individual stakeholders are those affected by any action, objective, or policy of the organisation. Hence, stakeholders include creditors, directors, employees, suppliers, and shareholders (Wikipedia, 2018). The stakeholders right refer to the right of parties related to an organisation. The protection of progeny includes protecting individuals' rights and respecting their privacy and respect and responsibility among different genders (Afridi, 2016). Employers need to consider their employees' rights by protecting them from harm and emphasising privacy, including anything that could bring down their dignity. In this context, the right to serve the interests of employees regardless of the level and position by treating them equally and promptly responding to the enquiry (Arsad et al., 2015). Likewise, Razali et al. (2021) also highlight that the workers need to be treated fairly and that their rights are respected. Moreover, Islam has encouraged protecting the dignity of humankind by prohibiting acts that can embarrass others physically or mentally (Afridi, 2016).

In an organisation, employers are responsible for protecting employees' privacy, but every individual must care for his dignity and safety. They must also safeguard the rights of other individuals and respect each other. For instance, the behaviours that can tarnish the image and self-esteem of others, such as slander, sexual harassment, and bullying will cause a person to experience depression, and cause resentment and revenge. An organisation should avoid activities that can harm the society and work for the betterment and welfare of the society (Tariq et al., 2017). Indeed, Islam forbids

behaviour that can harm oneself or others. Islam punishes those who commit an offence or crime. Each country has its laws to safeguard the country and society's interest, preserve human rights, and prevent crime from any perspective at all. The law is also created to preserve the people and nature to achieve the well-being of life. Every law created revolves around the damage done by the society itself. Indeed, the laws and punishment could prevent and teach the offender or the individual from repeating the mistake.

In this context, the organisation needs to consider the stakeholder's rights. They can affect or be affected by any action of an organisation. Each stakeholder, such as shareholders, customers or employees, is playing their roles to enhance the business activities. Preserving dignity has been categorised at the necessary level in Maqasid Shariah, which is in line with Islam. It emphasises the interest of communities and individuals towards the dignity that should be preserved to avoid the enormous consequences and preserve the individual, society, or the generation born (Afridi, 2016), which eventually will affect the country and ummah. Therefore, fostering a sense of responsibility may enhance the company's reputation and provide it with greater legitimacy in the eyes of the stakeholders (Tariq et al., 2017).

2.4.1.5 Environmental and Social Responsibility

Islamic finance is a component of Islamic economics that has been translated as Maqasid Syariah. The Islamic financial system based on the principles of Maqasid Shariah has promoted welfare to the society and nurtured it with community activities (Ahmed, 2011). In Islamic institutions, mainly Islamic banks, promoting the Maqasid Shariah has become a platform to deliver their concern especially to the community by providing aid, contributing to the needy through distributing *zakat* and *sadaqah*,

improving health, providing education, and enhancing social development (Abdul Aris et al., 2013). They deliver their responsibilities to the society through these contributions to improve the socio-economy.

Preservation refers to where the wealth is being used and expands its wealth other than business expenses. Islam encourages wealth to be used and managed wisely. For instance, sources need to be well managed to avoid wastage. They need to be distributed and mobilised wisely and through the right channel for the well-being and human development. For example, Muslims are required to pay zakat based on specific requirements and encourage charity. The rich need to circulate a portion of their wealth for zakat. They are also encouraged to give to the poor or needy as charity. Meanwhile, in the Islamic financial system, mainly, Maqasid Shariah is usually associated with the element of *riba* that needs to be eliminated in preserving the faith of Muslims from engaging with illegal activities. However, in this system, Maqasid Shariah is also emphasized to promote the circulation of wealth in the society, sustainability on investment and disbursement, provide economic prosperity for society to satisfy their needs, and transparency in managing wealth (Hurayra, 2015; Qoyum, 2018).

Moreover, for society's development, the organisation can contribute their wealth to build the nation by providing education or campaign or providing the facilities for human development. Other than that, the effort to preserve the environment is the company's social responsibility. A clean environment will affect the life of humans and other beings.

2.4.3 Maqasid Shariah Measurement

The recent study conducted by Rusydiana and Al Parisi (2017) measured the performance of Islamic banks. The study constructed the weighting Maqasid Shariah

index based on Mohammed et al.'s (2008) Maqasid Shariah measurement, which successfully developed the performance measures based on the Maqasid Shariah model of Abu Zaharah's classification as the basic Islamic bank's primary objective. Likewise, Mohammed et al. (2015) developed Maqasid Based Performance Evaluation Model (MPEM) to measure the performance of Islamic banks.

The terms of Shariah mechanism have been successfully studied by measuring the performance. Commonly, researchers used disclosure indexes by collecting all related Shariah matters to measure the performance of Islamic banks. Mohammed et al. (2015) developed the Maqasid performance evaluation model to evaluate the performance of Islamic banks. The study relates to five dimensions of Al-Ghazali's theory: Preservation of religion, life, intellect, progeny, and wealth to their five respective elements into a reinterpretation of Ibn Ashur's Maqasid theory.

The Maqasid Shariah disclosure was constructed in this study to examine the relationship with financial performance. Maqasid Shariah disclosure items were developed to measure the Maqasid Shariah disclosure. The Maqasid Shariah in this study interprets the Maqasid Shariah's Ibn Ashur theory, synthesises the elements of CSR, and harmonises them in the Maqasid Shariah. Further, based on Maqasid Shariah mechanisms, the study harmonised five elements into five classifications, as presented in Table 2.3.

Table 2.3: Classification of Measurement According to Maqasid Shariah

Maqasid Shariah	Classification of measurement
Preservation of faith	Product/ Service (Riba Free)
Preservation of life	Employee's welfare
Preservation of intellect	Employees/society development (Knowledge/training for employee)

Table 2.3 Cont.

Preservation of progeny	Stakeholder's rights and privacy (Shareholders, customers, employees, and government servants).
Preservation of wealth	Contribution-wellbeing of society and environmental awareness

Another study was conducted by Asutay and Harningtyas (2015) using the Bedoui's (2012) formula to calculate the Maqasid performance to measure Islamic banking and finance's social performance. The above study was divided into four key objectives: Safeguarding human life, human self, social, and physical environment. Then, it diverged into eight consequences to develop the dimension. The study used the Simple Additive Weighting (SAW) concept, and the analysis of the study was conducted at three levels: Bank level, country level, and industry level. At the bank level, the highest score was performed by the Indonesian bank. The other study by Ali and Hasan (2014) developed a Maqasid Shariah index to indicate dimensions by proposing a family of multidimensional measures.

2.4.4 Summary of Prior Studies on Maqasid Shariah

Following Table 2.4 shows the summary of prior studies on the Maqasid Shariah.

Table 2.4: Summary of Prior Studies on Maqasid Shariah

Author/years	Elements of study	MS (Faith/ life/ intellect/ Progeny)/ other elemets	Other elements
1 Razali et al. (2021)	The study's objective was to examine the extent of CSR based on Maqasid Shariah in terms of four dimensions.		Classified Maqasid Shariah in four perspectives, namely, workplace, environment, society and marketplace.
2 Abd Rahman et al. (2020)	Looking into how the Islamic legal maxims could provide a basis for Shariah audit practices to assist the institution's managerial practice to achieve Maqasid Shariah.		
3 Duguri et al. (2021)	Exploring the application of Maqasid Shariah in the foreign policy of Islamic states.		Discussed in general perspective. Not specified the specific Maqasid Shariah elements.
4 Arini et al. (2020)	This study examined the effect of sustainability reports on the performance of Maqasid Shariah in Islamic banks.		Education, Justice, Welfare
5 Ahmad & Ishak (2020)	This study explored how far the element of maqasid al-Shariah is realised through the practice of Shariah governance in Malaysia.		
6 Azmi et al. (2020)	This study aimed to analyse the effect of the Islamic social reporting index moderated by Sharia compliance on the Maqasid Shariah index.		Individual education, creation of justice, and attainment of welfare (Mohammed & Razak, 2008)
7 Md. Zain & Shafii (2020)	Discusses five elements of Maqasid Shariah in IFIs perspective.		
8 Iryani et al. (2019)	Assessing the effect of financial performance on Maqasid Shariah performance with Shariah governance as a moderating variable.	Zakat, infaq, sadaqah and awqaf, and qordhul hasan.	
9 Kurniawati et al. (2020)	This study's primary objective was to develop Shariah governance and MAqasid Shariah models in improving the performance of SMEs in Surabaya, Indonesia.	Individual education Justice creation Achievement of the public interest	
10 Tarique et al. (2017)	The research focuses on the CSR activities of the leading Islamic bank. The analysis was performed according to the levels of Maqasid Shariah (necessities, complements, and embellishments)	(Necessities, complements, and embellishments)	

Table 2.4 Cont.

11	Rusydiana & Al-Parisi (2016)	This study aimed to measure the Shariah Maqasid Index and the Profitability Index of Islamic banks and compare the Syariah Maqasid and Profitability Index (iv).	Educating Individual, Justice, Public interest
12	Mukhibad (2016)	The research was to prove whether the CG, SSB, and Corporate Ethics have contributed to the achievement of Maqasid Syariah (iv).	Maqasid Shariah performance

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Table 2.4 present the analysis of prior studies on Maqasid Shariah. The literature shows that many studies were conducted on the Maqasid Shariah. It reveals that the study on Maqasid Shariah had been conducted as the independent variable. Most Maqasid Shariah studies measured the performance using the Maqasid Shariah performance index based on the three elements, namely, individual education, creation of justice, and attainment of welfare or social interest (Mohammed et al., 2008). In addition, several studies used the social contribution elements, such as *sadaqah*, *zakat*, *infaq*, *awqaf*, and *qard hassan* as the elements of Maqasid Shariah.

In contrast, this study discusses the Maqasid Shariah based on the five classifications developed based on the Islamic bank's perspectives. The Maqasid Shariah elements include preservation of faith, preservation of life, preservation of intellect, preservation of progeny, and preservation of wealth (See Tables 2.2 and 2.3). This study also developed the Maqasid Shariah items based on the CSR elements discussed in subsection 2.3.2. Moreover, unlike the previous study, this study constructed the Maqasid Shariah as the independent variable instead of dependent variables. The Maqasid Shariah as independent variables were to test the relationship with the performance, to find out whether the Maqasid Shariah achievement may influence the Islamic banks' performance.

2.5 Board of Directors and the Performance of Islamic banks

In a corporation, corporate governance is a critical factor in moving the whole organization. At the same time, the banking industry has a higher level of inclination and importance to corporate governance. It is related to the bank's function in carrying out its responsibilities in handling public savings, which require the community's trust and the involvement of a broader range of stakeholders. There have been many events

reported and discussed in finding the solutions and causes to the failure of a large company; however, most will relate to corporate governance problems (Chang & Leng, 2004; Cormier & Magnan, 2014). It is found that poor governance has led to the collapse of an organization. Likewise, banks were found to be going through the same crisis, i.e., poor governance led to the collapse of these organizations during the crisis. In addition, financial scandals involving owners and management can have a systematic impact on the economy. In Islamic banking, a greater attention should be given as Islamic banks are exposed to more risk of non-compliance and the weak new market institutional environment in which most operate (Chik, 2012; Chowdhury & Shaker, 2015).

Furthermore, investment depositors appear to be part of the agency conflict in Islamic banks. They participate in profits and losses like shareholders, creating much-needed proper governance mechanisms to protect their interests and maintain their confidence. Due to the various stakeholders of the bank, such governance mechanisms need to be disseminated and disclosed in corporate reports (Darmadi, 2013b). Thus, the BODs is considered an important tool to protect shareholders and help control managers when they try to maximize their interests at the expense of the company's profitability (Khanifah et al., 2020). Essentially, the function of the BODs is to ensure an effective system of internal controls is laid down and conscientiously observed (Chapra & Ahmed, 2002). In addition, implementing the company's strategies starts with the BOD to achieve its goal and maximise its profit (Muhammad, Mengawing & Salsabilla, 2021). The BOD is a key factor in corporate governance to reduce conflicts between shareholders and management and avoid conflicts of interest between banks and regulators (De Andres & Vallelado; Klein, as cited in Srairi, 2015). Therefore, the board and management must be united in promoting integrity and creating it as a culture at all

levels to understand the importance of discharging responsibilities honestly and efficiently (Chapra & Ahmed, 2002).

Concerning the mediator's function in this study, the single corporate governance seems to be not enough to explain the Islamic banking sector's value creation and stability (Nawaz, 2017). Thus, with the BOD as an intermediary, this study was conducted to test Shariah governance and Maqasid Shariah in influencing the performance of Islamic banks. Furthermore, this study highlights the roles of the BOD, consistent with the agency theory. The agency theory refers to the relationship between the BOD and shareholders. The agency theory states that the roles of the BOD are crucial to meeting the expectations of the principles on their behalf to lead and make decisions (Borlea & Achim, 2013). In Islamic banking, the BOD is responsible for the decision-making, while the roles of Shariah governance are to ensure all the activities comply with Shariah. However, the BOD may lead to higher monitoring that may maximise the company's value. Still, in terms of the BOD, the company's performance depends on the corporate governance indicators' attributes (Bukhair & Rahman, 2015), as the characteristics of the BOD, such as BOD size and BOD independence have been widely addressed in either theoretical or empirical research (Darmadi, 2011a).

2.5.1 BOD Size

BOD Size refers to the total number of directors, including the CEO and chairman, for each accounting year (Shakir, 2008). Concerning BOD size, autonomy, structure, and effectiveness, the characteristics of the Board have been widely analysed in both theoretical and empirical research (Srairi, 2015). The size of a board is one of the factors that influence the effectiveness and performance of an organisation (Khanifah, 2020). Thus, it is crucial to determine the appropriate BOD size to ensure

the effectiveness of its functions (Agoraki et al., 2010; Gavrea & Stegorean, 2007; Samuel, 2012). In a study, Htay et al. (2013) related the agency theory and the BOD size and explained that the larger Boards are unnecessary and effective. BOD size is widely used in the studies on corporate governance and performance; according to the agency theory, the smaller BOD size may associate with firm performance (Agoraki et al., 2010; Isik & Riza Ince, 2016). It has also been examined that a smaller BOD size will result in better communication, management, and better disclosure quality (Htay et al., 2013).

In addition, Uwuigbe and Fakile (2012) argue that the board consisting of many members would assist with the agency problems and opine that a smaller BOD size could provide a better financial performance and reduce the problem of free-rider banks in Nigeria. Isik and Riza Ince (2016) indicate that the BOD size significantly positively affects financial performance. Meanwhile, Gavrea and Stegorean (2007) found that the BOD size has a negative and significant correlation with ROA and ROE. This result suggests that a smaller BOD size produces a higher performance for the firm. It indicates that the larger BOD size would lead to a lower ROE and ROA (Bebeji et al., 2015). Likewise, Uwuigbe and Fakile (2012) found a significant negative relationship between BOD size and bank financial performance. Based on their observation, the banks with BOD sizes below thirteen are more effective than those above thirteen. This result indicates that banks with larger BODs recorded profits lower than those with smaller BODs.

In contrast, Al-Saidi (2013) found an insignificant relationship between BOD size and bank performance. Due to the absence of corporate code in Kuwait, they conclude that the smaller BOD size may be manageable for coordination and communication, leading to an effective monitoring and fewer risks, improving bank performance. This

study finally implies that the smaller board structure is associated with better bank efficiency through better credit risk management. The study by Agoraki et al. (2010) examined the relationship between BOD size and banks efficiency, which was measured in terms of cost and profit efficiency. They infer that smaller boards are more efficient and directly present the negative correlation between BOD size. This study implicates that larger BODs are usually associated with more intense coordination, communication, and process problems.

The study by Guest (2009) on the relationship between BOD size and firm performance with a large sample size in the UK found that the BOD size has a negative impact on firm performance measured using profitability, Tobin's Q, and share return. This result implies that the large BOD size is more likely to reflect problems in carrying out the advisory role than the monitoring role. That is consistent with a few other extensive BOD size studies facing less effectiveness, considerable coordination, communication and decision-making, and the excessive risk of CEO. Meanwhile, Hassan (2013a) reported a negative relationship with firms' performance, measured by accounting-based measures, and increasing the BOD size will decline the firm's performance. Hassan (2013b) revealed a negative and statistically significant relationship between the performance of Jordanian banks and bank size.

Shakir (2008) found that the relationship with market performance has a consistent negative relationship with Tobin's Q, suggesting that the smaller BOD size would be more effective in monitoring. The study by Sanda et al. (2005) on corporate governance mechanisms and firm financial performance in Nigeria reveals that the BOD size is significantly and positively related to the firm performance. This study points out that the large BOD can affect the firm. This result is consistent with the study conducted by Aljifri and Moustafa (2007). The study conducted in Vietnam by Drobetz

and Drobetz (2003) indicates that BOD size does not reflect the company's role and has not reflected the performance.

Consistent with a study conducted by Haider et al. (2015), increasing BOD size will produce better performance, indicating that larger BODs encourage and appreciate accountability and transparency to maximize firm performance. However, many empirical studies suggest that large BOD size is hard to manage and less effective due to the accruing of the different costs and the procrastination of some critical decisions (Gavrea & Stegorean, 2007). In addition, Al-Baidhani (2014) opines that larger BODs seem less efficient due to the slow pace of the decision-making and the difficulty in arranging BOD meetings and reaching consensus.

The other study conducted by Al-Saidi (2013) analysed the relationship between BOD composition and bank performance using the sample of nine listed banks in Kuwait sample between 2006 and 2010. The result found an insignificant relationship between BOD size and bank performance using the market measure due to the absence of corporate code in Kuwait. The empirical results indicate that BOD size is positively related to firm performance. The increasing BOD size has increased its profitability, such as the study by Chaghadari (2011). Finally, the study by Ahmed Sheikh et al. (2013) investigated whether internal governance mechanisms affects the performance of Pakistani firms.

2.5.2 BOD Independent

In an organisation, the BOD carries out the crucial roles in providing a clear direction for the management in determining the effectiveness of Islamic banks. An independent directors' existence can influence the profitability of Islamic banks (Muhammad et al., 2021). The BOD consists of three types of directors, namely,

executive director, non-executive director, and independent director. According to BNM (2013),

- 1) Executive director: A staff of an Islamic bank on payroll and employed under a service contract and involved in the Islamic bank's day-to-day management responsibilities.
- 2) Non-executive director: Not a staff of an Islamic bank and not under the Islamic bank's payroll. He is not involved in the daily management of the Islamic bank.
- 3) Independent director: A director who is independent of management and free from any business or other relationship, which could interfere with the exercise of independent judgement or the ability to act in the best interest of the Islamic bank.

BOD composition is related to the BOD independence, diversity of BOD members, and CEO duality. In contrast, BOD independence refers to the independent directors entrusted by shareholders to represent them and help reduce agency problems, consisting of independent outside directors (Fuzi et al., 2016). Clifford and Evans (1997) define the independent director as outside directors who have no affiliation with the firm except their directorship. Further, they classify the non-executive director as the number of independent non-executive directors on the board relative to the total number of directors (Bebeji et al., 2015), as in the study conducted by Sheikh and Kareem (2015). Ghaffar (2014) refers to BOD independence as the number of outside non-executive directors present in the bank's board.

BOD independence has been widely addressed in either theoretical or empirical research (Darmadi, 2011a; Muhammad et al., 2021; Shatnawi, 2020). As most previous studies were conducted, the BOD composition was seen as having a significant relationship with the firm's performance. A recent study by Isik and Riza Ince (2016)

shows that BOD composition correlates with bank performance in Turkish. The study conducted at the listed bank in Nigeria found a significant relationship between BOD composition and the performance of banks; this reveals that the independent outside directors perform better than others because they must protect their reputation as influential independent decision-makers (Bebeji et al., 2015). Ghaffar (2014) found a significant relationship between BOD independence and profitability, and the author concludes that increasing the number of outside directors will increase bank profitability. According to Htay et al. (2013), more independent directors will result in better disclosure quality, consistent with Norita and Shamsul Nahar's (as cited in Htay et al., 2013) study.

In contrast, the study conducted by Sheikh and Kareem (2015) indicates that the BOD composition non-executive director has no significant relationship with the financial performance of Islamic commercial banks in Pakistan. Likewise, Hermalin, and Weisbach (as cited in Uwuigbe & Fakile, 2012) conclude that the BOD composition is not associated with corporate performance. Agoraki et al. (2010) measured BOD composition using cost efficiency and profit efficiency. The result of the study reflects a negative relationship between BOD compositions and cost efficiency, while profit efficiency indicates an insignificant relationship. Likewise, Brick and Chindambaran (2007) state that BOD independence and bank size have adverse and significant effects on ROA. Meanwhile, Brick and Chindambaran (2007) argue that the increase of BOD independence could reduce the incidence of corporate fraud. Likewise, according to Weisbach (1988), the independent boards are likely to replace poorly performing management.

2.5.3 BOD Meeting

The BOD meeting is one of the elements of corporate governance indicators that commonly relates to a firm's performance. The BOD meeting is referred to the number of BOD meetings conducted in a year. Most empirical studies found that the BOD meeting has a positive and significant effect on financial performance. The frequency of BOD meetings can assist the board members to engage with members and allow them to discuss and understand the bank's operations in performing the board tasks appropriately. Al-Baidhani (2014) states that the variation of meeting across firms could better represent the degrees of monitoring across firms. In addition, increasing BOD meetings is an inexpensive way to increase the firm value (Giannarakis, 2014). Moreover, the meeting frequently conducted among the board gives the members a chance to share the information, raise the job and work distribution issues, and discuss the assignment (Laksmana, 2008).

Following a prior firm performance study by Vafeas (1999) contends that the number of annual BOD meetings is related to and improves the firm's performance (Brick & Chindambaran, 2007). This result is consistent with an argument by Gavrea and Stegorean (2007) that a higher frequency of BOD meetings allows better monitoring activities. In addition, Giannarakis (2014) concludes that a frequent BOD meeting enables management to manage better business operations.

2.5.4 Muslim in BOD

The study on the Islamic organisations consistently emphasised religion as contributing to the organisation's performance. They argue that the religious background is a factor that influences an Islamic institutions' performance due to religious background that may influence the decision and action based on beliefs. A

firm's performance is not restricted to financial health, but the religious factors may contribute to the ethics that every religion brings values. The Shariah has specified that Muslims must follow the guidelines and apply Islamic values in all aspects of their lives and every affair (Jaballah; Nomran as cited in Shatnawi, 2020). Moreover, the board with religious background knowledge has an advantage in knowledge related to the financial system and Shariah.

Generally, previous studies have proven that religion can influence corporate decisions (Shatnawi, 2020). The composition of Muslim BOD in an Institution believe that the direction and the Islamic values would influence their actions based on their beliefs. This value is significant to explain the variation in transparency, specifically, the corporations that portray a more outstanding commitment to applying Islamic values into their operations and work by involving greater corporate governance disclosure (Albassam & Ntim, 2017). This argument is consistent with Hassan et al. (2015) study on BOD diversity. It also mentions religious beliefs as one of the mechanisms that could enhance firm value because diversity forces directors to explain their ideas logically, which leads to better communication in decision-making. Muslim managers believe there is a commitment to be responsible to their stakeholders and believe they are held accountable by Allah SWT (Shatnawi et al., 2020). He found that a higher number of Muslim directors on the board would result in a higher quality of accounting information than the non-Muslim directors.

Yusoff (2010) states that corporate board diversity improves decision making, policies, procedures, and business networking. In contrast, in his study, Shatnawi (2020) revealed no positive relationship between the number of Muslim directors on the board and the corporate performance of Jordanians where the study was conducted in industry and service listed companies. The influence of religion is more pronounced, and as a

result, it becomes more important in management practices than in any other setting (Baydoun, et al., 1999).

Religion can influence managers' behaviour and attitudes (Baydoun, Mamman, & Mohmand, 1999). The behaviour is reinforced by the idea of reward and punishment, which influences the managerial functions that advocate no separation between worldly and religious aspects of life (Hassan & Christopher, (2005). Unlike other religions, Tayeb (as cited in Hassan & Christopher, 2005) contends that Islam is an all-encompassing creed. It governs every aspect of life, public and private, political and economic, relevant to business activities.

The number of Muslim becomes one of the indicators of BOD in this study. BOD Muslim has been applied in previous study to indicates whether the BOD Muslim influence or not to the performance of a firm (Shatnawi, 2020). Thus, this study used the BOD Muslim as one of the BOD's. Following Table 2.5 shows the summary of prior studies on the BOD.

Table 2.5: Summary of Prior Studies on Board of Director

	Author/years	IV/DV/Med/ Mod/CV	Board	Size	Indep.	Meeting	Muslim
1	Muhammad et al., 2021	IV	/		/		
	Abdallah & Bahloul, 2021	IV		/	/		
2	Khan & Zahid, 2020	IV	/	/	/		
3	Grassa et al., 2020		/	/	/		
4	Ridwan & Mayapada (2020)	IV	/	/		/	
5	Alam et al., 2021	IV	/				
6	Mansoor et al., 2020	IV	/		/		
7	Elgattani & Hussainey, 2020	CV	/				
8	Khanifah et al., 2020	IV	/				
9	Harun et al., 2020	IV	/	/		/	
10	Shatnawi, 2020	IV	/	/	/	/	/
11	Aslam & Haron, 2020	IV	/		/		
12	Saidat et al., 2019	IV	/				
13	Khudhair et al. 2019	IV					
14	Iryani et al., 2019	Mod	/	/	/		
15	Salem et al., 2019	IV	/		/		
16	Shatnawi et al. 2020	IV					/
17	Hassan et al., 2017)				/		
18	Mukhibad (2016)	IV	/	/	/		

Note: IV = Independent Variable, DV= Dependent Variable, CV = Control Variable, Med = Mediator, Mod = Moderator

2.6 Financial Performance

Performance can be defined as the potential over efforts and actions taken that lead to achieving objectives. According to Lesmana and Haron (2019), performance refers to the potential for future successful action to achieve objectives. A firm's performance, however, not only can be observed based on the quantitative measure, such as financial or accounting-based, but it can also be measured qualitatively, such as non-financial measures or based on managerial performance. Financial measures can be observed from financial ratios (Fredendall & Hill, 2011). In contrast, non-financial measures can be observed based on customer satisfaction (Al-Beshtawi et al., 2014; Md Zain & Shafii, 2018) and effectiveness (Dossi & Patelli, 2010).

Most of the studies agree that corporate governance practice could directly influence financial performance. Poor corporate governance practice may impact weak financial performance. The financial performances can be measured using financial indicators, such as financial ratios to explain the firm's performance. Khanifah et al. (2020) revealed that the Islamic banks with a higher corporate governance disclosure reported high operating performance measured by ROA. In contrast, the financial performance of ROE is not significantly related to the disclosure of sharia bank governance.

Meanwhile, in a study, Omaliko et al. (2020) found that intellectual capital disclosure, risk management disclosure, and corporate governance disclosure have a significant influence on firms' performance of ROE, while Lahrech et al. (2014) found a positive relationship between transparency and financial performance. Ghaffar (2014) opines that banks should follow a sound corporate governance system to have better profitability. Effective corporate governance guarantees the safety of the invested funds

and the returns on investment (Bijalwan & Madan, 2013). Ghaffar (2014) supports that corporate governance practice has a significant relationship with bank profitability.

Similarly, Aljifri and Moustafa (2007) argue that corporate governance mechanisms significantly impact firm performance, such as the payout dividend ratio, debt ratio, and governmental ownership. The other study conducted by Hifza Inam and Aqeel Mukhtar (2014) found that good corporate governance significantly impacts bank performance, mainly in capital adequacy ratio. Further, they also indicate that good corporate governance is directly related to the expense management of all banks and the banks that have good corporate governance to improve the performance and maintain the interest of shareholders.

2.6.1 Prior Studies on Financial Performance's Measurement

The performance variables were utilised to explain the relationship between governance and performance (Hassan, 2013a). In financial institutions, a good corporate governance practice is frequently highlighted in an organisation because good governance leads to the effectiveness of management and the health of the business environment that reflects the firm's performance. Thus, profitability is one of the measurements commonly used by investors as an indicator to determine a firm's ability to generate profits (Siswanti et al., 2017). Nawaiseh (2015) found that firm financial performance has a significant and positive impact on CSR disclosure. Likewise, according to Maskun (2013), the level of leverage, company size, and profitability influence the CSR disclosure, improving the society's welfare. The financial performance in this study was measured based on three financial ratios, namely, return on Asset (ROA), return on equity (ROE), and debt-equity ratio (DER), in line with the

summary of prior studies on the financial measurements (ROA, ROE, and DER) shows in Table 2.6.

Table 2.6: Summary of Prior Studies on Financial Measurement

	Author/years	Profitability		Leverage/ Gearing
		ROA	ROE	DER
1	Muhammad et al. (2021)	/		
2	Balqis (2021)	/		/
3	Abdallah & Bahloul (2021)	/	/	/
4	Shatnawi (2020)	/	/	
5	Nurhikmawaty et al. (2020)			/
6	Shatnawi et al. (2020)	/	/	
7	Khan & Zahid (2020)	/	/	
8	Nomran & Haron (2020)	/	/	
9	Masruki et al. (2018)	/		/
10	Szegedi et al. (2020)	/	/	
11	Nurmawati et al. (2020)	/	/	
12	Elgattani & Hussainey (2020)	/	/	
13	Khanifah et al. (2020)	/	/	
14	Prasojo & Hadinata (2020)	/	/	
15	Omaliko et al. (2020)	/	/	
16	Sencal & Asutay (2020)	/		/
17	Saidat et al. (2019)	/		
18	Khudhair et al. (2019)	/	/	
19	Nurmasari (2017)		/	/
20	Tumonggor et al. (2017)		/	/
21	Rusydiaana & Al-Parisi (2016)	/	/	
22	Hassan et al. (2017)	/	/	
23	Mukhibad (2016)	/	/	
24	Musibah & Alfattani (2014)	/	/	

Table 2.6 illustrates the prior studies on the financial performance indicators. These indicators have been used to indicate the company's health. There are many types of financial ratios commonly applied in different studies. This study analysed three financial performance indicators (ROA, ROE, and DER) to measure the performance of Islamic banks. The ROA and ROE are the frequent financial ratios utilised in numerous studies, while DER is less used than the ROA and ROE.

Profitability is a financial indicator that is commonly applied in many studies (Abdallah & Bahloul, 2021; Balqis, 2021; Muhammad et al., 2021; Khan & Zahid, 2020; Shatnawi et al., 2020). The profitability concept indicates the company's actual performance representing management performance and measures the benefits obtained

(Rusydiaana & Al Parisi, 2016). Meanwhile, Siswanti et al. (2017) state that profitability becomes one of the indicators specifically for investors' investments decision-making because profitability is used to determine the company ability to generate profits, which was also applied by Grassa et al. (2020) in their study. Moreover, they specify that the relationship between ROA and corporate governance practice shows a different result: The outstanding corporate governance practice shows the lowest mean of ROA. A firm with outstanding corporate governance practices shows the highest mean of ROE, whereas the lowest corporate governance practice indicates the substandard corporate governance practice (Bijalwan & Madan, 2013). In contrast, the firm with a reasonable corporate governance practice indicates the highest means of ROA.

Several studies have been conducted to see the performance of the firm. In the current study, dependent variables are the bank's performances which are measured by financial. According to Hutchinson and Gul (2004), accounting-based performance is preferable to investigate corporate governance and performance. Hifza Inam and Aqeel Mukhtar (2014) indicate that corporate governance is positively associated with profitability, bank interest income, and return on equity. They also state that good corporate governance provides the recommendation to sustain the growth opportunities, help to improve the quality of assets and financial indicators, such as income, earning on equity, and earning per share (EPS).

A bank's performance has conventionally been evaluated based on financial ratios using financial ratios and several quantitative indicators, translating into a company's financial strength (Shamsudin & Mohammed, 2015). Generally, financial ratios contribute to the analysis of profitability, efficiency, liquidity, leverage. The current study adopted several variables found from previous studies and were used as the measurement of financial performance to measure the dependent variable. For instance,

the accounting-based variables of ROA, ROE, and profit margin are extensively applied to measure firm financial performance (Abdallah & Bahloul, 2021; Aduda et al., 2013; Balqis, 2021; Muhammad et al., 2021; Mollah & Zaman, 2015). According to Ehikioya (2009), the profitability of measuring financial performance is due to the availability of data and the choice of statistical analysis. He employed four variables of performance measurement, namely, ROA, price-earnings ratio, return on equity, and Tobin's Q.

Ahmed Sheikh et al. (2013) examined the impact of corporate governance and firm performance using ROA, which shows the significance and positively related to the ROA and revealed that the outside director and managerial ownership are statistically significant but negatively related to the ROA. Another study by Chang and Leng (2004) examined the elements of corporate governance with the firm performance, namely, ROA and dividend payout used for a regression analysis. They also used return on sales (ROS), ROA, and growth rate of sales (GRS) to measure the firm's performance in their study on corporate social responsibility and corporate performance in China. Meanwhile, in their study, Aduda et al. (2013) and Uwuigbe (2011) constructed two financial performance variables, ROA and ROE, as dependent variables.

Meanwhile, the gearing ratio or leverage is one of the indicators of financial ratio applied to indicate the financial status or performance (Grassa et al., 2020). Leverage is considered an essential indicator that various researchers have studied leverage or debt-equity ratio in the past (Abdallah & Bahloul, 2021; Balqis, 2021; Dasgupta, 2003; Nurhikmawaty et al., 2020). Revealing this information enables the public or stakeholder to evaluate the ability of the firm to pay its debts on time and, in turn, reduce agency costs (Ismail, 2002).

However, DER may differ with the other industries and depending on the characteristic and types of a business (Nurdiwaty & Faisol, 2017). A high debt-equity ratio can be good because it shows that a firm can easily service its debt obligations (through cash flow) and is using the leverage to increase equity returns., for instance Solihati (2021) opined that the higher the DER, the higher the financing made by the company to run its company. In addition, if the company earns a profit, the company tends to use the profit to pay debts rather than dividing dividends (Ginting et al. (2017).

The analysis thus implies that high bank leverage is the appropriate idealized-world baseline for analysing bank capital structure in the presence of a demand for liquid financial claims per se (Christopher, 2013). High DER may consider as high obligation that cause a difficulty for a company to obtain the fund from other sources. However, for certain industry this obligation not necessarily bad if the company can generate the income and provide the profit to its owners from the debt such as in the banking system Heikal et al. (2014).

Dasgupta (2003) argues that companies having more debt in their financial structure would disclose more to restore confidence amongst shareholders that their company is doing well. On the other hand, Andrikopoulos and Krikiani (2012) revealed that the companies with high levels of financial leverage tend to reduce disclosures due to the disclosure preparation being a costly procedure. However, a study on disclosure by Malaysian Listed Companies conducted by Abdullah and Ku Ismail (2008) revealed that the leverage does not appear to influence the level of disclosure significantly. Likewise, Masruki et al. (2018) in a study found no significant association between gearing and Shariah governance, supporting numerous disclosure studies, such as Aly et al., Hussainey et al., and Hassan et al. as cited in Masruki et al. (2018).

2.7 Summary of the Gap

Further, this section summarises the gap found between this study and prior studies. Table 2.7 summarises the gap of study.

Table 2.7: Summary of the Gap

Current Study	Previous study
1) Shariah governance and Maqasid Shariah were conducted in this study as the independent variable.	1) Each variable was conducted in a single study. E.g., SG only, Maqasid Shariah only, or SSB only.
2) Financial performance as an independent variable.	2) Masruki et al. (2018) - SG as a dependent, performance as independent.
3) BOD as Mediator.	3) BOD function as independent variables
4) SG disclosure.	4) Hanefah et al. (2020) – Shariah governance (SGF & SGPD) in a case study on Shariah non-compliant income.
5) Interpretation and harmonisation of Maqsid Shariah of five and CSR disclosure.	5) Razali et al. (2021) analysed the score and ranking of Maqasid Shariah disclosure items for the Malaysia and MENA regions. The authors discuss four perspectives 1) Workplace, 2) Environment, 3) Social, and 4) Marketplace.
6) SG and Maqasid Shariah relationship to the performance.	The Maqasid Shariah disclosure items were based on the Education, Justice, & welfare as Maqasid performance- ratio - Mohammed et al. (2008), Rusyidiana, 2016, Arini 2020 – Maqasid Shariah performance.
7) Unlike Hanefah et al. (2020), SGF and SGPD were used in this study as the main ref. / source in developing the SG mechanisms concerning this study on Shariah governance.	6) Ahmad & Ishak 2020- Conducted a case study in Islamic banking on the Maqasid Shariah in the Shariah governance. The Maqasid Shariah is discussed in general perspective.
8) Maqasid Shariah was the dependent variable to examine the relationship between Maqasid Shariah and financial performance.	7) Hanefah et al. (2020)– Illustrate the SG in Malaysia by discussing SGF and SGPD 2010.
9) This study was conducted on empirical to examine the SG (Shariah audit to the performance).	8) Iryani et al. study - Financial performance IV, Shariah governance as moderating, Maqasid Shariah as DV.
	9) There is a limited empirical study on Shariah audit. Many studies were conducted on the effectiveness and are qualitative studies.

2.8 Underpinning Theory

Firms from financial or non-financial industries can create economic value due to practical and innovative management of resources. Numerous resources are available

to create competitive advantages, firmly moving on to ideas creation, experience, and knowledge. Whether financial or non-financial industry, utilising the resource is how the firms manage the resources to create a competitive advantage.

There is a need for management best practices to plan and manage the resources wisely since the resource is an important mechanism that influences a firm's performance (Bontis et al., 2000). For instance, concerning firm performance, according to the resource-based view, firms achieve competitive advantage and high performance through the acquisition, shareholding, and use of the strategic asset (Wernerfelt, 1984). Hence, RBV via intellectual capital is used to explain the need for a resource with specific knowledge of Shariah. Islamic banks must possess the SC to play their role in Shariah matters and create confidence. There is a need to consolidate and explicate Shariah governance practice through intellectual resources compatible with the study in IFIs. Since this industry carries out the responsibility of implementing Shariah governance practices and promoting Shariah-compliant products and services to Muslims, failure in presenting the Shariah-compliant practices might create a bad reputation for this industry. Nawaz (2017) found a significant positive relationship by studying the effect of intellectual capital on financial performance, which indicates that intellectual capital becomes an essential factor in sustaining performance and competitiveness in the IFIs. The intellectual resource enables the organisation to develop the strategies and plan the direction to enhance the industry in a competitive advantage, fulfil the needs of specific groups, and maintain the industry's reputation in line with its developments.

In this regard, the current study adopted the intellectual capital model (ICM) to explicate the practice of corporate governance and Shariah governance. Therefore, the following section discusses specifically the intellectual capital model to understand how

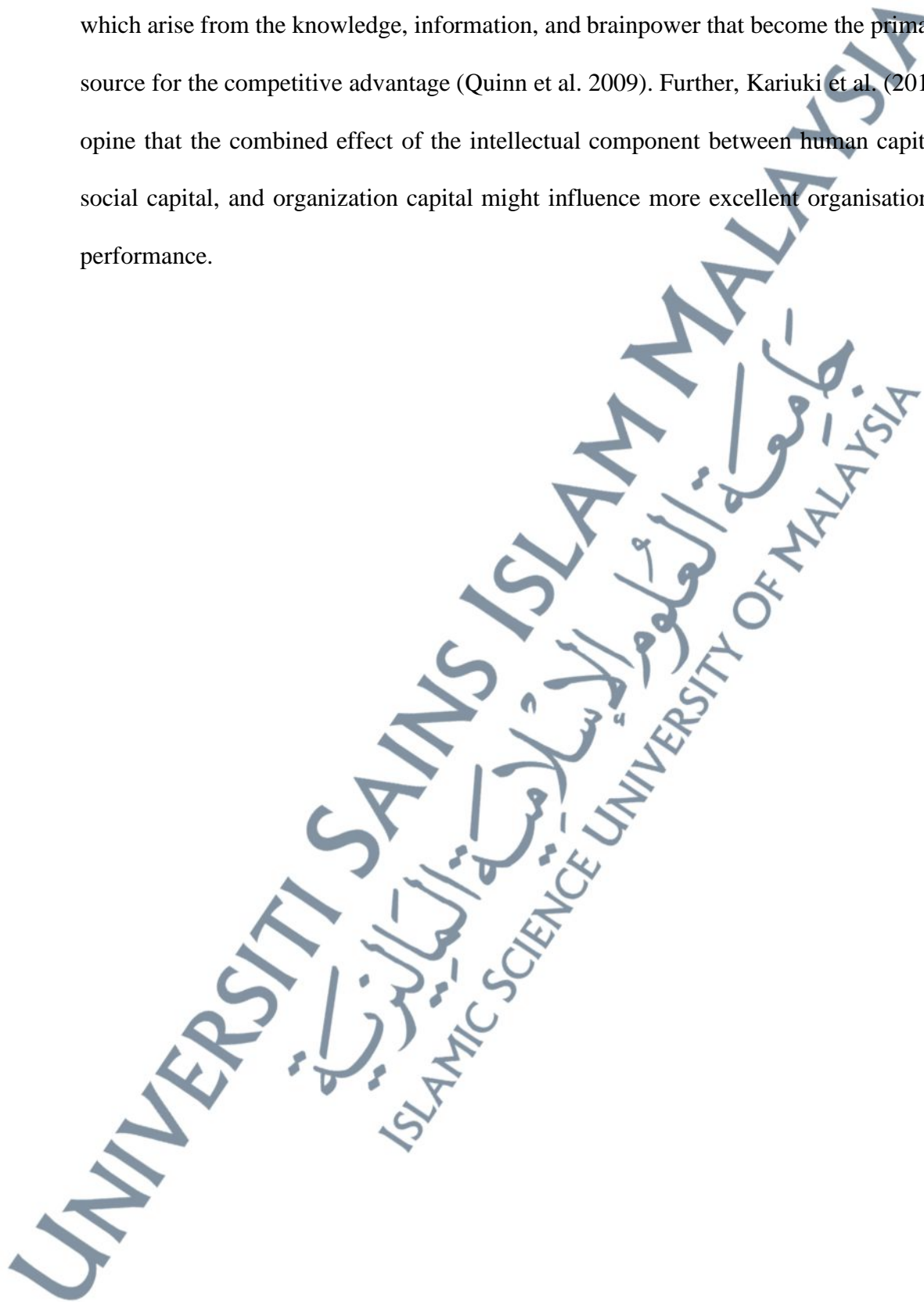
this model shows the flows and the relationship between Shariah governance and performance.

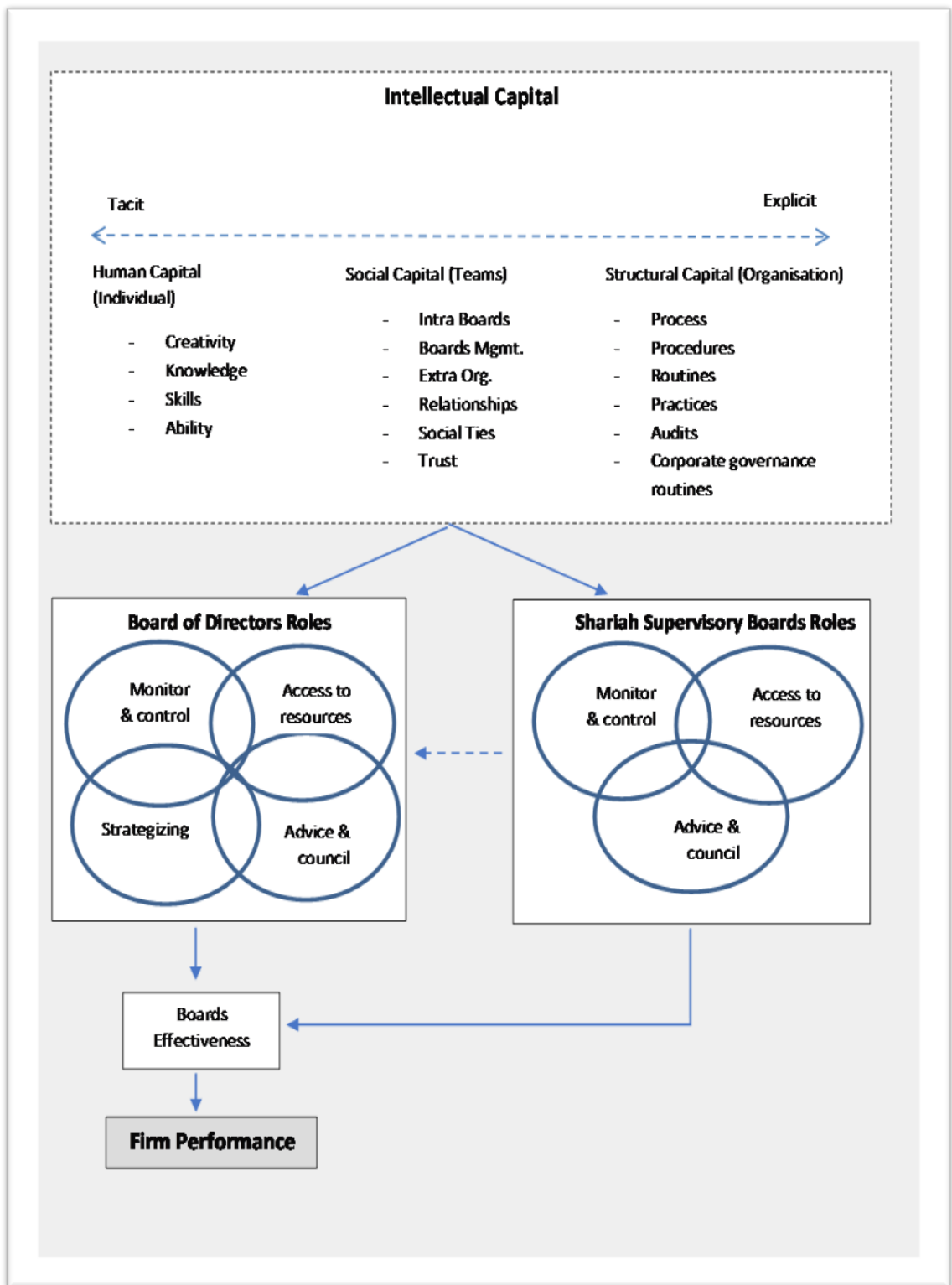
2.8.1 Intellectual Capital Model (ICM)

Unlike the corporate governance practices in the non-Islamic financial institution, IFIs has two board independent, namely, the BOD and SSB (Nathan & Ribière, 2007). The existence of the SSB or SC in the IFIs is to ensure the whole operation and transaction are complying with the Shariah. Therefore, since the corporate governance theories, namely, agency theory, shareholder theory, stakeholder theory, and stewardship theory are applied in a single board, the ICM is an additional model to meet the requirement of SC in IFIs. This model has been applied by Nathan and Ribière (2007) to study corporate governance in Islamic banks, adapted from Nicholson and Kiel (2004). Like the study conducted in Islamic banks, the corporate governance theories and the ICM are appropriate to explain the Shariah governance, corporate governance, and Islamic intellectual capital in realising the implementation of Shariah governance, the achievement of Maqasid Shariah, and explaining the concept of disclosure and transparency. Thus, the intellectual capital model can be seen as a model to guide the study of Shariah governance towards performance.

The intellectual capital was first introduced by John Kenneth Galbraith year 1969 (Haghshenas & Barzegar, 2014; Kariuki et al., 2015; Meihami et al., 2013). Further, the intellectual capital was explained by the management guru Peter Drucker in year 1993 in his description of a post-capitalistic society (Haghshenas & Barzegar, 2014). Many scholars agree that a firm rich in intellectual capital could achieve a highly competitive advantage. There are four levels of professional intellect increasing importance that lead to higher performance, namely, cognitive knowledge (or know-what), advanced skills

(know-how), systems understanding (know-why), self-motivated creativity (care-why), which arise from the knowledge, information, and brainpower that become the primary source for the competitive advantage (Quinn et al. 2009). Further, Kariuki et al. (2015) opine that the combined effect of the intellectual component between human capital, social capital, and organization capital might influence more excellent organisational performance.





Source: Nathan & Ribière (2007)

Figure 2.4: Intellectual Capital Model

Intellectual capital can be classified into three, which are human capital, social capital, and structural capital. Human capital is at the individual level, and the team supports the social capital and the structural capital derived from the organization. The BOD controls this group of intellectual capitals, while the SSB plays a role in the Islamic perspective. However, at the SSB level, all the activities, supervisory and advisory will be reported and reflected in the BOD to ensure the firm's effectiveness, whether in the Shariah application or the entire business operation that shows through the firm's performance.

2.8.2 Theoretical Background

Theoretically, previous studies opine that the theoretical perspective that guided the current study links the idea that banks with an efficient corporate governance structure have a better performance (Al-Hussain, 2009). After reviewing the literature on corporate governance, several theories were identified to be applied in this study. Obid and Naysary (2014), Staikouras and Agoraki (2015), and Bebeji et al. (2015) adapted the agency theory, stewardship theory, and stakeholder theory in their studies of corporate governance and performance. Likewise, Obid, and Naysary (2014) conducted a study on Shariah governance in IFIs to explain Shariah perspectives. Peters and Bagshaw (2014) and the resource dependency theory are the most important theories to explain in their study as effective and efficient in monitoring and controlling corporate governance functions.

The agency theory is widely used in academia on corporate governance to explain the nature of corporate governance and the possible issues in an organisation. The stakeholder theory attempts to address the question of stakeholders that deserve management's attention (Peters & Bagshaw, 2014). Stakeholders consist of

shareholders, employees, investors, customers, and suppliers as direct stakeholders. Stakeholder theory considers the interest of all parties affected by their action. Concerning this study, the stakeholder theory is appropriate for defining the relationship between stakeholders' roles and the firm's performance.

In a corporate governance practice, stewardship theory is necessary to address, apply, and link with the nature of corporate governance. The stewardship theory addresses trust and acts as a steward to guide the manager to produce the best performance and gain high satisfaction by achieving the organisational goal. Meanwhile, the stewardship theories focus on the structures that empower and facilitate the manager to perform the duty (Habbash, 2010).

Therefore, two theories in this study were identified to explain the board's function. For instance, board attributes can minimize agency conflicts and agency costs (Haniffa and Hudaib, 2007), which will lead to improved corporate value (Bukhair & Rahman, 2015). The agency theory suggests that the information asymmetry between agents and principles can also be reduced over the execution of monitoring mechanisms to promote the level of disclosure information (Grassa et al., 2020; Jensen & Meckling, 1976). Through the disclosure, the shareholder can access the information to reduce uncertainties and information asymmetry.

Firstly, concerning the stewardship theory, there is a strong relationship between managers and company success through performance improvement (Yusoff & Alhaji, 2012). They argue that the stewardship theory is linked to the performance that meets stakeholders' needs and balances governance and performance. Moreover, stewardship theory concerns the company's interest as a priority by reacting to the conflict situation (Borlea & Achim, 2013). Secondly, the stakeholder theory argues the right of the stakeholders to participate in the decision-making process (Obid & Naysary, 2014). It

concerns the interest of both parties, which are the stakeholders and shareholders (Yusoff & Alhaji, 2012). A study by Rehman et al. (2020) states that this theory is a valuable tool for further improving the company's performance. The management can perform their responsibilities as best as possible regardless of their interests.

2.8.2.1 Stewardship Theory

The agency theory first applied by Jensen and Meckling (1976) mentions that the manager acts as an agent, while the shareholders are principals. Theoretically, the principal empowers the management to decide a representative of shareholders. The agency theory states that the roles of the board are crucial to meet the expectations of the principles on behalf of them to lean and make decisions (Borlea & Achim, 2013). The agency problem appears when the agent intentionally decides for their interest instead of fulfilling the principal's best interest. The different goal between shareholders and managers leads to the agency problem, whereby the manager as an agent focuses on achieving his personal goals (Mohammed & Muhammed, 2017). In addition, the agency theory suggests that the information asymmetry between agents and principles can also be reduced over the execution of monitoring mechanisms to promote the level of disclosure information (Grassa et al., 2020; Jensen & Meckling, 1976). Through the disclosure, the shareholder can excess the information that would reduce the uncertainties and information asymmetry.

In relation, the stewardship theory was introduced by Donaldson and Davis (1991) as a normative alternative to the agency theory (Subramaniam, 2018). The term 'steward' refers to the person who protects and responds to the needs of others. This theory's fundamental is based on social psychology, which is the behaviour of the executives of managers. The stewardship theory refers to the manager responsible for

making decisions on behalf of the owners and protecting the interest of shareholders or owners. In this theory, the managers are left independently and act as stewards responsible for their controlled assets (Maliah et al., 2015). This theory also argues that managers with a solid self-esteem and self-fulfilment will improve their performance, eventually meeting their needs (Obid & Naysary, 2014). From the psychological and sociological perspectives on this theory, the steward is entrusted as faithful, influential people, and thus, they are classified as good administrators for entrusted resources (Borlea & Achim, 2013).

The stewardship theory suggests that the success of an organisation is backed by the steward's need (Uwuigbe, 2011). This theory perceives a strong relationship between the manager and firm success by improving the firm's performance (Yusoff & Alhaji, 2012). To this extent, the stewardship theory is the argument expressed in firm performance that meets stakeholders' needs and produces the equilibrium of dynamic performance for balanced governance. In sum, as opposed to the agency theory, the stewardship theory assumes that the managers are not acting for their interest but acting in a given conflict of interest situation whereby they put the interest of the company as a priority instead of for their advantage (Borlea & Achim, 2013).

From an Islamic bank perspective, the stewardship theory explains that Islamic banks are motivated to act as stewards to provide the best service (Azmi et al., 2020). This theory always stands with the Shariah principles in serving the customers and the community at the best possible to achieve the Maqasid Shariah. Meanwhile, in Islamic banks, the BOD acts as an intermediation between implementing any policy and strategy and monitoring any progress on the corporate objective. The Board is acting as an intermediation between the policy and any activities of banks toward the performance. Thus, with the stewardship theory, the BOD and SC will perform the best

possible to achieve the Maqasid Shariah and finally impact the banks' performance (Azmi et al., 2020). Management, performing its stewardship function, needs to ensure that compliance to Shariah is being met for the promised Shariah-compliant values to be delivered to the shareholders as the investors' concern with Shariah-compliant values motivates them to invest in the first place.

2.8.2.2 Stakeholder Theory

Empirically, the stakeholder theory is applied to describe the nature of the firm, the way of managing, the board's reaction towards the interest of corporate constituencies and the way the corporation is managed, and to explain specific corporate characteristics and behaviours (Donaldson & Preston, 1995). The stakeholder theory states that the main objective of an organization is to maximise stakeholder's value emphasising the stakeholder-related issues in an organization (Rehman et al., 2020). The stakeholder theory is becoming better known because many researchers have recognised that the activities of corporate entities affect external environmental factors and require organizational accountability to a broader scope rather than limited to the shareholders (Yusoff & Alhaji, 2012).

This is in line with the principles of corporate governance, known as the system, to ensure the board and corporate management strike a balance between the interests of various stakeholders (Rossouw, 2008). Mitchell et al. (1997) provide three characteristics of stakeholders: Power, legitimacy, and urgency. The manager needs to be aware of the entities in an environment where he is in power and intends to execute his interest in the firm. Power and urgency must be taken if the manager serves the law and the interests of legitimate stakeholders (Mitchell et al., 1997). According to Salami et al. (2014), the stakeholder theory builds a satisfaction. It promotes stakeholders'

interests that always aim to ensure each area receives some satisfaction. Furthermore, stakeholders are recognised as assets, while managers are expected to manage them effectively (Rehman et al., 2020). This theory is the nexus of a contract between the firm and interested parties that known as stakeholders, such as employees, shareholders, creditors, government, and other stakeholders (Obid & Naysary, 2014; Sanda et al., 2005), by participating in the role of the management process of the firm and control (Iqbal & Mirakhor, 2004).

However, some studies argue that this theory is narrow since shareholders are considered the only interest group of a corporate entity (Yusoff & Alhaji, 2012). According to Phillips and Reichart (2000), the stakeholder's significant weaknesses are identifying the stakeholders' identity, distinguishing between the stakeholders and those who are not. Similarly, according to Mitchell et al. (2006), the definition of the stakeholder is narrow as the managers cannot attend to all actual or potential claims. This argument views that corporate governance structures highlight stakeholders' right by reducing the information asymmetry and emphasising enforcement component to protect the rights of stakeholders (Bonnafeous-Boucher, 2005; Donaldson & Preston, 1995; L'Huillier & Marie L'Huillier, 2014).

Unlike the agency theory, the stakeholder theory does not mention the information asymmetry between managers and the shareholders. However, it argues the right of the stakeholders to participate in the decision-making process (Obid & Naysary, 2014). It concerns with the interest of both parties, which are the stakeholders and shareholders (Yusoff & Alhaji, 2012). A study by Rehman et al. (2020) states that the stakeholder management assumption of the theory is a helpful tool to gain profitability.

2.8.2.3 Legitimacy Theory

The legitimacy theory is the central thought of the social contract between organizations and society by considering the rights of the public in general, not merely focusing on the right of investors alone (Yusoff & Alhaji, 2012). In this effort, a firm will disclose the social activities information to the public to strengthen their image towards socially responsible for attracting their stakeholder groups.

From the CSR perspective, the legitimacy theory emphasises that the community allows an organization to use natural resources legally and allows the organization to obtain human resources by employing people from the local community. With these resources, an organization utilizes them to benefit its business by producing its products and services, yet unfortunately, pollutes the environment through its waste (Aslam et al., 2018). To maintain this relationship, an organization needs to demonstrate its good behaviour as a corporate member to the community. They act as a corporate body that shows that the community needs their support by providing facilities and assistance. In response, the community accepts all their activities and action. However, failure to meet the society's expectations of its propensity can trigger unforeseen actions against the operations and cause restrictions on its resources and demand (Yusoff & Alhaji, 2012). For instance, health and safety are the society's main concerns, and it can change the society's perception if corporate bodies emphasise the importance and provide this facility to society (Gray et al., 1995).

Concerning the aim of a business, it is recognised that maximising the profit and giving shareholder values is a direction to gain the business success. Therefore, numerous studies have examined a firm's performance based on profitability since profit maximisation is an indicator of corporate performance (Yusoff & Alhaji, 2012).

However, according to Ramanathan (1976), in the legitimacy theory perspective, profit is seen as an indicator of organisational legitimacy in total.

On the other hand, many empirical studies applied the legitimacy theory in social and environmental reporting and related corporate disclosures and community expectations (Deegan, 2004). Hillman et al. (2000) consider external environmental factors' potential influence and reduce uncertainty to reduce transaction costs related to external relationships. Consistent with Gales and Kesner (1994), state that legitimacy potentially reduces uncertainty.

Therefore, it is essential to explain the validity of the Shariah-based elements in providing products and services in the Islamic financial system. Reporting on the operation's background, activities, and transactions can convince the community, especially Muslims, because their involvement with Islamic financial products is due to the Shariah-based system fulfilling the obligations of Shariah requirements. If the needs of these Muslims are not met, they will turn and find other alternatives to meet their needs. In addition, Islamic banks will continue to strive to ensure that their companies are seen to operate according to the boundaries and norms of society, and they also always ensure that their corporate activities are accepted by external parties (Azmi et al., 2020). Based on the theory of legitimacy, in the effort of Islamic banks to seek legitimacy from the community or other external parties, they need to disclose relevant information as an intermediary between Banks and the public. Moreover, by providing information on his company's performance, the community will be confident to be his customers. Likewise, disclosing the information about banks' activities in supporting the community can attract banks' customers to respond to banks' efforts in serving the community.

2.9 Research Framework

The previous discussion on underpinning theories led to the study's research framework, as shown in Figure 2.5. The independent variables (IV) studied were Shariah governance (SC, Shariah audit and Shariah risk) and Maqasid Shariah disclosure. These independent variables were hypothesised to have significant relationships with the dependent variable (DV): Financial performance (ROA, ROE, and DER). This study also intended to investigate the BOD in mediating the relationships between the Shariah governance dimensions and Maqasid Shariah with Islamic banks' performance. Figure 2.5 presents the framework of the proposed research.

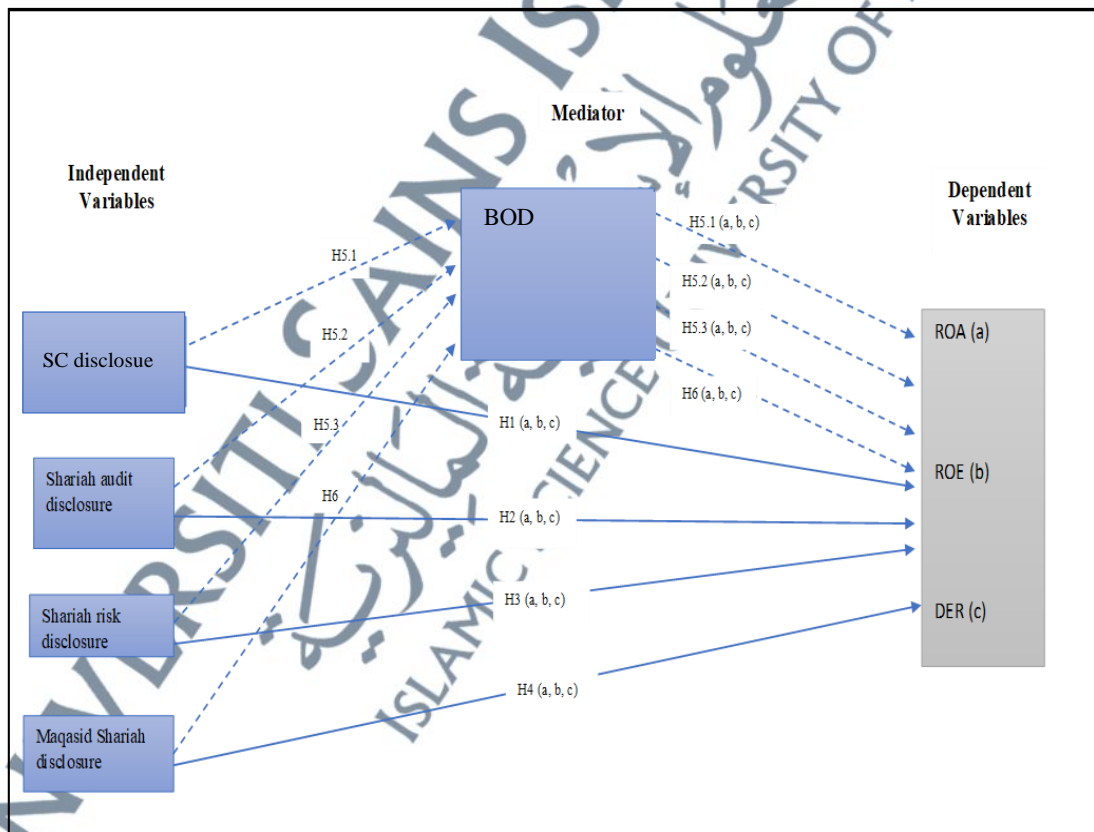


Figure 2.5: Theoretical Framework of Study

The conceptual framework was developed based on the previous literature and theories. The underpinning theory in this study is the Intellectual capital model (ICM) and three other related theories to this topic, namely, the stakeholder's theory, stewardship theory, and legitimacy theory as discussed in the previous section adopted in this study to explain each of the study's variables. In addition, this study also provides an additional model, namely, the Intellectual Capital Model (ICM) related to the Shariah governance. This study is appropriate since the corporate governance theory, such as the agency theory, stakeholder theory, and stewardship theory, were applied in a single board. Since this study was conducted in Islamic banks, the ICM explains Shariah governance and corporate governance. It was known that the Islamic banks were involved with the additional role by SC. Thus, ICM in this study explains the Shariah matter concerning the Shariah governance and Maqasid Shariah, which require the SC to implement the Shariah governance and achieve Maqasid Shariah by explaining the concept of disclosure and transparency. Thus, the intellectual capital model can be seen as a model to guide the study of Shariah governance towards performances.

2.10 Hypothesis Development

Based on the reviewed related literature and underpinning theories discussed in the previous sections, this section develops the hypotheses that give tentative answers to the research questions that were extended based on the problem statement and the background of this study. In this sense, the study hypothesised the relationships between the Shariah governance and Maqasid Shariah with the Islamic banks' performance. The study also hypothesised the mediating role of the Board between these independent variables, namely, SC, Shariah Audit, Shariah risk and Maqasid Shariah, and the

dependent variable, namely, ROA, ROE, and DER as the financial performance indicators.

The disclosure quality of annual reports is considered a critical element in corporate governance because it illustrates good corporate governance (Htay, 2013). In addition, Htay et al. (2013), Beekes and Brown (2006) revealed that an excellent company in corporate governance provides a complete and informative disclosure. Thus, the study on the Shariah governance and Maqasid Shariah governance disclosure is consistent with the legitimacy theory to emphasise the need to disclose the information to provide accurate, practical, and realistic information to the stakeholder's public. The information related to the company policy, such as related to regulation, namely, Shariah governance, is crucial to the investor, customers, and other stakeholders for their decision-making for those seeking the legitimacy of an organisation. On the other hand, the Maqasid Shariah highlighted in this study will benefit the society, employees, and other stakeholders. The Maqasid Shariah information emphasises the effort of an organisation to meet the need of society and shows a symbol of concern and support for the social interest.

2.9.1 Shariah Committee Disclosure and Performance

The SC is an independent committee to observe the business operation and assure the stakeholders that the business is conducted based on Islamic principles (Aribi & Gao, 2010). The SC is an independent Board to investigate, audit, and provide Islamic banks with Shariah principles at ex-ante and ex-post for all financial transactions as a standard policy (Quttainah, 2012). The SC is selected based on the qualification and knowledge in Shariah. The Shariah background is significant to monitor and lead the Islamic banks towards an Islamic governorship to ensure that the banks' activities

comply with Islamic laws and build the Islamic values in the organisation. In Shariah governance practice in Islamic banks, the institution must implement the Shariah requirements stipulated by the BNM for IFIs. The SC plays a significant role to ensure the entire operation following Shariah compliance. Also, the Shariah supervisions under the SC present various objectives, including providing legitimate solutions for barriers and conflicts and improvements for the future (Garas & Pierce, 2010).

Recently, many studies have revealed that the SC is acting as an essential mechanism in Islamic banks to ensure that the activities of Islamic banks comply with Shariah. It is considered one of Shariah governance's significant components in IFIs (Grassa, 2013). The primary function of the SC is to ensure the transaction in Islamic banks following Islamic principles. Lack of Shariah governance practice would cause most people to lose confidence in the Islamic banking system, especially the Muslim community (Alnasser, 2012).

In addition, Amalina et al. (2013) state that the role of the SSB is also to assure the Shariah compliance that could influence the Shariah related disclosure in the annual report in Islamic banks. Likewise, Ghayad's (2008) study on corporate governance and the performance of Islamic banks highlights the roles of the SSB on the performance of Islamic banks, including the governorship of the Shariah board, and the Shariah board and profit. In addition, the governorship of the Shariah board controls the bank transaction based on Islamic law entrusted with directing, reviewing, and supervising the Islamic bank activities to ensure the activities always comply with Shariah principles. Bukhari (2013) also states that the SSB is responsible for ensuring the financial activities in an organisation are conducted based on *fatwas* and will review whether the transaction is under the Shariah. The execution of the SSB by Islamic

financial institutions deals with the transaction in the business activities towards Shariah issues in financial transactions to ensure compliance with Shariah requirements.

Almutairi and Quttainah's (2017) study found a positive relationship between the size of SSB and financial performance. This information is essential to be disclosed in the annual report to increase shareholders' confidence in dealing with IFIs (Tawfeeq & Alabdullah, 2017). Likewise, Mollah and Zaman (2015) investigated the impact of Shariah supervision, including the supervisory or advisory role of SSB on performance. This study found that the effect of SSB on accounting-based performance is positive when Shariah boards have a supervisory role.

Meanwhile, the study conducted by Masruki et al. (2018) found that SC and disclosure are significantly associated with ROA. In contrast, the effect is negative when the Shariah boards have an advisory role. Hence, based on the discussion, the following three main hypotheses were developed:

H1a: There is a significant relationship between SC disclosure and ROA of Islamic banks.

H1b: There is a significant relationship between SC disclosure and ROE of Islamic banks.

H1c: There is a significant relationship between SC disclosure and the DER (Debt to equity ratio) of Islamic banks.

2.9.2 Shariah Audit Disclosure and Financial Performance

The roles of the Shariah audit are crucial in serving the public assurance on the products. It becomes the immediate support to ensure the Shariah-compliant (Abdul Aziz, 2013). Shariah audit provides an independent assurance to the stakeholders and

engages with a periodic assessment to meet the effectiveness of the internal control system towards the Shariah compliance system. Thus, the firm must disclose the information as a medium of communication to inform the stakeholders regarding the Shariah audit involved in the Islamic banks.

In addition, the implementation of the SGF has had a significant impact on the audit function within the IFIs, as studied by Shafii et al. (2010). Kasim et al. (2013) argue that the current Shariah audit manual is considered insufficient and emphasise that the proper Shariah audit framework is essential to guide practitioners in implementing the Shariah compliance auditing. Chik (2011) opines that the Shariah audit function is needed due to the possible negative impact from the lack of practice in IFIs, which might influence the financial or non-financial status.

Several studies argue that the existence of audits in an organisation could improve the performance of the firm. Khalid et al. (2018) support that competency and work performance are positively correlated with an internal Shariah audit effectiveness. Similarly, a study conducted by Alaswad and Staniši (2016) found a correlation between audit function and a firm's performance. This correlation plays a significant role in the performance of financial institutions. Awdat (2015) revealed that the importance of the internal audit function had positively impacted a firm's financial performance. Therefore, the study concludes that an effective internal audit function positively influences financial performance (Bett, 2014).

An efficient internal audit is important because it is associated with the financial report to reflect its performance. Similarly, the audit function might signal the entire management where is lacking in an organisation. It is also to ensure that work is properly done based on guidelines. Any problematic issue is subject to be discussed

with the management to find a way to solve them. Consequently, this will help to improve the organisation performance.

The Islamic agency theory and its proponents emphasise that internal Shariah auditors as experts in their field assist the IFIs to achieve growth in accordance with the ability to deal with the process and accomplish their tasks with superior quality (Khalid et al. 2018; Safieddine, 2009). Hence, based on the discussion above, three hypotheses were developed:

H2a:	There is a significant relationship between Shariah audit disclosure and ROA of Islamic banks.
H2b:	There is a significant relationship between Shariah audit disclosure and ROE of Islamic banks.
H2c:	There is a significant relationship between Shariah audit disclosure and the DER of Islamic banks.

2.9.3 Shariah Risk Disclosure and Financial Performance

Banks are, in essence, risk-taking enterprises; they are expected to ensure a proper flow of risk reporting to the marketplace (Linsley & Shrives, 2006). Such a system would help monitor managers' attitudes towards risk exposure, foster banks' transparency, and decrease the information gap between both sides (Grassa et al., 2020; Jensen & Meckling, 1976).

According to Yazid and Muda (2006), risk disclosure provides better assessments concerning the risks they face. Disclosing on the Shariah risk is consistent with the legitimacy theory, of which information disclosed may reduce the legitimacy gap. Disclosing the information of the Shariah risk may give the information to the

stakeholders regarding the policy, the action, and the representative in discharging the Shariah risk. This information is crucial that it may influence investors in their decision based on the status of the compliance risk and capability of the firm in dealing with the risk.

Furthermore, Rosli et al. (2017) opine that the corporation must disclose the policy's information, especially on their possible risk. Disclosing this information may reduce the legitimacy gap between corporations and stakeholders. A firm intends to inform the stakeholders about the policy, status, and capability that influence their perception (Lindblom, 1994).

Grassa, Moumen, and Hussainey (2020) revealed that Islamic banks seem more secretive about exposure to material risk than conventional. Different results were obtained in the same study, of which a multi-test was conducted for the relationship between ROA and risk-related disclosure (RRD). The coefficient on ROA in the (RRD) equation remains positive and significant. On the other hand, the coefficient on RRD in the financial performance equation is statistically insignificant. Another study conducted by Rosli, Mohammed, and Sanusi (2017) examined the determinants of voluntary risk disclosures of Shariah-compliant companies. The authors found that firm size has a significant contribution to voluntary risk disclosure. The finding reveals no relationship between religiosity of Board members and directors' ownership to the level of voluntary risk disclosure. The empirical findings reveal that the risk disclosure quality is positively and significantly associated with Board independence (Salem et al., 2019). Hence based on this discussion, three main hypotheses were developed:

H3a:	There is a significant relationship between Shariah risk disclosure and ROA of Islamic banks.
H3b:	There is a significant relationship between Shariah risk disclosure and ROE of Islamic banks.
H3c:	There is a significant relationship between Shariah risk disclosure and the DER of Islamic banks.

2.9.4 Maqasid Shariah Disclosure and Performance

Islamic banks practically and principally differ from the conventional bank, which can be seen in the corporate objective, the control system, and principles of the corporate governance system. The objective of Islamic banks towards the Shariah principles is the main one that can relate with the Maqasid Shariah. Other than that, Islamic banks consistently emphasise welfare, need, and respond to all the stakeholders that lead to the Maqasid Shariah achievement. This response has noticed the public, employees, community, and all stakeholders and has given them values. As a result, the public is aware of an organisation that parallels with their norms. Therefore, from the Islamic banking perspective, Maqasid Shariah achievement through its disclosure becomes one of the mechanisms that may influence the performance of Islamic banks.

According to legitimacy theory, there is a contract between an organisation and the society (Aslam et al., 2018) because it depends on the society to achieve its goal. The society as a part of their workers, and the environment or natural resource are among the factors that the organisation needs to consider in achieving their goal. In this regard, the organisation needs to present their responsibility to the society when they share the natural and human resources to perform the job on behalf of the organisation.

Failure to emphasise a particular community's right could lead the community to treat any activities as harming their norms. Thus, an organisation should create the legitimacy gap between the society and organization by presenting an excellent corporate citizen to the society to preserve the right of the community to achieve their corporate goal (Haniffa & Cooke, 2005).

According to Deegan et al. (2000), the legitimacy theory has increased the annual report's reporting following the controversy of moral and social pressure on the proper reporting. In addition, according to the legitimacy theory, a CSR disclosure is intended to affect the stakeholders and society's perception (Hooghiemstra, 2000). A CSR disclosure has gained the popularity following the demand from the stakeholders who intend to access the information about the company (Boesso & Kummar, 2007). By providing social information through annual reports, the company can enhance its reputation to stakeholders by meeting the needs and welfare of the community (Hassan et al., 2010).

Furthermore, since CSR has been related to the Maqasid Shariah by several studies and has been harmonised in this study, it can be concluded that a CSR disclosure may affect a firm's performance, which is consistent with the legitimacy theory as the Maqasid Shariah disclosure. Rahman et al. (2017) conducted a study on the Maqasid Shariah to examine the firm performance and uphold Islamic values and objectives. Meanwhile, Mergaliyev et al. (2019) studied the elements of Maqasid Shariah about social and ethic reporting designed to measure Islamic banks' performance. Maqasid Shariah was also applied in a study by Asutay and Harningtyas (2015) to measure the level of performance of Islamic Banks in several countries and rank the Islamic banks from the best to the worst. Matuszak and Róžańska (2017) found a positive relationship

between CSR and firm performance based on the stakeholder theory and legitimacy theory, like Freeman (1984) and Suchman (1995).

Therefore, to implement social responsibilities and achieve the Shariah Maqasid, disclosing the information in the company's report an advantageous to promote the social activities to the public and encourage the CSR program by promoting activities towards the social well-being. This approach has demonstrated accountability to Allah SWT from the Islamic perspective, which is essential to inform their stakeholders regarding Islamic principles (Arsad et al., 2015). However, a study by Hosen et al. (2019) found that the Maqasid Shariah and Islamic social reporting were not statistically significantly affected by the profitability of Islamic banks. Thus, this study used the Maqasid Shariah disclosure to indicate their achievements. Hence, based on the discussion of previous studies and the theory, this study hypothesised that:

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- H4a: There is a significant relationship between Maqasid Shariah and ROA of Islamic banks.
- H4b: There is a significant relationship between Maqasid Shariah and the ROE of Islamic banks.
- H4c: There is a significant relationship between Maqasid Shariah and the DER of Islamic banks.
-

Mediator Effect

Further, this study aimed to test the mediation effect by testing the Board's function in mediating the relationship between Shariah governance disclosure and the performance of Islamic banks. In many studies, the Shariah governance disclosure has been developed to measure the Islamic banks' disclosure level (Abdallah & Bahloul,

2021; Al-Sartawi & al Musleh, 2020; Md Amin et al., 2021; Norman & Haron, 2020). The Shariah governance in this study consists of the SSB, Shariah audit, and Shariah risk. This study attempted to prove that the roles of the Board in this study mediate the relationship between Shariah governance and Maqasid Shariah disclosure, with the performance of Islamic banks, following the hypotheses developed on the mediator (Board) to examine the relationship between Shariah governance disclosure and performance of Islamic banks (H5.1, H5.2, and H5.3).

2.9.5 Board Mediates the Impact of Shariah Governance and Performance of Islamic banks

In a business corporation, an agency problem is a common issue that arises due to shareholders and management's interests (Darmadi, 2011a). Jensen and Meckling (1976) theorise that the agency problem as an agency theory is also related to the higher level of ownership concentration that leads to the problem between controller and shareholders (Shleifer & Vishny, 1997). In relation, the corporate governance mechanisms have been explored by many researchers who found that the corporate governance in the banking industry has a higher level of significance to minimise this conflict since this industry is dealing with a large number of public funds and to maintain the public trust (Darmadi, 2011a).

The BOD is one of the critical factors in ensuring the effective implementation of good corporate governance. They become a leading player in dealing with and resolving conflicts of interest between banks and regulators (Klein, 1998; Nawaz, 2017) and monitoring the management, affecting a bank's performance (Fama & Jensen, 1980a). In this regard, the Board and management must be together to promote the integrity culture and consistently cultivate such culture, so that all parties understand the job

scope in performing their duties honestly and efficiently (Chapra & Ahmed, 2002). It is debatable that the Islamic bank's Board may enhance the management in improving the performance (Bukhair & Rahman, 2015). Numerous studies investigated the impact of the Board (e.g., BOD size, Board independence, CEO duality, and composition) on a company's performance (Bukhair & Rahman, 2015). They also examined the social contribution to the performance of Islamic banks.

MCCG 2012 states that the Board holds a significant role in realising the excellence of corporate governance practices (Securities Commission (SC), 2012). For instance, the corporate governance mechanism as a monitoring tool can ensure that the financial statements can deliver valuable information to investors for their decision making (Rosli et al., 2017). The existence of a BOD in the banking industry is crucial compared to other sectors (Pathan & Skully, 2010). It is due to banking as an industry that allows the economic driver by holding a significant financial asset and investing to generate wealth. Meanwhile, for Islamic banking, the BOD is responsible for managing the bank prudentially and based on the Shariah principles (Darmadi, 2011a). However, the single corporate governance seems not enough to explain the Islamic banking sector's value creation and stability (Nawaz, 2017).

In relation, the BOD is responsible for the decision-making, while the role of Shariah governance is to ensure all the activities comply with Shariah. This supervisory board comprises eminent religious scholars responsible for decision-making constrained by a Shariah board that sanctions or rejects any proposals by considering the Islamic law (Ghayad, 2008). However, the SC comprises prominent religious scholars appointed by the BOD. Likewise, the BOD is responsible for managing a firm's business operations (Ghayad, 2008). In a business corporation, the leadership role lies with the BODs. It carries an essential role in creating a climate of integrity,

transparency, social responsibility, and compliance within the business operation (Hassan & Christopher, 2005). These elements are crucial to establishing and maintaining good corporate governance. Consistent with the agency theory, the roles of the BOD are crucial to meeting the expectations of the principles on behalf of them to lean and make decisions (Borlea & Achim, 2013).

In an Islamic organisation, religious factors are more prominent and influence its management practices than other elements (Baydoun et al., 1999). This factor is also associated with most Muslims, such as in Malaysia (Endot, 1995). An Islamic organization has implemented Shariah governance and applied the understanding of the Shariah principles in performing tasks. With this understanding, religious values have affected an individual's behaviour, tendency, and thought and subsequently control the human action and behaviours contrary to religious norms. In addition, Islam emphasises the concept of integrity, responsibility, transparency, and accountability in all transactions to preserve Maslahah to all stakeholders (Ahmad & Ishak, 2020). These concepts are for human assessment, and the belief that every action will be held accountable to Allah SWT, which is based on the reward for a good deed and punishment for an evil deed (Hassan & Christopher, 2005).

Moreover, Islamic banks must strictly control the financial reporting system and the regular disclosure of pertinent information and ensure its reliability (Safieddine, 2009). Providing accurate and valid information indicates that the banks are practising transparency in their business. In addition, Islamic banks are highly recommended to apply financial reporting standards to address the specific issues of Islamic banking (Karim & Archer, 2013; Chapra & Ahmed, 2002). The information and reporting are essential for shareholders as they are entitled to obtain the company's information.

The BOD plays an essential role to ensure the business plan is conducted correctly. They are responsible for getting and improving the policy and strategy, monitoring all the progress towards the corporate objective, ensuring accountability on the management, and protecting the right of shareholders and investment depositors. In addition, an internal control that functions independently supports the implementation of a policy. The internal control is also responsible for ensuring that the management implements the policies set by the board, and they are required to report directly to the board (Chapra & Ahmed, 2002).

Chapra and Ahmed (2002) state that the board and management should be aware of the risks and develop a sound risk management within the bank. Furthermore, banks need to be highly cautious concerning risk management for their exposure to all risks since many risks are inherent in this industry. In the case of failure to manage such risks, the banks will experience the decline in depositors' confidence towards the bank that influences the economic development of a country (Darmadi, 2011a). Hence, the banking sector needs to promote an effective risk management, and banks need to have adequate capital to deal with those risks (Darmadi, 2011a).

Moreover, in the Islamic banking industry, both corporate governance systems are led by two boards, namely, the BOD and the Shariah board (Nathan & Ribière, 2007). The background and knowledge of both boards' related fields show a combination to enhance the company's performance further. They play a role in complementing each other in supporting the business goal that is aligned with the implementation of Shariah compliance to meet the need and expectations of Muslims.

This combination is consistent with the ICM that emphasises the dual roles in the Islamic banks that explain the dual board function practices.

The potential conflict may arise from the information asymmetry, and this study is consistent with the legitimacy theory on the Shariah governance disclosure. The legitimacy theory explains that a company must comply with the society's expectations, need, and norms (Mohammed & Muhammed, 2017). The legitimacy theory suggests that all the company's activities must be disclosed and published to inform the public concerning the transactions and the company's activities. For instance, in Islamic banks, the Muslim's community is concerned over the transaction and the governance system. According to Darmadi (2011a) and Labelle (2002), monitoring and an internal control can be enhanced with the features of good corporate governance, and further, it can improve the company's performance. The information disclosed in a company's report enables the public to access the information that might assist in their decision. The empirical finding reveals that the legitimacy theory has a positive and significant association between a risk disclosure quality and board independence (Salem et al., 2019). This relationship indicates that the governance structure is related to the company's risk disclosure (Abraham & Cox, 2007). Numerous studies emphasise the importance of risk disclosure to meet the stakeholder's demands to assess a company's risk and market value (Salem et al., 2019). According to Darmadi (2011a), in a study, it was found that the dimension of board and risk is substantial. Therefore, it is vital to improve the risk's disclosure, especially during the crisis or when dealing with any challenge, or evaluate its performance (Salem et al., 2019). Hence, based on the discussion and related theory, three main hypotheses were developed:

5.1 The Function of BOD in Mediating the Impact of SSB and Performance of Islamic Banks

H5.1a: BOD mediates the relationship between SSB and ROA.

H5.1b: BOD mediates the relationship between SSB and ROE.

H5.1c: BOD mediates the relationship between SSB and DER.

5.2 The Function of BOD in Mediating the Impact of Shariah Audit and Performance of Islamic Banks

H5.2a: BOD mediates the relationship between Shariah audit and ROA

H5.2b: BOD mediates the relationship between Shariah audit and ROE

H5.2c: BOD mediates the relationship between Shariah audit and DER

5.3 The Function of BOD in Mediating the Impact of Shariah Risk and Performance of Islamic Banks

H5.3a: BOD mediates the relationship between Shariah risk and ROA

H5.3b: BOD mediates the relationship between Shariah risk, and ROE

H5.3c: BOD mediates the relationship between Shariah risk and DER

2.9.6 The Function of BOD in Mediating the Impact of Maqasid Shariah and Performance of Islamic Banks

The corporate governance theory based on maximizing stakeholders' interests has proven its effectiveness because it achieves competitiveness in winning the community's trust (Borlea & Achim, 2013). This function requires an effort to understand and meet the community's interests and needs of stakeholders. From the Islamic perspective, meeting the needs and safeguarding the interests of all parties is an essential element and a basis in achieving the Maqasid Shariah. In a corporate

organisation, every decision and planning are linked to corporate governance, where the BOD is one of the essential mechanisms in a sound corporate governance system. The company's performance depends on the corporate governance indicators' attributes by emphasising the BOD. Bukhair and Rahman (2015) state that the board may lead to higher monitoring, which may maximise the company's value through a study on the board structure and social contribution to the Islamic banks' performance.

Concerning the roles of Maqasid Shariah disclosure towards the performance of Islamic banks, the relationship between the performance of Islamic banks has been discussed in numerous studies that prove a significant relationship between Maqasid Shariah and the performance. However, in Islamic banks or other organisations, the board 's roles are pertinent. The board is responsible for setting and approving overall policy and strategy and monitoring progress toward corporate objectives (Chapra & Ahmed, 2002).

In addition, a study by Maali et al. (as cited in Issalih et al., 2015) emphasises the principle of full disclosure through accountability in meeting the community's needs by providing the necessary information to society about their transactions. This concept provides directions to the community to understand the influence of business operations to meet the public welfare and ensure that they conform with Shariah requirements (Bukair & Abdul Rahman, 2013). Consistent with the legitimacy theory, which attracts the public, the banks need to expose the activities that will benefit the community, showing that the institution is aware of the community to gain profit and interest.

Islamic banks principally differ from the conventional banks, which can be seen in the corporate objective, the control system, and the principles of the corporate governance system. The objective of Islamic banks towards the Shariah principles can

be related to the Maqasid Shariah. Other than that, Islamic banks consistently emphasise the welfare, need, and response to all the stakeholders that lead to the Maqasid Shariah achievement. This response has noticed the public, employees, community, and all stakeholders and given them values. It will lead to public awareness of the existence of an organisation that is consistent with its norm.

Thus, the Maqasid Shariah, as discussed, which arose from the relevant CSR elements, became a phenomenon influenced by the existence of the board by emphasising the relationships of the board within the management, stakeholders, and society as a whole (Money & Schepers, 2007). In relation, the stakeholder theory ensures that all relevant parties' interests are not neglected. This interest can win the trust and improve the company's economic performance (Borlea & Achim, 2013), and finally, achieve the Maqasid Shariah.

In addition, the stewardship theory also emphasises the banks' responsibility to provide the best practice and comply with the principles of Islamic banks for their customers and the community (Azmi et al., 2020; Donaldson & Davis, 1991). This theory always stands with the Shariah principles in serving the customers and the community at the best possible to achieve Maqasid Shariah. Meanwhile, in Islamic banks, the board acts as intermediation between implementing any policy strategy and monitoring banks' corporate objectives and activities toward the performance. Thus, with the stewardship theory, the board and SSB will perform the best possible to achieve the Maqasid Shariah and finally impact the banks' performance (Azmi et al., 2020). Hence, based on the discussion and related theory, this study hypothesized that:

H6a:	BOD mediates the relationship between Maqasid Shariah and ROA.
H6b:	BOD mediates the relationship between Maqasid Shariah and ROE.
H6c:	BOD mediates the relationship between Maqasid Shariah and DER.

Therefore, based on the theory and the discussion of prior studies, Table 2.8 shows the hypothesis statement generated in this study.

Table 2.8: Hypotheses Statement

1	Shariah Committee and Performance
H1a:	There is a significant relationship between SC disclosure and ROA.
H1b:	There is a significant relationship between SC disclosure and ROE.
H1c:	There is a significant relationship between SC disclosure and DER.
2	Shariah Audit and Performance
H2a:	There is a significant relationship between Shariah audit disclosure and ROA.
H2b:	There is a significant relationship between Shariah audit disclosure and ROE.
H2c:	There is a significant relationship between Shariah audit disclosure and DER.
3	Shariah Risk and Performance
H3a:	There is a significant relationship between Shariah risk disclosure and ROA.
H3b:	There is a significant relationship between Shariah risk disclosure and ROE.
H3c:	There is a significant relationship between Shariah risk disclosure and DER.
4	Maqasid Shariah and Performance
H4a:	There is a significant relationship between Maqasid Shariah and the ROA.
H4b:	There is a significant relationship between Maqasid Shariah and the ROE.
H4c:	There is a significant relationship between Maqasid Shariah and the DER.
5	Mediation Relationship
5.1	The Function of BOD in Mediating the Impact of SSB and Performance of Islamic Banks
H5.1a:	BOD mediates the relationship between SC and ROA.
H5.1b:	BOD mediates the relationship between SC and ROE.

Table 2.8 Cont.

H5.1c: BOD mediates the relationship between SC and DER.

5.3 The Function of BOD in Mediating the Impact of Shariah Risk and Performance of Islamic Banks

H5.3a: BOD mediates the relationship between Shariah risk and ROA.

H5.3b: BOD mediates the relationship between Shariah risk and ROE.

H5.3c: BOD mediates the relationship between Shariah risk and DER.

6 Mediation Relationship of BOD between Maqasid Shariah and Islamic Banks' Performance

6.1a: BOD mediates the relationship between Maqasid Shariah and ROA.

6.2b: BOD mediates the relationship between Maqasid Shariah and ROE.

6.2c: BOD mediates the relationship between Maqasid Shariah and DER.

2.11 Chapter Summary

This chapter has reviewed relevant studies on corporate governance, Shariah governance, Maqasid Shariah, Board, financial performance, and several related theories. This study is essential to identify and fill the gaps in Shariah governance and Maqasid Shariah studies. This chapter highlights Shariah governance in Malaysia's perspective and reviews related literature in the broader scope of studies. Likewise, the relevant Maqasid Shariah reviewed industry perspectives by integrating the CSR into the Maqasid Shariah. The function of the Board is reviewed in the Islamic and conventional perspective since the roles of the Board is similar in both views. Finally, based on the relevant literature and theories, this chapter produced the research framework and hypotheses.