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The Influence of Corporate Governance on Earnings Management: An Empirical Analysis on Islamic Banks

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Abstract. The problem of financial statement fraud in the banking industry, including Islamic banks, has become an important issue because it has an impact on customer trust. This research aims to analyze the role of governance in reducing earnings management in Islamic banks in Indonesia. This study is relevant and important because there are still only a limited number of studies that examine governance and earnings management in Islamic banks and use the quality of auditing by public accounting firms as an additional variable. The sample comprises 80 firm-year observations from Indonesian Islamic banks during the 2017-2022 period. The independent variables analyzed are the effectiveness of the sharia supervisory board (SSB), the board of commissioners, and the audit committee. The dependent variable is earnings management as measured by discretionary loan loss provisions (DLLP). The moderator variable is auditor quality. The test results using the partial least squares (PLS) technique show that the effectiveness of the SSB has no influence on earnings management (β=0.081, p-value=0.21). Meanwhile, the effectiveness of the board of commissioners has a significant negative influence on earnings management (β=-0.402, p-value <0.01) and the audit committee has a negative influence on earnings management (β=-0.071, p-value=0.04). The results of testing the moderating role of the public accounting firm's auditor quality show that only hypothesis 5 is supported (β=-0.187, p-value=0.03). The practical relevance of this study is the importance of regulators and the government in strengthening the role of the board of commissioners, audit committee, and auditing by public accounting firms and SSBs in preventing and reducing the practice of manipulating financial reports in Islamic banks.

Keywords: Islamic bank, earnings management, sharia supervisory board, board of commissioners, audit committee, Auditor

1 Introduction

Islamic banks need to ensure that their management of resources, earnings, and financial reporting accord with Islamic principles. Therefore, it is the duty of those responsible for corporate governance to ensure that the financial reports published by Islamic banks are free from the kinds of fraud or manipulation that diminish their image and increase the risk to their reputation. Nevertheless, there have been several cases of fraudulent financial statements being issued by Islamic banks in Indonesia, namely statements based on aggressive earnings management practices. The existence of these scandals is one of the reasons for the lack of public trust in Islamic banking which has resulted in its market share declining between 2017 and 2022. This is unbalanced given the number of Muslims in Indonesia; they make up 86.9% of the country's total population.

Research on corporate governance and earnings management in Islamic banks is very limited compared to the research that has been conducted on conventional banks. Furthermore, the findings of the existing research have been inconsistent because it has limited its analysis of earnings management to Islamic corporate governance mechanisms from the internal perspective only. Research that discusses earnings management in terms of the quality of auditing that Islamic banks undergo is still rare. Therefore, this study adds the variable of auditor quality which functions as a means of examining the external side of a company by measuring the degree to which external auditors limit earnings management. This is because external auditors can provide guaranteed information about the quality and credibility of the company. Good quality external auditors are a guarantee of financial reports that avoid earnings management. It is necessary to have an independent and competent external party to reduce concerns about the manipulation of financial reports.

This research is important and relevant in several ways. First, this study focuses on the context of Islamic banks, whereas previous research has generally focused on conventional banks. Second, this research analyzes the role corporate governance in Islamic banks plays in reducing earnings management practices by adding several variables that have only been analyzed to a limited extent, namely the role of the sharia supervisory board (SSB) and the quality of auditors. This study develops a model in which auditor quality moderates the influence of Islamic corporate governance on earnings management.

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2 Literature Review

This study uses the stewardship theory to develop a research model. The stewardship theory, which is also known as governance theory, is based on psychological and sociological concepts where the executive board acts as the manager (steward) and is encouraged to act in the interests of the party providing the mandate (principal) (Donaldson & Davis, 1991). In this case, stewards work hard to realize organizational goals, for example by looking at sales growth or profitability. This behavior is a collective trait possessed by stewards; as managers, they will maintain and optimize ownership value for shareholders through achieving company performance, because this will effectively increase the utilization of governance principles (Donaldson & Davis, 1991).

Islamic banks are financial institutions that operate in accordance with sharia principles, meaning that, in their operations, the banks follow the provisions of sharia law, especially with regard to commercial transactions (*muamalat*). The aim of Islamic public banks, in general, is to encourage and accelerate the economic progress of a society by carrying out banking, financial, commercial, and investment activities in accordance with sharia rules. This is what differentiates it from conventional banks whose main goal is to achieve the maximization of profit (Athief 2024; Mamatzakis et al., 2022; Salman et al., 2023; Zainudin & Lui, 2020; Aslam & Haron, 2020). Islamic banking activities are an application of Islamic sharia principles with characteristics including the prohibition of usury in various forms, the concept of money as a medium of exchange and not as a commodity, and not being permitted to carry out speculative activities.

Islamic banks are recognized in normative juridical and empirical juridical terms in Indonesia and various other countries. Normative juridical recognition is incorporated into Indonesian laws and regulations while, in empirical juridical terms, Islamic banks are given broad opportunities to develop their business throughout Indonesia (Sudiyatno et al., 2023). As Islamic financial institutions, sharia commercial banks, in carrying out their business activities, must refer to sharia principles (Suripto et al., 2023). Compliance with sharia values and good Islamic corporate governance are aspects that differentiate conventional and sharia systems (Mamatzakis et al., 2022; Mutamimah & Saputri, 2022; Choudhory, 2008; Alam & Homy, 2020; Choudory & Hoque, 2006).

In Bank Indonesia Regulation (PBI) No.11/33/2009 concerning the Implementation of Good Corporate Governance (GCG) for Sharia Commercial Banks and Sharia Business Units, it is stated that the implementation of GCG in the Islamic banking industry must comply with sharia principles. Sharia compliance is an Islamic bank's obligation to comply with sharia principles. This is what differentiates the GCG of conventional banks and the GCG of Islamic banks. In Indonesia, the sharia principles referred to are the principles of Islamic law in banking activities based on fatwas issued by the *Dewan Syariah Nasional* (National Sharia Council) which was formed by the *Majelis Ulama Indonesia* (Indonesian Ulema Council). PBI No.11/33/2009 outlines the implementation of the duties and responsibilities of the sharia supervisory board (SSB) which is an organ of governance that performs advisory and supervisory functions for an Islamic bank, thereby regulating the fulfillment of sharia principles in the assembling and distribution of banking services.

According to the stewardship theory, there is a need for effective internal corporate governance in order to mitigate earnings management practices in companies (Ratmono & Frendy, 2022). In this research, internal governance can be measured in terms of the effectiveness of the SSB as a form of Islamic corporate governance involved in Islamic banking. In addition to this, there is the effectiveness of the board of commissioners, the effectiveness of the audit committee, and the quality of the auditors. Corporate mechanisms in Islamic banks are very important for improving performance and cost efficiency and reducing risk (Nurkhin et al., 2023; Mamatzakis et al., 2022; Mutamimah & Saputri, 2022; Pahlevi, 2022; Noor & Mohamed, 2019; Bhatti & Bhatti, 2010; Boulila Taktak, 2011)

An SSB has the responsibility to safeguard company assets and ensure that the financial reports produced are accurate. Basically, if the SSB actually carries out its responsibilities and duties, corporate governance can function well (Sueb et al., 2022). This will be even better if the number of members is larger because the SSB's performance will be more effective with each member being able to share his or her experience and expertise with others. According to stewardship theory, the effectiveness of collaboration between SSB members and managers will also minimize earnings management. Aside from these factors, the effectiveness of an SSB can be seen in terms of how often it holds meetings. Furthermore, the expertise of an SSB's members is also an important element in mitigating earnings management in banking (Sueb et al., 2022). This is because, in essence, earnings management is an activity that is not permitted according to Islamic principles. Research by Alam & Homy (2020), Elnahass et al. (2022), and Mukhibad et al. (2021) shows that the level of SSB effectiveness in mitigating earnings management can be measured by SSB size, frequency of SSB meetings, and the financial expertise of its members.

In the corporate governance structure in a company, the board of commissioners has an important role to play (Dwiharyadi, 2017). The effectiveness of the board of commissioners can be measured by how many members it has. It must consist of at least two members, including an independent commissioner. The greater the number of commissioners, the more effective its supervisory function will be. Aside from this, its effectiveness can also be balanced with the frequency of its regular meetings. To carry out supervision and provide advice on decision-making in a company, the board of commissioners needs to have members with financial expertise. If all indicators are implemented, the role played by the board of commissioners will be more effective. Therefore, this effectiveness is proxied by board size, frequency of meetings, and the independence and financial expertise of its members (Mamatzakis et al., 2022). This is supported by the research of Abdelsalam et al. (2021); Elnahass et al. (2022); Fitri & Siswantoro (2021); Mangala & Singla (2021); Usman et al. (2022) and Aleqab & Ighnaim (2021). If the board of commissioners effectively carries out its duties, it can pressure managers to produce financial reports transparently. This makes mitigating the occurrence of earnings management in the company easier.

The audit committee in a company has the important role of ensuring that financial reports are accurate, although the management of Islamic banks is already governed by rules regarding everything that is reported in so far as it must be appropriate and in accordance with Islamic principles. However, this is better achieved with the help of an audit committee that gives the principal a sense of trust in the stewards. This means that the committee needs to have members who are experts in the fields of finance and accounting. The frequency of audit committee meetings and the number of audit committee members are also factors that support the production of accurate financial reports. This shows that the effectiveness of the audit committee in suppressing earnings management practices can be seen from the size of the committee, the frequency of its meetings, and the financial expertise of its members. These indicators can support the effectiveness of the audit committee, thereby reducing the possibility of earnings management and even fraudulent financial statements (Mousavi et al., 2022). Previous research by Almarayeh et al. (2022); Fitri & Siswantoro (2021); Mangala & Singla (2021); Mollik et al. (2020) proves that audit committee size, meeting frequency, and financial expertise can reduce earnings management practices. This indicates that there is a negative relationship between audit committee effectiveness and earnings management.

An external auditor is a licensed public accountant who analyzes the financial records and business activities of a company while having no membership relationship with the company (DeAngelo, 1981). The quality of the auditor is seen in terms of his or her capability to predict, identify, and report the findings of the audit process carried out; therefore, the confirmation of an external auditor will increase the integrity of the company's financial reports. The professionalism of the experts at the “Big 4” public accounting firms (hereafter Big 4 auditors) is believed to be able to provide effective audit services and quality (Yang et al., 2017). Apart from that, industry-specialization auditors are also considered capable of reducing earnings management and being able to predict the company's future cash flows because they have more knowledge about the industries they specialize in (Gerayli et al., 2011).

Previous research shows that the quality of auditors in a company can be seen in terms of the size of the public accounting firm, that is to say the Big 4 auditors, and industry-specialization auditors who are considered more professional in conducting audits of financial reports, meaning the detection of earnings management can be easier and more effective. This is because the Big 4 auditors have a lot more experience than non-Big 4 auditors (Alves, 2013; Farook et al., 2014; Alzoubi, 2018; Harianto, 2022) and industry-specialization auditors have more knowledge about the industries they specialize in (Gerayli et al., 2011; Lennox & Pittman, 2010). Therefore, it can be concluded that there is a negative relationship between auditor quality and earnings management. This study aims to analyze the influence of corporate governance on earnings management in Islamic banks with auditor quality as a moderating variable.

Based on the literature review, the following hypotheses are proposed:

H1: The effectiveness of the sharia supervisory board has a negative influence on earnings management.

H2: The effectiveness of the board of commissioners has a negative influence on earnings management.

H3: The effectiveness of the audit committee has a negative influence on earnings management.

H4: Auditor quality strengthens the negative influence of the effectiveness of the sharia supervisory board on earnings management.

H5: Auditor quality strengthens the negative influence of board of commissioners effectiveness on earnings management.

H4: Auditor quality strengthens the negative influence of audit committee effectiveness on earnings management.

3 Methods

The population is all Islamic banks in Indonesia during the 2017-2022 period. Sample selection used the purposive sampling method, with the following criteria:

1. Islamic banks registered with the Financial Services Authority (OJK) consecutively during the 2017-2022 period.
2. Islamic banks that published annual reports on their respective websites and other official websites during the 2017-2022 period.

The dependent variable in this research is earnings management with a model developed by Othman (2016), Ashraf et al. (2015), and Othman & Mersni (2014) using discretionary loan loss provisions (DLLP). The independent variables are the effectiveness of the SSB, the board of commissioners, and the audit committee. The effectiveness of the SSB and the audit committee is measured, in both cases, by the number of members, the number of meetings, and the expertise of their members in the field of finance. Meanwhile, the effectiveness of the board of commissioners is measured by the number of members, the number of meetings, and its members' independence and expertise in the financial sector. The moderating variable in this study is the quality of auditors from public accounting firms as measured by their specialization in the banking industry and being from one of the Big 4 auditors.

The data were analyzed using the structural equation model (SEM) approach with the partial least square (PLS) method. Using WarpPLS software is one of the techniques used to operate structural equation models. The reason for choosing the PLS method is because it is suitable for testing the variables of effectiveness of the SSB, effectiveness of the board of commissioners, effectiveness of the audit committee, and quality of auditors, each variable using three or four formative indicators. Through the application of PLS, the results of the data processing process can be accepted simultaneously.

4 Results and Discussion

The results of descriptive statistical analysis presented in Table 1 provide a description of the location size and dispersion of each research variable.

Table 1. Descriptive Statistics

Variables	Minimum	Maximum	Mean	Standard Deviation
Earnings Management	0.0067	0.9512	0.1567	0.1737
SSB SIZE	2.00	4.00	2.33	0.57
SSB MEETING	12.00	49.00	18.61	9.55
SSB EXPERTISE	0.00	1.00	0.73	0.35
BOC SIZE	2.00	10.00	3.98	1.41
BOC MEETING	6.00	37.00	14.21	6.45
BOC INDEPENDENCE	0.50	1.00	0.72	0.18
BOC EXPERTISE	0.50	1.75	0.81	0.32
AC SIZE	2.00	10.00	4.04	1.36
AC MEETING	12.00	48.00	18.64	6.62
AC EXPERTISE	0.30	1.00	0.96	0.13

EM = Earnings Management; SSB = Sharia Supervisory Board; BOC = Board of Commissioners; AC= Audit Committee

Earnings management is measured by discretionary loan loss provisions (DLLP) and the average DLLP value in Table 1 is 0.1567, which means that earnings management practices in Islamic banks in Indonesia are still relatively low, and a standard deviation of 0.1912t means that the results of this value are spread out. There are no big gaps in the data.

The first indicator of the independent variable sharia supervisory board (SSB) effectiveness is SSB SIZE which is the number of members on the SSB and there is a minimum value of 2.00 and a maximum value of 4.00. The average value of SSB SIZE is 2.33 and the standard deviation is 0.57. Therefore, it can be concluded that the minimum size of SSB members is in accordance with the stipulation of regulation PER-01/DSN-MUI/X/2017, namely that every sharia financial institution, sharia business institution, and sharia economic institution must have an SSB that has at least two members and one of them is designated as chairman. SSB MEETING is the frequency of SSB meetings as the second indicator of the SSB effectiveness independent variable. It has a lowest value of 12 and a highest value of 49, and the average value is 18.61; therefore, it is in accordance with Bank Indonesia Regulation No. 11/33/PBI /2009 Article 49 which states that SSB meetings must be held at least once a month. SSB EXPERTISE is the financial expertise of the SSB's members as the third indicator of the SSB effectiveness independent variable with a proxy which is the ratio between the number of SSB members who have financial and accounting expertise and the total number of members which shows a minimum value of 0.00 and a maximum value of 1.00. This means that there are still SSBs that do not have expertise in the financial sector and are instead limited to expertise in sharia principles.

The board of commissioners' effectiveness variable has several indicators. The first one is denoted by BOC SIZE or the size of the board of commissioners as a proxy for the number of members of the board of commissioners in an Islamic bank. BOC SIZE has a minimum value of 2.00 and a maximum value of 10.00 and the average value of the size of the board of commissioners is 3.98. Therefore, it can be concluded that the minimum size of members of the board of commissioners in this study is in accordance with the stipulation of OJK Regulation No. 33 of 2014, namely that the board of commissioners has a minimum of two members. The second indicator of the effectiveness of the board of commissioners variable is BOC MEETING or the frequency of board of commissioners meetings. BOC MEETING has a minimum value of 6.00 and a maximum value of 37.00 and has an average value of 14.21 and a standard deviation of 6.45. Thus, it can be concluded that the minimum frequency of board of commissioners meetings held based on the research data is in accordance with the stipulation of POJK No. 17 of 2023 Article 55 which states that the board of commissioners is obliged to hold regular meetings at least once every two months. BOC INDEPENDENCE or independence of the board of commissioners or the third indicator of the effectiveness of the board of commissioners independent variable with a proxy which is the ratio between the total number of independent commissioners and the total number of members of the board of commissioners. The test shows that the lowest value is 0.50 and the highest value is 1.00. The average value for the independence of the board of commissioners is 0.72, which means that in Islamic banking, on average, 72.00% of the members of the board of commissioners are independent commissioners. Therefore, it can be concluded that the value for the independence of the board of commissioners in this research is in accordance with the stipulation of POJK No. 17 of 2023 Article 38 Paragraph (1) that at least 50% of the number of members of the board of commissioners must be independent commissioners. The BOC EXPERTISE variable or the financial and accounting expertise of the board of commissioners is the fourth indicator of the the effectiveness of the board of commissioners independent variable with a proxy which is the ratio between the number of members of the board of commissioners who have financial and accounting expertise and the total number of members of the board of commissioners; this indicates a minimum value of 0.50 and the maximum value is 1.75. The average value of financial and accounting expertise for the board of commissioners is 0.81, which means that 81.00% of the members of the board of commissioners, on average, have financial and accounting expertise. It can be concluded that this result shows that, on average, companies are in accordance with the stipulation of POJK No.17 of 2023 that the board of commissioners must have members with expertise in the banking or financial sector.

AC SIZE is the size of the audit committee as the first indicator of the independent variable audit committee effectiveness which has the lowest value, namely 2.00, thus indicating conformity between the research data and the stipulation of POJK Regulation No.17 of 2023 Article 64, namely that there be a minimum of two members of the audit committee. And the highest value is 10.00. AC MEETING is the frequency of audit committee meetings as the second indicator of the independent variable audit committee effectiveness, which has a minimum value of 12.00 and a maximum value of 48.00, and an average value of 18.64. Therefore, it can be concluded that the minimum number of audit committee meetings is a frequency that is in accordance with the stipulation of OJK Regulation No.17 of 2023 Article 77, namely that there be at least one meeting of the audit committee per month or 12 times in one year. AC EXPERTISE or audit committee financial and accounting expertise, shows a minimum value of 0.30 and a maximum value of 1.00. The average value for the financial and accounting expertise of the audit committee is 0.9671, which means that the company has an average level of audit committee financial and accounting expertise of 96.71% of the total audit committee members. It can be concluded that almost all the audit committee members included in the research data have banking, financial, and accounting expertise in accordance with POJK regulation No.17 of 2023.

Table 2. Frequency Distribution of Auditor Quality Variable

Indicators	Category	Number	Percentage
Big 4 Auditor	Non-Big 4	47	58.75%
	Big 4	33	41.25%
Specialization	Non-Specialist	9	11.25%
	Specialist	71	88.75%

Based on the frequency distribution in Table 2, it can be concluded that 47 (58.75%) of Islamic banks use the services of non-Big 4 auditors, while the remaining 33 (41.25%) choose to use Big 4 auditors. Table 2 also indicates that 71 (88.75%) of Islamic banks use banking specialist auditors. The remaining nine (11.25%) do not use auditors who have special expertise in the banking industry. Thus, it can be concluded that the majority of Islamic banks in this research sample have been audited by auditors who have special expertise in banking.

This study uses the PLS-SEM method for hypothesis testing because there are several formative latent variables (Hair et al., 2022). Table 3 presents the results of testing the model fit index. It appears that all model fit indicators have met the criteria.

Table 3. Model Fit Indices

Criteria	Result	P-Values	Rule of thumb
Average Path Coefficient (APC)	0.169	0.022	P < 0.05
Average R-Square (ARS)	0.215	0.000	P < 0.05
Average Block VIF (AVIF)	1.545		≤3.3
Average Full Collinearity VIF (AFVIF)	1.380		≤3.3
Tenenhaus GoF (GoF)	0.394		≥0.25
Sympson's paradox ratio	0.833		≥ 0.70
R-squared contribution ratio	0.977		≥ 0.90
Statistical suppression ratio	0.833		≥ 0.90
Nonlinear bivariate causality direction ratio	1.000		≥ 0.00

With the goodness of fit evaluation having met the criteria, hypothesis testing is carried out using PLS-SEM. Figure 1 presents the results of hypothesis testing at the structural model stage. Meanwhile, a summary of test results and the conclusions are presented in Table 4.

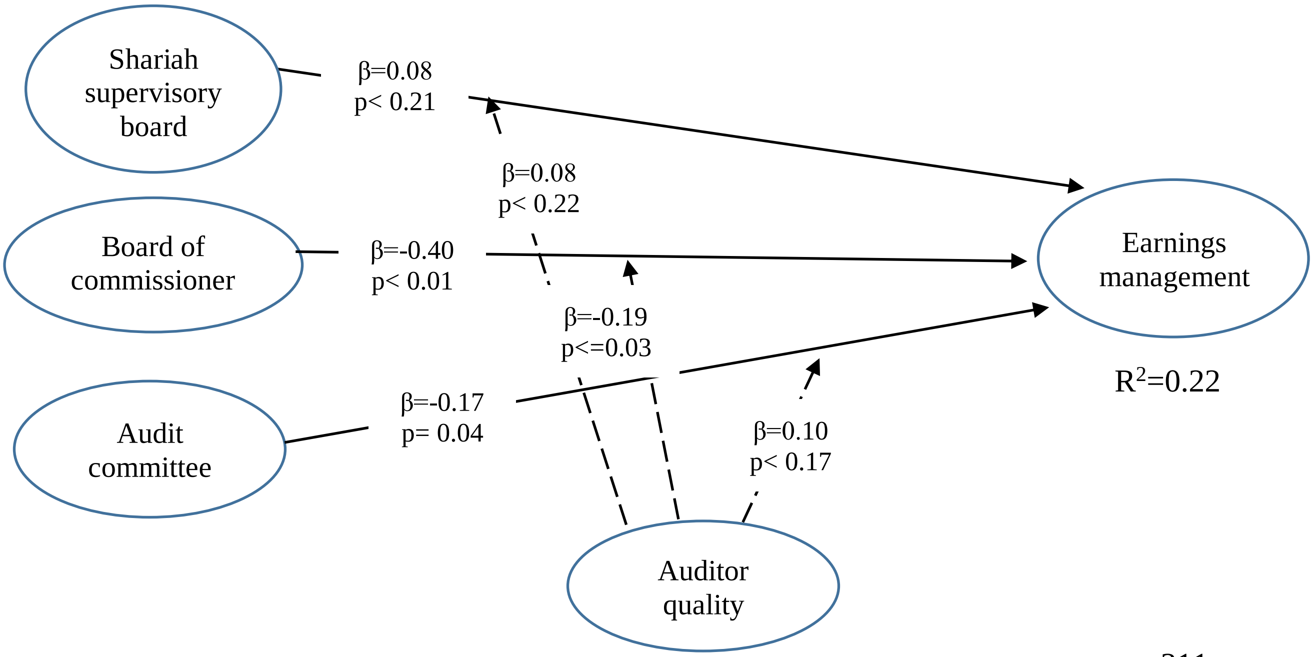

Fig. 1. Results of PLS-SEM analysis

The results presented in Figure 1 and Table 4 show that SSB effectiveness has no influence on earnings management (β=0.081, p-value=0.21), so **hypothesis 1 is not supported**. Meanwhile, the effectiveness of the board of commissioners has a significant negative influence on earnings management (β=-0.402, p-value <0.01), so **hypothesis 2 is supported**. Audit committee effectiveness has a negative influence on earnings management (β=-0.071, p-value=0.04). The results of testing the moderating role of public accounting firm auditor quality show that only **hypothesis 5 is supported** (β=-0.187, p-value=0.03). The test results show that **hypotheses 4 and 6 are not supported** so that the quality of public accounting firm auditors does not weaken the negative influence of SSB and SSB effectiveness on earnings management.

Table 4. Results of Path Coefficients and P-Values

Path	Expected Sign	*Coefficients*	Conclusion
Effectiveness SSB → Earnings Management	(-)	0.081	H1 not supported
Effectiveness BOC → Earnings Management	(-)	-0.402***	H2 supported
Effectiveness AC → Earnings Management	(-)	-0.171**	H3 supported
Effectiveness SSB*Auditor → Earnings Management	(-)	-0.077	H4 not supported
Effectiveness BOC*Auditor → Earnings Management	(-)	-0.187**	H5 supported
Effectiveness AC*Auditor → Earnings Management	(-)	0.096	H6 not supported

Note: *significant at alpha 10%, ** significant at alpha 5%, *** significant at alpha 1%

The PLS-SEM test results show that the first hypothesis is not supported. It can be concluded that the research findings show that the effectiveness of SSB has not been able to reduce earnings management practices. According to the descriptive statistics, there are still SSB members who do not have expertise in the financial sector. The findings of this research are different from those of Elnahass et al. (2022), Shira (2022), and Mukhibad et al. (2021) who show that SSB can mitigate earnings management in Islamic banks. This may be because the duties of SSBs are more focused on advising and supervising all bank activities so that they comply with sharia principles rather than financial reporting.

The test results show that the second hypothesis, which states that the effectiveness variable of the board of commissioners has a negative influence on earnings management, is supported empirically. The more effective the boards of commissioners in Islamic banks are, the less earnings management there will be. This result is likely because the sample of Islamic banks in this study has met the effective criteria. First, the average size of the board of commissioners is four people while POJK No.33 of 2014 stipulates that there be at least two members on a board of commissioners. Second, the average frequency of board of commissioners meetings is 14 times, which is in accordance with the stipulation of POJK No.17 of 2023 Article 55. Third, the independence of the board of commissioners, with an average of 72.00%, is in compliance with the stipulation of POJK No. 17 of 2023 Paragraph (1) that at least 50% of the board of commissioners in banking are independent. Fourth, the financial and accounting expertise of the members of of the board of commissioners, with an average of 81.00%, is also in accordance with the regulations. The results of this study are consistent with research by Mamatzakis et al. (2022), Aleqab & Ighnaim (2021), Lestari & Murtanto (2018), Mangala & Singla (2021), and Mardjono et al. (2020).

The test results also show that the effectiveness of the audit committee has a significant negative influence on earnings management. The more effective the audit committee in an Islamic bank is, the less earnings management there is. Based on the results of descriptive statistics, this research shows that the average value of the audit committee effectiveness variable with three indicators, first, size of the audit committee, frequency of meetings, and financial and accounting expertise is in accordance with POJK No.17 of 2023. The empirical evidence provided by this study supports previous research findings of by Mardjono et al. (2020), Mukhibad et al. (2022), Usman et al., (2022), and Anzelya & Kurniawati (2020). The effectiveness of the audit committee can be increased through regular meetings with internal and external auditors, with the aim of investigating any information in the audit process in order to reduce the risk of earnings management. Apart from that, with a large number of members on an audit committee, and if this is balanced with financial and accounting expertise, the effectiveness of the audit committee can also be more optimal in preventing earnings management.

The results of hypothesis testing for the moderating role of public accounting firm auditors show that only the fifth hypothesis is accepted. Auditor quality can moderate the negative influence of the effectiveness of the board of commissioners on earnings management. The findings from this moderation hypothesis test are consistent with the results of research conducted by Christiani & Nugrahanti (2014) and Alzoubi (2018) which showed that auditor quality has a negative influence on earnings management. Auditor quality cannot moderate the relationship between SSB effectiveness and earnings management, possibly because the interaction between the two is very limited. On the other hand, the effectiveness of the audit committee is not moderated by the quality of the public accounting firm auditor because the audit committee has sufficient competence to limit earnings management practices.

5 Conclusions and Suggestions

The results of this research provide empirical evidence that components of governance in the form of the effectiveness of the board of commissioners and audit committee can reduce earnings management in Islamic banks. The quality of the auditors from public accounting firms can strengthen the negative influence of the effectiveness of the board of commissioners on earnings management. Meanwhile, the role of the sharia supervisory board is more to focus on sharia compliance, so it cannot reduce earnings management in Islamic banks.

The implication of the results of this research is that it is important for Islamic banks to strengthen the role of the board of commissioners, audit committee, and public accounting firm auditors to prevent and reduce the practice of manipulating financial reports. The implication is that there is a need for regulators, in this case, the Financial Services Authority, to continue to improve the competency of these components of governance, including the sharia supervisory board, to minimize financial statement fraud in the banking industry. Regulators need to develop and evaluate various policies to prevent and minimize earnings manipulation in the banking industry because it can increase the risk to reputation.

The limitations of this study include the way the effectiveness of governance is measured using various indicators. While these indicators are the best proxies for governance research in Islamic banks when using quantitative methods, they are, however, limited in observing their implementation in detail. Future researchers could consider using qualitative methods to analyze the governance practices of Islamic banks in depth.

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