

# Factors that Influence Islamic Social Reporting

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## Abstract

Islamic banking is the largest sector in the Islamic financial industry. The development of Sharia banking must also be accompanied by accountability that is implemented correctly, both accountability to fellow humans and accountability to Allah SWT. One form of accountability is social responsibility, or what can be called Islamic Social Reporting (ISR). This accountability can make relationships between people better because it reflects caring. Implementing an attitude of caring and helping each other is by assisting such as zakat, infaq and alms, which are included in the ISR indicators. The Sharia Supervisory Board and Customer Pressure are some of the reasons for Islamic banks to express and carry out social responsibility. The research aims to identify how much influence the size of the Sharia Supervisory Board has on ISR and the influence of Customer Influence on ISR. The explanatory research method used in this research is a quantitative approach. The research data were analyzed using panel data regression analysis. The research sample was 27 Indonesian and Malaysian Sharia banks in 2019 and 2020. The research results showed that the size of the Sharia Supervisory Board had a positive effect on ISR, and Customer Influence had a positive effect on ISR.

**Keywords:** Islamic Social Reporting; Sharia Supervisory Board; Customer Influence

## 1. Introduction

Banks are institutions whose business activities serve the community by collecting savings and distributing funds to the community through credit and other forms. In general, we know two types of banks, namely conventional banks and sharia banks. Sharia banks carry out their business activities with Sharia principles, namely the principles of justice, benefit, universality, no usury, masyir, gharar, unjust and haram objects (UU RI, 2008). Islamic banking is the largest sector in the Islamic financial industry. Southeast Asia has gained significant momentum in Islamic finance growth over the past few years. This growth is primarily supported by the growing Muslim population in the region (Elgari et al., 2021). According to (Kristina, 2021), the country with the majority Muslim population in Southeast Asia is ranked number one in, Indonesia. The number of Muslim citizens in Indonesia in 2020 reached 87% of the total population, followed by Brunei Darussalam, 75% of the total population, and Malaysia, reaching 66%. The rapid development of sharia banking accompanies the growth of the Muslim population in Southeast Asia. The pioneer of Sharia banks in Indonesia, Bank Muamalat, was founded in 1992. In 1998, Sharia banks in Indonesia experienced relatively rapid development. Meanwhile, banking growth in Malaysia has been more present since 1983 with the Islamic Bank Act, IBA (Rofi'ah, 2017). This reasonably rapid development must be accompanied by good performance because the performance of Sharia banking is included in the achievements of its operational activities. (Utami et al., 2021). The development of Sharia banking must also be accompanied by accountability that is implemented

correctly, both accountability to fellow humans and accountability to Allah SWT. One form of accountability is social responsibility, or what can be called Islamic Social Reporting (ISR). This accountability can make relationships between people better because it reflects caring. One implementation of an attitude of caring and helping each other is by giving zakat, infaq and shodaqoh to those in need.

PSAK 101 regulates the Presentation of Financial Reports of Sharia Institutions; however, this rule only regulates financial presentation and does not regulate ISR, so there are differences in disclosure because there are no particular standards. ISR was first put forward by Ros Haniffa in 2002 and then perfected by Othman in Malaysia in 2009 (Murdiansyah, 2021). The existence of this disclosure concept is expected to create operational activities that are following sharia principles. Islamic Bank ISR research was carried out (Maesya'bani et al., 2019). There were 20 samples of Islamic banks in Southeast Asia, including banks from Indonesia and Malaysia, with research in 2015-2017, and the data found that in all the samples used, not a single Islamic bank carried out 100% disclosure of its corporate social responsibility.

According to (Dzulfaroh, 2021), COVID-19 was officially declared a pandemic, resulting in many companies going out of business and decreasing income, increasing unemployment and poverty (Utami et al., 2022). As Muslims, an attitude of caring and helping each other in this time of crisis is very much needed, considering that most people have lost their jobs, which means that a person's survival depends on other people providing assistance and donations. As was done in Indonesia by PT Bank Syariah Mandiri and its employees, they provided food assistance to communities affected by the COVID-19 pandemic. The Malaysian Government Institution also launched a program called Musa'adah Covid Fund to assist residents affected by the COVID-19 pandemic. Aid and donations are included in ISR disclosures. ISR disclosure is encouraged by several things, such as the Sharia supervisory board tasked with monitoring bank operational activities in compliance with Sharia principles and carrying out supervision when distributing zakat, infaq and shodaqoh funds included in the bank's social responsibilities (Milenia & Syafei, 2021). Therefore, the Sharia Supervisory Board can encourage a company to express and carry out social responsibility. Another factor is customers. The greater the company's dependence on customer savings to fund its capital projects, the greater the customer's expectations regarding the role of Islamic banks in carrying out social responsibility activities (Darus et al., 2015). Based on the background, the author wants to know whether the size of the Sharia supervisory board and customer influence influence the disclosure of Islamic Social Reporting (ISR) in Indonesian and Malaysian Sharia Banks.

### 1.1 Objectives

The research aimed to identify the size of the Sharia Supervisory Board and the influence of customers on Islamic Social Reporting (ISR) disclosures.

### 2. Literature Review

Shariah Enterprise Theory is a theoretical concept where Allah SWT is the primary source of trust, and the mandate from Allah SWT is given to stakeholders responsible for carrying out this mandate following the goals and methods that Allah SWT has determined. Companies can convey their mandate to stakeholders by making disclosures through ISR to prove that the company pays attention to the surrounding environment (Utami, 2022). The purpose of making disclosures is to show the activities car-

ried out by the company and show its positive impact on society (Meutia, 2010).

### 2.1 Size of the Sharia Supervisory Board

According to Islam, the Sharia Supervisory Board is an officer in every Sharia financial institution as a particular supervisor in financial transactions. The task of a Sharia Supervisory Board is to exercise control over the activities of Sharia Financial Institutions so that they comply with Sharia principles. The requirement to become a Sharia Supervisory Board member is someone who is an expert in trade procedures and laws according to Islamic Sharia. The minimum number of DPS members is three people (AAOIFI, 2010). The more Sharia supervisory boards in Sharia banks can increase their supervision of their governance. Research result (Milenia & Syafei, 2021) The size of the Sharia Supervisory Board has a positive effect on ISR; this is because the Sharia Supervisory Board monitors Sharia bank activities so that they operate following Sharia, which contains social responsibility so that the Sharia Supervisory Board can expand the disclosure of social responsibility.

### 2.2 Customer Influence

A customer is a consumer or can also be interpreted as a person or organization who benefits from products and services originating from a bank. Customers play a crucial role in the banking industry, including Sharia banks, because the funds customers save become part of the bank's capital to carry out its operational activities. The greater the sharia bank's dependence on funds obtained from customers, the greater the level of company management to respond to customer expectations. These expectations are pressure for management from external parties to be able to fulfil the desires expected by customers. These customer expectations will pressure management behaviour to discipline the market (Roberts, 1992). Research result (Darus et al., 2015), Customer Influence has a significant positive effect on ISR because the more the bank uses third-party funds compared to equity for its business activities, the greater the management's ability to respond to customer expectations regarding the bank's role in social responsibility.

### 2.3 Disclosure of Islamic Social Reporting (ISR)

ISR is a concept based on Islamic principles implemented in the form of responsibility. This form of responsibility is, firstly, being responsible to Allah SWT, secondly, being responsible to fellow humans, and thirdly, being responsible to the natural environment. ISR is an extension of Sharia-based social performance reporting standards, first coined Ros Haniffa in 2002 and refined by Othman et al in 2009. The ISR theme is structured based on ten ethical concepts in Islam, namely Tauhid, Halal Haram, Wajib, Ummah, Honesty, Adl, Khilafah, Mizan, Akhirah, and I'tidal use Israf. There are 6 ISR disclosure themes divided into 46 indicators (Othman et al., 2009).

## 3. Methods

The research method uses explanatory research, where this method is explanatory. This research approach is quantitative. Panel data regression is used in this research by selecting the Common Effect Model, Fixed Effect Model, and Random Effect Model by selecting model tests using the Chow Test, Hausman Test and Lagrange Multiplier Test methods. Furthermore, concluding using the t-test statistical test.

#### 4. Data Collection

Secondary data obtained from the 2019 and 2020 Sharia Bank Annual Reports were collected in this research. The sample used was 27 Sharia Banks consisting of the State Syariah Bank of Indonesia and the State Syariah Bank of Malaysia. The sample was determined using the purposive sampling method with the following criteria:

1. Indonesian and Malaysian Sharia Banks are included in the top 100 largest Sharia Banks according to The Asian Banker in 2020,
2. Sharia Banks issue Annual Reports in English or Indonesian,
3. Sharia Bank issued the 2019 and 2020 Annual Reports.

The measurement variables for this research are:

**Table 1. Variable Indicators**

Variable	Indicator
Size of the Sharia Supervisory Board (X <sub>1</sub> )	Total number of Sharia Supervisory Board (Herawati et al., 2019)
Customer Influence (X <sub>2</sub> )	Third-Party Funds / Total Equity (Darus et al., 2015)
Islamic Social Reporting (Y)	Disclosure is measured based on ISR items disclosed using a dummy variable: score 1 = disclosed; score 0 = not disclosed. Next, the number of disclosure items is divided by the total number of items (Cahya, 2017)

Source: data processed by the author (2023)

#### 5. Results and Discussion

##### 5.1 Descriptive Statistical Results

Descriptive statistics is a helpful tool for describing data in information that is easy to understand, thus providing an overview of the research. The results of descriptive analysis in this research are:

**Table 2. Descriptive Statistical Analysis**

	X1	X2	Y
Mean	3.57	6.40	0.50
Maximum	8.00	14.00	0.80
Minimum	2.00	0.00	0.30
Std. Deviation	1.79	3.42	0.12

Source: data processed by the author (2023)

Based on Table 2 above, variable According to AAOIFI in GSIFI No. 1, The minimum size of the Sharia Supervisory Board is three people (AAOIFI, 2010), so that the Sharia Bank in this study complies with AAOIFI regulations, the larger the size of the sharia supervisory board will cause the level of supervision of the bank to be higher. The maximum value for variable X<sub>1</sub> is 8, and the minimum is 2. The standard deviation value for variable X<sub>1</sub> is 1.79, with an average value of 3.57, meaning the data varies.

Based on Table 2 above, variable This figure is very high, but this is good because the bank has succeeded in attracting customers to save their funds at the bank. However, this also impacts Sharia

banks because customers have entrusted their savings to Sharia banks; of course, there must be reciprocity, one of which is carrying out social responsibility. The maximum value of  $X_1$  is 14, and the minimum is 0.00. The standard deviation value for variable  $X_1$  is 3.42, with an average value of 6.40, meaning the data varies.

Based on Table 2 above, variable Y, ISR, has an average value of 0.50, meaning that the Islamic banks used as a sample only reveal 50% of the 46 existing indicators. This is because of the 6 Islamic Social Reporting themes, 2 of which only a few Islamic banks have disclosed, such as the product and service and environmental themes. The maximum value of the Y variable is 0.80, and the minimum value is 0.30. The standard deviation value for variable Y is 0.12, with an average value of 0.50, meaning that the data varies.

## 5.2 Classical Assumption Test Results

### 1. Normality test

The test results obtained a probability value of 0.65, meaning the probability value is  $> 0.05$ , so the data is usually distributed.

### 2. Multicollinearity Test

The test results show that the correlation value  $X_1$  and  $X_2$  is -0.05, so there is no multicollinearity problem.

### 3. Heteroscedasticity Test

The test results obtained a value of Prob. Chi-Square (Obs\*R-square) is  $0.46 > 0.05$ , so there is no heteroscedasticity problem.

### 4. Autocorrelation Test

The test results obtained a value of Prob. Chi-Square (Obs\*R-square) is  $0.90 > 0.05$ , so there is no autocorrelation problem.

## 5.3 Statistical Results

This research analysis uses panel data regression so that the most accurate model selection among the three alternatives must be determined, namely:

### 1. Test Chow

The selection criteria for this Test is if the value of Prob.  $> 0.05$ , the Common Effect Model approach was chosen. If the value of Prob.  $< 0.05$ , the Fixed Effect Model approach was chosen.

### 2. Hausman test

The selection criteria for this Test is if the value of Prob.  $> 0.05$ , the Random Effect Model approach was chosen. If the value of Prob.  $< 0.05$ , the Fixed Effect Model approach was chosen.

### 3. Lagrange Multiplier Test

The selection criteria for this Test is if the value of Prob.  $> 0.05$ , the Common Effect Model approach was chosen. If the value of Prob.  $< 0.05$ , the Random Effect Model approach was chosen.

The results of the model selection test are:

**Table 3. Model Selection Test Results**

Model	Prob	Information	Conclusion
Chow Test	0.0000	$< 0.05$	The fixed Effect Model is ac-

			cepted
Hausman Test	0.0672	>0.05	The random Effect Model is accepted
Lagrange Multiplier Test	0,000	< 0.05	The random Effect Model is accepted

Source: data processed by the author (2023)

Based on Table 3 above, the Random Effect Model suits this research. The hypothesis is concluded in two stages: the partial Test or t-test and the coefficient of determination. Partial Test or t Test is carried out to determine whether there is a partial influence of each independent variable, namely the Size of the Sharia Supervisory Board (X1) and Customer Influence (X2) on the dependent variable, namely ISR (Y). The t-test compares the t-table values with t-statistics and probability values with the significance level. The following are partial test results:

**Table 4. Partial Test**

Variable	Coefficient	Prob.
X1	0.025628	0.0247
X2	0.003266	0.0237

Source: author's data (2023)

The partial test results show that X1 has a prob value. < 0.05 with a positive coefficient value of 0.025628 so that X1 positively affects Y. Variable X2 has a prob value. < 0.05 with a positive coefficient value of 0.003266, so X2 positively affects Y. The Coefficient of Determination Test determines the magnitude of the influence of the independent variable on the rise and fall of the value of the dependent variable.

**Table 5. Coefficient of Determination Test Results**

Adjusted R-Squared	0.156864
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Source: author's data (2023)

Based on Table 5, the coefficient of determination test results mean that only 15.6% of the variation in Y can be explained by variables X1 and X2, while other variables explain the remaining 84.4%.

### 5.4 Discussion

Based on Table 4, partial test results show that variable X1 positively affects variable Y. The Sharia Supervisory Board has the duty and authority to control banking business activities so that they comply with applicable Sharia regulations and principles. The size of the Sharia Supervisory Board is based on Bank Indonesia regulation no. 6/24/PBI/2004, namely a minimum of two people and a maximum of five people (Bank Indonesia, 2004). According to AAOIFI in GSIFI No. 1 The minimum size of the Sharia Supervisory Board is three people (AAOIFI, 2010). The Sharia Supervisory Board has an average score of 3.57, meaning it has met the standards of a Sharia Bank. The larger the Sharia Supervisory Board size will increase Sharia banks supervision, the higher the ability to review all transactions to ensure Sharia Bank operational activities are more controlled (Hussainey, 2016). An adequate number of Sharia



Supervisory Boards helps Sharia banks increase Sharia compliance in social responsibility disclosures. Disclosure of ISR is the aim of Sharia compliance because ISR is part of Islamic law following maqashid Sharia. The more Sharia Supervisory Boards there will be, the greater the number of disclosures of ISR as a social activity because the Sharia Supervisory Board considers ISR part of Islamic law. This is in line with what was stated (Milenia & Syafei, 2021) that the primary function of the Sharia Supervisory Board regarding Sharia compliance is to supervise company activities in the distribution of zakat, infaq and shodaqoh funds, which are included in the company's ISR items so that the size of the Sharia Supervisory Board is following applicable regulations with a variety of perspectives, experiences and Competency expertise in Islamic business will expand social responsibility through ISR.

Based on Table 4, the partial test results show that variable  $X_2$  positively affects variable Y. Customer Influence is external pressure on the company that can influence the company's operational activities. The company's survival depends on the capital owned by the company, including Sharia banks. Customer Influence is measured by the ratio of Third Party Funds divided by Total Equity. Based on the research results, the average ratio of customer influence reached 6.40 or 640%, with a maximum value reaching 14.00 or 1,400%. This is good because the bank succeeded in attracting attention and retaining customers to save their funds in the Sharia banks used as samples. However, this also impacts Sharia banks because customers have entrusted their savings to Sharia banks; of course, there must be reciprocity. In line with the theory (Darus et al., 2015) that customers have the right to keep their money, banks must attract and retain customers. So, the more capital used by Sharia banks that is obtained from customers, the more Sharia banks are required to make efforts so that customers continue to entrust their funds to be saved using transparency (Roberts, 1992) states that the greater the company's dependence on customer deposits as capital, the greater the level of company management to respond to customer expectations. These customer expectations are pressure for management from external parties to be able to fulfil the desires expected by customers. According to (Darus et al., 2015), these expectations are customer expectations regarding the bank's role in social responsibility or ISR. The aim of ISR is a form of transparency towards society. Transparency is hoped to increase the trust of the public/customers and investors because Islamic banks have carried out their business activities following Islamic law as stated through ISR disclosures. So, the higher the customer influence on a Sharia bank, the greater the customer's expectations regarding the company's role in social activities through ISR.

## 6. Conclusion

Research finds that the size of the Sharia Supervisory Board positively affects ISR. The adequate size of the Sharia Supervisory Board helps Sharia banks increase Sharia compliance in disclosing social responsibility with ISR as the goal of Sharia compliance because ISR is part of Islamic law following maqashid Sharia. The more Sharia Supervisory Boards in a Sharia bank, the more adequate the number for disclosure as social activity will be higher because the Sharia Supervisory Board assesses items as part of Islamic law. Customers are significant for banking because customers are capital for banks from third-party funds. The greater the company's dependence on customer savings as capital, the greater the level of company management to respond to customer expectations regarding the bank's role in social responsibility with ISR. One of the goals of ISR is transparency towards society. The higher the customer influence on a Sharia bank, the greater the customer's expectations regarding the company's role in social activities through ISR.

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