PROCEEDING

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The 4th International Conference on Management Sciences
Universitas Muhammadiyah Yogyakarta, Indonesia

"Disruptive Innovation in Modern Business Era"

held in UMY, Indonesia, on March 28, 2018

Department of Management

FACULTY OF ECONOMICS AND BUSINESS

Universitas Muhammadiyah Yogyakarta

in collaboration with:

Universiti Sains Islam, Malaysia
Tamkang University, Taiwan
Khon Kaen University, Thailand

The 4rd International Conference on Management Sciences 2018 (ICoMS 2018)

March 28 2018

Universitas Muhammadiyah Yogyakarta, Indonesia

Chair Person

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2. Dr. Kawpong Polyorat (Khon Khaen University, Thailand)
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Preface IcoMS 2018

The 4rd International Conference on Management Sciences 2018 (ICoMS 2018)

March 28 2018

Universitas Muhammadiyah Yogyakarta, Indonesia

Dear Presenters and Delegates,

Department of Management, Economics Faculty, University of Muhammadiyah Yogyakarta, in collaboration with the Tamkang University Taiwan, Khon Kaen University Thailand, USIM Malaysia, organized an International Conference which will be held on March 28 2018.

We are proud to know that tehre is a thick manuscript submissions came to our table for this conference. In detail, there are 42 international academic manuscripts which we received from Indonesia, Malaysia, Thailand. And in this conference we choose **Disruptive Innovation in Modern Business Era** as the main theme.

Our international conference is a manifestation of the Government of Indonesia through the Directorate General of Higher Education, which has encouraged the internationalization of research and teaching in order to foster high-caliber academic institutions globally and increase competitiveness in International Higher Education.

We are very confident that our presenters and delegates will get a lot of ideas together and experience of this conference. In addition, our participants will enjoy additional insight from our plenary session keynote speakers, namely, Prof.Dr.Shu-Hsien Liao from Tamkang University Taiwan, Dr. Kawpong Polyorat from Khon Kaen University Thailand, Prof. Dr. Syadiyah Abdul Shukor from USIM Malaysia, and Punang Amaripuja, S.E., S.T., M.IT. from Universitas Muhammadiyah Yogyakarta.

Through this conference, we are committed to promote and improve our mission and academic culture synthesize global progress with local knowledge. Therefore, it is my great honour to welcome you to IcoMS 2018 in great cultural city of Yogyakarta, Indonesia. I look forward to seeing you soon in the conference.

Best wishes,

Dr. Indah Fatmawati

Chair of IcoMS 2018

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TABLE OF CONTENTS

The 4th International Conference on Management Sciences 2018 (ICoMS 2018)

Wednesday, March 28 2018

Universitas Muhammadiyah Yogyakarta, Indonesia

ICOMS 2018

THE DEPARTMENT OF MANAGEMENT
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The Role of Corporate Governance in Decreasing Risk and Increasing Earning of Sharia Bank in Indonesia

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Abstract

This study aims to identify the role of good corporate governance toward risk dan profit. Risk is measured with liquidity risk and credit risk. Profitability is measured with Return on Asset (ROA) and operational efficiency ratio (BOPO). This study used data from annual financial report of Sharia bank from 2012 until 2016. This study sample used 11 Sharia banks as a sample with 53 observations. The regression analysis was done with Eviews program. The result showed that Good Corporate Governance has positive significant effect toward ROA; Good Corporate Governance has significant negative effect toward BOPO. The impact of Good Corporate Governance toward Non Performance Finance (NPF) is negatively significant, therefore Good Corporate Governance has no significant effect toward Finance Deposit Ratio (FDR)

Keywords: *Good Corporate Governance, ROA, BOPO, NPF, FDR*

BACKGROUND

Bank is one of the components in the economy of a country that plays an important role in economic growth, and it involves many parties and is exposed to many risks in practice. Banks must have the ability to maintain the trust of stakeholders, investors and the community towards the bank, so application of GCG to the banking world is needed. Good Corporate Governance (GCG) is basically a system that organizes, manages, and oversees the business management process to smoothen relationships among management, shareholders, and other interested parties, and the goal is to create added value for the company. In a broader aspect the application of GCG principles is to gain the trust of the surrounding community. To improve the quality of good management and operations, BI issued Circular Letter of Bank Indonesia Number: 9/12 / DPNP Date May 30, 2007, which is the implementation guidance of PBI 8/4 / PBI / 2006, which has been updated with PBI No. Bank Indonesia through the SE, explains in more detail the five GCG principles; transparency, accountability, responsibility, independency, and fairness.

Overall the concept of corporate governance arises as an attempt to brake or overcome self-serving management behavior by creating mechanisms and control instruments to enable a balanced profit and wealth sharing system for stakeholders and create efficiency for the company (Shindhunata and Cynthia, 2005). With corporate governance, it is hoped that the company can live sustainably and give benefit to the stakeholders (Yusriati et al, 2010).

Principles of GCG implementation are realized in the implementation of the duties and responsibilities of the Board of Commissioners and the Board of Directors; completeness and execution of duties of committees and working units which operate the bank's internal control functions; implementation of compliance function, internal auditor and external auditor; implementation of risk management, including internal control system; provision of funds to related parties and provision of substantial funds; the bank's strategic plan; and transparency of financial and non-financial conditions. Each bank is required to conduct a self-assessment on the implementation of GCG, prepare its GCG implementation report periodically, and then will be assessed by BI (Booklet of Indonesian banking, 2012).

With the measurement of corporate governance practices at the corporate level, many studies have found a positive relationship between corporate governance and the value or performance of companies, including Black et al. (2003); Klapper and Love (2002); Siddharta and Cynthia (2005). Purba’s (2011) study on the effect of GCG on the financial performance of 30 banking companies listed on the Indonesia Stock Exchange shows that GCG implementation has significant effect on BOPO and ROE ratio, and GCG has no significant effect on CAR, ROA, LDR, and NIM. Research conducted by Syam and Nadja (2012) see the effect of GCG implementation quality on financial performance at seven sharia banks in Indonesia. The results show that the quality of GCG implementation has no significant effect on ROA and the quality of GCG implementation has significant effect on the NPF. The diversity of previous research results makes the writers interested in conducting a research related to the role of GCG to risk and profit in sharia commercial banks in Indonesia

THEORETICAL BACKGROUND AND HYPOTHESIS FORMULATION

1. Theoretical review

Corporate Governance in Indonesia (FCGI) Forum defines Good Corporate Governance as a set of rules governing relationships among shareholders, managers of companies, creditors, government, employees and other internal and external leadership holders of their rights and obligations or in other words a system that regulates and controls the company. The purpose of corporate governance is to create added value for all stakeholders. According to Yudistira (2004), corporate governance encompasses the ways of directors, senior management and the entire organization in managing businesses and institutions, and influences how banks:

1. Setting company goals
2. Running daily operations
3. Consider the interests of stakeholders
4. Aligning the activities and behaviors of the company in the hope that the bank will operate safely and steadily and comply with law and regulation
5. Protecting the interests of depositors

Based on Bank Indonesia Circular Letter No 13/24 / DPNP in 2011, Good Corporate Governance becomes one of the components of bank health assessment. BI Regulation is in connection with the implementation of Good Corporate Growth since the issuance of Bank Indonesia Regulation (PBI) no. 8/4 / PBI / 2006 dated January 30, 2006 on the Implementation of Good Corporate Governance for Commercial Banks as amended by Bank Indonesia Regulation no. 8/14 / PBI / 2006 dated 6 October 2006 and Bank Indonesia Circular Letter No. 9/12 / DPNP dated May 30, 2007. The general rules stipulated in Bank Indonesia Circular Letter No. 9/12 / DPNP are among others:

1. Transparency, namely openness in expressing material and relevant information and openness in decision making process. Second, accountability is the clarity of the function and implementation of the Bank's organ liability so that its management runs effectively. Third, the responsibility is the suitability of Bank management with the prevailing laws and regulations and sound Bank management principles. Fourth, independency is the professional management of the Bank without the influence / pressure of any party. Fifth, fairness is justice and equality in fulfilling the rights of stakeholders arising based on the agreement and the prevailing laws and regulations. In order to apply the five basic principles mentioned above, the bank must be guided by various prevailing laws and regulations related to the implementation of GCG.
2. Banks are required to implement GCG principles in their business activities at all levels or levels of the organization. What is meant by all levels or levels of the organization is the management and employees of the bank ranging from board of commissioners and directors up to executing officers.
3. In implementing the transparency as mentioned above, banks are required to submit reports on the implementation of good corporate governance. The existence of such report, is needed to educate and improve the check and balance of bank stakeholders and competition through market mechanism.
4. In the effort to improve and increase the quality of the implementation of good corporate governance, banks are required to periodically conduct a comprehensive self-assessment of the adequacy of GCG implementation, so that if there are still deficiencies in its implementation, the bank may immediately establish an action plan covering corrective action required.

The purpose of corporate governance is to create added value for all stakeholders, as a form of implementation in realizing a healthy banking government by applying a blueprint formed by the Indonesian Banking Architecture (API) which is the embodiment of the vision of the national banking system. As for the realization of the program the government has made a foundation based on 6 (six) pillars, among others (Erwin and Eko, 2007).

1. Creating a healthy domestic banking structure capable of meeting the needs of the community and promoting sustainable national economic development
2. Creating an effective bank regulatory and supervisory system and refers to international standards
3. Creating a strong banking industry and have high competitiveness and have resilience in facing risk
4. Creating GCG in order to strengthen the internal condition of the national banking system
5. Realizing a complete infrastructure to support the creation of a sound banking industry
6. Achieving empowerment and consumer protection of banking services

Shleifer and Vishny (1997) state that corporate governance, a concept based on agency theory, is expected to serve as a tool to give investors confidence that they will receive a return on the funds they have invested. Corporate governance deals with how investors believe that managers will benefit them, believes that managers will not embezzle or invest in unprofitable projects relating to invested funds / capital, and how investors control managers. In other words, corporate governance is expected to work to reduce or decrease agency costs.

Implementation of GCG is considered to improve the image of the banking, to protect the interests of stakeholders and to improve compliance with applicable legislation and general ethics in the banking industry in order to improve the sound banking system, reduce the risk due to management actions that tend to benefit themselves (Totok, 2010).

Composite Value of GCG self-assesment of of companies are measured and grouped into five levels as follows:

a. Composite Values of GCG self-assessment < 1,5 shows a very good condition
b. Composite Values of GCG self-assessment 1,5 – 2,5 shows a good condition
c. Composite Values of GCG self-assessment 2,5 - 3,5 shows a pretty good condition
d. Composite Values of GCG self-assessment 3,5 - 4,5 shows a less good condition
e. Composite Values of GCG self-assessment 4,5 - 5 shows a not good condition

Source: Bank Indonesia Circular Letter Number 15/15/DPNP (2013)

2. Hypothesis formulation

a. GCG and Non Performing Financing (NPF)

Non Performing Financing (NPF) is the ratio between non performing financing on total financing disbursed. The NPF ratio aims to measure the level of problem financing faced by banks. The higher this ratio indicates that the quality of financing in banks is getting worse (Bank Indonesia Circular Letter, 2007). Basically, the bank has an intermediary function between the party who needs the funds and the one which has excess funds. Distribution of funds from banks is expected to minimize the risk of failure of loan repayment. Given the principle of good corporate governance, banks become more careful in channeling funds. The existence of GCG principles is important, as this principle will assist the bank in carrying out the existing principles and be able to guarantee the rate of return borrowed and provide the maximum profit for the bank (Surya and Yustiavandana, 2008). The principle of openness is very important to implement, because it is able to prevent misuse of funds provided in order to save expenditure of funds in case of deviation. In the end, the application of GCG principles to the banking world is closely related to the channeling of funds to be provided by banks to prospective borrowers by prioritizing prudential principles. Thus, when banks implement GCG, the level of problem in financing will decrease, due to the application of prudential banking of banks in disbursing funds (Pratiwi, 2016). Based on the description, hypothesis 1 proposed in this research are:

H1 = Quality of GCG implementation has a positive effect on NPF ratio.

b. GCG and FDR

The ratio of Financing Deposit Ratio (FDR) is the ratio between the amount of financing disbursed and the total funds of third party. The FDR ratio is used to assess the bank's ability to meet liquidity requirements and adequacy of liquidity risk management. When a bank is unable to maintain its liquidity level, it can lead to an unavoidable liquidity crisis in the bank, meaning a decrease in the trust level of the community to the bank. Given the principles of good corporate governance, banks are becoming more cautious in channeling their funds to avoid a crisis of confidence with the rush on the banks. The existence of GCG principles becomes important, because this principle will help the bank in carrying out the existing principles and can improve the trust or image of the banking.

It can be deduced that the application of GCG principles will affect the level of liquidity in the bank. Based on the description above, hypothesis 2 is formulated as follows:

H2 = The quality of GCG implementation influences the FDR ratio.

c. GCG and ROA

The Return on Assets (ROA) ratio is the ratio of earnings before tax to the average earning assets. ROA ratio measures the ability of bank management to generate profit from total assets owned. The greater the ROA of a bank, the greater the rate of profit achieved and the better the bank's position of asset use (Taswan, 2010). Basically the company's management is the business wheel that drives the company in the search for profit. The success can be achieved by the implementation of the principles of GCG as a whole. Implementation of GCG mechanism basically has a purpose to give progress to the performance of a company, one of which is profitability of company. Thus, the implementation of GCG principles can improve the profitability of the company due to the success of the performance achieved.

According to a research conducted by Black, et.al (2003), there is a strong and robust relationship between the implementation of GCG with the profitability of companies in South Korea and Russia (Black, 2001). These findings highlight that companies with GCG will perform better both financially and in market value. There is a need to perform a similar research in Indonesia.
Based on the description and previous research that has been done, the hypothesis 3 proposed in this study is:

H3 = The quality of GCG implementation has a positive effect on ROA ratio.

d. GCG and BOPO

BOPO ratio is the ratio between operational cost and operating income. The purpose of BOPO ratio is to measure the efficiency of operational activities of Sharia banks. The smaller the ratio of operational costs will be better, because the cost incurred is smaller than the income received (Taswan, 2010). Some benefits that can be gained by implementing corporate governance based on Forum for Corporate Governance in Indonesia (2001), among others, are to improve the performance of the company through the creation of better decision-making process, to improve the operational efficiency of the company and to improve the service to stakeholders.
Based on the description, it can be concluded that the implementation of GCG can improve the operational efficiency of the company, including in it is the operational cost efficiency incurred by the company in its activities. This means that there is a strong influence between the implementation of GCG with the level of operational efficiency of the company. The better the implementation of good corporate governance, the more efficient or smaller the BOPO is.

Based on the above explanation, hypothesis 4 proposed in this study is:

H4: The quality of GCG implementation negatively affects the BOPO ratio.

RESEARCH METHOD

1. **Population and Sample**
   The objects of this research are companies listed on The Indonesian Stock Exchange (BEI) that implement Good Corporate Governance (GCG), with the observation samples period starting from 2012 to 2016. Sampling was done by using purposive sampling, namely the determining the sample with a target or specific considerations (Sekaran, 2003).

The criteria used in this study are as follows:
1. Sharia Commercial Banks in Indonesia during 2012-2016
2. Issuing Annual Report from 2012-2016
3. Delivered GCG reporting as measured using composite values
4. Have a positive ROA during the study period.

Variables and Variables Measurement

In this research, we use Good Corporate Governance (GCG) as an independent variable and 4 (four) dependent variables; Return on Asset (ROA), Operational Efficiency Ratio (BOPO), Non Performing Loan (NPF), and Financing Deposit Ratio (FDR). The measurement of each variable is as follows:

Table 1. Variables Measurement

No.	Variable	Notation	Measurement
1	Good Corporate Governance	GCG	based on the self-assessment of bank GCG implementation report. Its maximum score is 5. The lower the index of GDG, the better its implementation. So that, GCG in this research was measured by 5-scale index of GCG.
2	Return on Asset	ROA	$ROA = \frac{Income\ Before\ Tax}{Avarage\ of\ Total\ Asset} x100\%$
3	Operational Efficiency Ratio	BOPO	$BOPO = \frac{Total\ Operating\ Cost}{Total\ Operating\ Income} x100\%$
4	Non-Performing Loan	NPL	$NPL = \frac{Total\ Substandard\ Loans + Total\ Doubtful\ Loans}{Total\ Loans}$
5	Financing Deposit Ratio	FDR	$FDR = \frac{Financing}{Deposit}$

2. The Data Analysis

This research used linier regression model to measure the impact of Good Corporate Governance implementation to profitability and risk of sharia banking in Indonesia by Eviews program. Simple linear regression analysis can be used if an equation in the regression model has one independent variable (Ghozali, 2006). The regression model is as follows:

Model 1: $ROA = \alpha + \beta_1 GCG + e$

Model 2: $BOPO = \alpha + \beta_1 GCG + e$

Model 3: $NPF = \alpha + \beta_1 GCG + e$

Model 4: $FDR = \alpha + \beta_1 GCG + e$

Clues:

α : Constants

β : Regression Coefficient

ROA : Return on Asset

BOPO : Opperational Efficiency Ratio
NPF : Non Performing Finance
FDR : Finance Deposit Ratio
GCG : Good Corporate Governance
E : Error

Descriptive statistics

Descriptive statistic is statistic that describes a phenomenon or characteristic of data (Jogiyanto, 2004). Descriptive statistics will provide an overview of research variables related to minimum values, maximum values, mean, and standard deviation.

Classic Assumption Test

Classic assumption test used in this research consists of:
1. Normality Test
2. Multicolinearity test
3. Heteroscedasticity Test
4. Autocorrelation Test

Coefficients Determination

Ghozali 2011, states that R value is used to measure the ability level of the model in explaining the variations which are too limited. The value of the coefficient of determination (R) is between 0 (zero) and 1 (one), where the value of R is small or close to zero means that the ability of independent variables in explaining the variation of the dependent variable is very limited, but if the value of R is large or close to 1 independent variable it means that independent variables provide almost all the information needed to predict the variation of the dependent variable.

Partial Test (t Test)

According to Gozali (2011), the base of t test shows how far the effect of 1 independent variable individually in explaining the dependent variable. Hypothesis is accepted if value sig < 0,05.

RESULTS AND DISCUSSION

Independent variable used in this research is Good Corporate Governance (GCG). The dependent variables are Return on Assets (ROA), Opperational Efficiency Ratio (BOPO), Non Performing Finance (NPF) and Finance Deposit Ratio (FDR).

Table 1
Estimated coefficients for ROA, BOPO, NPF and FDR

Independent Variables	Dependent Variables			
	NPF	FDR	ROA	BOPO
Constant	7.292255 (0.0000)	9.770974 (0.0000)	-1.979565 (0.0532)	9.498539 (0.0000)
GCG	-5.505406 (0.0000)*	-1.473962 (0.1466)	2.566807 (0.0132)*	-3.779904 (0.0004)*
Adjusted R-Squared	0.360468	0.022052	0.114406	0.203525
F Statistic	(30.309500)	(2.172565)*	(6.588497)	(14.28767)
* Sig 5%				

Source: Result of data processing

1. The effect of GCG toward NPF

The result of hypothesis test 1 shows that the quality of GCG implementation has a significant positive effect on NPF ratio in Sharia bank. Bank is an institution that prioritizes the prudential principle in channeling its funds and the occasional evaluation of risk management in order to minimize the level of problem financing. Bank Indonesia Regulation in the implementation of GCG requires BUS to have a Risk Management Committee and Risk Management Unit which in theory can reduce the risk of financing arising. It is reinforced by internal and external audit function which also reduces financing risk in BUS (Syam and Nadja, 2012). This means that the indicators set by Bank Indonesia in the implementation of GCG can reduce the problematic financing that arise in the BUS. The result of the research is in accordance with Pratiwi’s (2016) study which shows that the quality of GCG implementation has an effect on NPF ratio.

2. The effect of GCG toward FDR

The quality of GCG implementation does not affect the ratio of FDR to Sharia commercial banks. Theoretically, the implementation of GCG can increase the customers' trust to channel their funds or to finance the bank. The FDR ratio is used to assess the bank's ability to meet liquidity requirements and adequacy of liquidity risk management. When a bank is unable to maintain its liquidity level, it causes an unavoidable liquidity crisis for the bank. This means there is a decrease in the level of trust of society to the bank. On the other hand, according to the Forum for the Corporate Governance in Indonesia (FCGI) (2001), the benefits that can be gained through the implementation of corporate governance are, among others, further improving services to stakeholders, thereby enabling GCG implementation to increase customer confidence in channeling funds or financing at banks.

The results are in line with Purba’s (2011) study which stated that GCG implementation does not affect the LDR ratio in 30 conventional banks listed in Indonesia Stock Exchange. The quality of GCG does not seem to affect the FDR and LDR in Sharia banks and conventional banks. Good corporate governance has not been able to increase the amount of financing disbursed to the public, nor does it make banks more strict in lending to meet the level of liquidity.

3. The effect of GCG toward ROA

The results showed that the quality of GCG application had a significant positive effect on ROA ratio. ROA ratio shows how much net profit can be obtained from the wealth owned by the company and show the company's ability to generate profit. The implementation of good GCG mechanism causes the company to increase its assets. Good management can encourage the effectiveness of the use of company assets and improve the ability of banks in obtaining net income, so as to increase the profitability ratio of the company. This is in accordance with the research conducted by Black et al, (2003); Klapper and Love (2002).

4. The effect of GCG toward BOPO

Based on hypothesis test to 4, the result shows that GCG has a significant negative effect on BOPO ratio in Sharia bank. BOPO ratio is the ratio between operational cost and operating income. The purpose of BOPO ratio is to measure the efficiency of bank operations. The implementation of good corporate governance encourages the performance of the company to work more efficiently, including improving the operational efficiency of the company's activities, in accordance with the Forum for the Corporate Governance in Indonesia (FCGI) (200), which states that the benefits of GCG can improve the company's performance through the creation of the process of taking better decisions, and improve the operational efficiency of the company.

CONCLUSION

Based on the results of the analysis that has been done, it can be concluded that:

1. The risk proxy in this study which is represented by NPF and FDR variables shows different results. Good Corporate Governance proved to have a significant positive effect on NPF, while Good Corporate governance is not proven to significantly affect FDR. Variable of Good Corporate Governance is proven to reduce risk in Sharia Commercial Bank with Non-Performing Loan (NPF).

2. Proxy gained in this study which is represented by ROA and BOPO variables shows significant results. GCG proved to have a significant positive effect on ROA and have a significant negative effect on BOPO. Good Corporate Governance variable is proven to increase profit and can make Sharia Commercial Bank more efficient in its operational activities.

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