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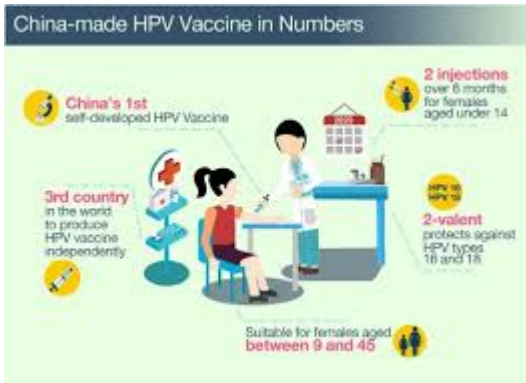
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EFFECTS OF IMPLEMENTATION OF COSO-ERM WITH KHALIFATULLAH FIIL ARD PHILOSOPHY MODERATION ON UNIVERSITY FINANCIAL PERFORMANCE

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Abstract

This research explains empirically the effect of implementation of COSO Enterprise Risk Management (ERM) Framework with Philosophy of Khalifatullah Fiil Ard moderation and roles of governance element on university financial performance in East Java. The underlying background of this research is the inconsistent results of previous research and the phenomenon of low accountability at universities and the low function of internal control based on the final report of Supervision, Control and Development for the period of 2016. The data collection technique was survey and the data analysis used Structural Equation Modeling (SEM) PLS. The results of the research show that ERM significantly affects the financial performance and moderation variables cannot strengthen ERM relationship with financial performance. The implications of future research are to expand the object of research by differentiating Islamic and non-Islamic universities, adding the dependent variable of non-financial performance as well as the use of experimental research methods.

Keywords: COSO-ERM Framework, Khalifatullah Fiil Ard (Islamic Leadership) Philosophy, Roles of Element of Higher Education Governance and Financial Performance

INTRODUCTION

This research explains empirically the effect of implementation of COSO Enterprise Risk Management (ERM) Framework 2004 with Philosophy of *Khalifatullah Fiil Ard* (Islamic Leadership) moderation and roles of governance element on university financial performance in East Java. The backgrounds of this study are; First, the inconsistent results of research related to the COSO 1992 framework compared to COSO 2004 framework. Second, there are only a few studies discussed the effects of COSO framework on performance with inconsistent results, while based on one of missions of COSO establishment adopted by one of the council members in 2008 was to improve organizational and governmental performance (Landsittel & Rittenberg, 2010). Third, during a long period from 1985 to the 2000s, the developing empirical

research only leads to private sector organizations with a research theme related to how to minimize fraudulent financial statements. In fact, based on the mission and goals of the establishment of COSO, it is not only for private sector organizations but also educational institutions. Fourth, there is no research related to ERM implementation which providing sharia perspective by using *khalifatullah fiil ard* (Islamic Leadership) philosophy which should be embedded in the soul of a leader in carrying out his duties and functions especially in Universities. There are many universities that do not have accreditation status according to the accreditation report in 2016 that 59% universities consisting of 190 private universities in East Java having accredited from total 322 private universities (Jawa Pos, January 2017). The final report of Supervision, Control and Development (WASDALBIN) for the period of 2016 shows that private universities whose institutions have not been accredited are 52%. This phenomenon indicates the low accountability of universities both in terms of financial and non-financial aspect, as well as the low function of internal control functions that exists (Nurhayati, 2016). The results of the findings of Wasdalbin Coordination of Private Higher Education Region VII (Kopertis Wilayah VII) in 2016 also concluded that 289 universities have established the SPMI Team (91%), yet the establishment of SPMI Team or the Internal Quality Assurance System does not counterbalance with the quality of higher completely. It is proven that as many as 161 private universities (50.15%) established SPMI Team as a formality, in the sense that not it has not applied the cycle in the form of determination, implementation, evaluation, control and continuous improvement of Standard yet. Internal Quality Assurance System is a crucial element that can guarantee the quality of an institution and it should be balanced with the cycle of all round quality assurance of higher education.

Based on the research gap and supported by the phenomenon of declining performance of universities and supported by the findings of Wasdalbin, then the researcher is motivated to conduct a research to explain the effect of implementation of COSO-ERM framework on the performance of universities in East Java. Nurhayati (2016) in a study using a qualitative research paradigm states that the implementation of the COSO concept and *Khalifatullah Fiil Ard* (Islamic Leadership) Philosophy through sharia forensic accounting can prevent and detect the fraud at universities. Ahmadova (2016) suggests that Islamic internal control in non-Islamic environment is also required and used as a tool to manage risk in companies in Japan. The philosophy of *khalifatullah fiil ard* (leadership of Islam) and the involvement and leadership roles in this study are the variables that are assumed strengthening the COSO-ERM relationship with the performance as stated by Ballantyne (2013) that ERM adoption will give implications for performance when executive leadership and integration of organizational culture are involved. These results provide insight to risk-based internal control for organizations and leaders as they determine the most effective ways to manage future risks. Fan (2014) states that the effect of the diversity or demography of

the board member will be positively correlated with the performance especially for the board of directors with financial expertise to moderate the implementation of ERM relationship and the value/performance of the company. It is also supported by Mensah (2015) that the relationship of ERM with performance will be positively correlated if the roles and presence of CRO (Chief Risk Officer), AC (Audit Committee) and TM (Top Manager) within a company exist.

Previous studies have shown that the COSO-ERM framework influences performance [Gordon et al. (2009); Christ et al. (2012); Salehi et al. (2013); Ballantyne (2013); Brown et al. (2014); Fan (2014); Ahmed and Manab (2016)]. Although there are some researchers who state that the implementation of COSO ERM does not directly mention the effect on performance but it does affect the quality of earnings according to Brown et al. (2014), influences company operations according to Mei and Sarah (2015) and is also an internal control tool as a preventive and detective financial statement (Chen, Shaio Yan et al. (2007); Altamuro (2010); Baxter (2013); Abiola and Oyewole (2013); Kulikova and Kazan (2016); Dut (2016)). This shows that COSO ERM has been empirically stated to have an effect on organizational performance from a different perspective. But according to Christopher and Sharen (2015) states that ERM is not congruent with culture in Australia so that it has a different impact on the outcome produced. Based on this description, the research hypothesis is:

H1 = Framework Enterprise Risk Management affects the Financial Performance of Higher Education.

Christopher and Sharen (2015) in empirical research conducted stated that the adoption of ERM is not congruent with environmental culture in Australia but still influences performance on condition that there must be a more comprehensive leadership role in each function. Nurhayati (2016) states that building the philosophy of Khalifatullah Fiiil Ard in an organization will strengthen one's self control in carrying out their duties and functions and also strengthen the organization's internal control by implementing the COSO framework and can prevent and combat fraud behavior. Wandaud et al. (2014) also states that by stimulating the quality of Islamic Leadership can improve organizational performance. This is based on Islamic Leadership Theory which contributes to the success of organizational performance which will positively influence economic growth and increase employee motivation to be better in the long run.

Aabed (2006) stated in his dissertation that the theory and practice of Islamic leadership in 12 (twelve) Michigan Islamic Schools was effectively implemented into leadership practices and behaviors in accordance with the values and principles of the Qur'anic-based Islamic Leadership exemplified by the Qur'an Prophet Muhammad SAW. As also stated by Mohsen (2007), that the spirituality and responsibility of leaders significantly

influence the relationship of trust with the effectiveness of leadership in the business world in 206 sample companies in Malaysia. Ahmadova (2016) also stated in her research that Islamic internal control in a Non-Islamic environment is needed and used as a tool to manage corporate risk caused by the behavior of the Board that manages subsidiaries in Japan in Islamic finance. From this description, the research hypothesis is:

H2 = Philosophy Khalifatullah Fiil Ard strengthens the relationship between Enterprise Risk Management and the financial performance of Higher Education.

Empirical research stating that the roles, abilities and structure of the Audit Committee influence organizational and company performance (Loana and Mariana (2004); Drymiotis (2008); Alabede and Tony (2015); Mensah (2015)) and BOD diversity have a positive correlation with performance company (Farag and Mallin, 2016). However, Collum (2014) states that in the United States Medical Cost Reports Hospital, the structure of the BOD will affect performance if there is compensation for the existing BOD. In other words, the payment or compensation given to the BOD significantly moderates the relationship of the BOD structure to the financial performance of the Hospital. the minister and PTS are responsible for the Organizing Body.

Beasley et al. (2005) states that the factors associated with ERM are the presence or role of BOD. So that the BOD communication process and the internal Auditor will affect the quality of the Financial Statements of Cohen et al. (2007). Nevertheless, Yatim (2009) states that in addition to a strong BOD structure too; company size, complexity of company operations and use of the Big Four Public Accountant Firms that affect the relationship between risk management and the BOD structure of companies registered in Malaysia.

Similar research results were carried out by Fan (2014) that the BOD leadership factor positively moderated the relationship of ERM with organizational culture to stakeholder values. Likewise Muller and Hilb (2016) stated that the role of BOD greatly influences risk that is not controlled. Based on the description, the research hypothesis is:

H3 = The Role of Higher Education Governance Elements strengthens the relationship between Enterprise Risk Management and the Financial Performance of Higher Education Universities.

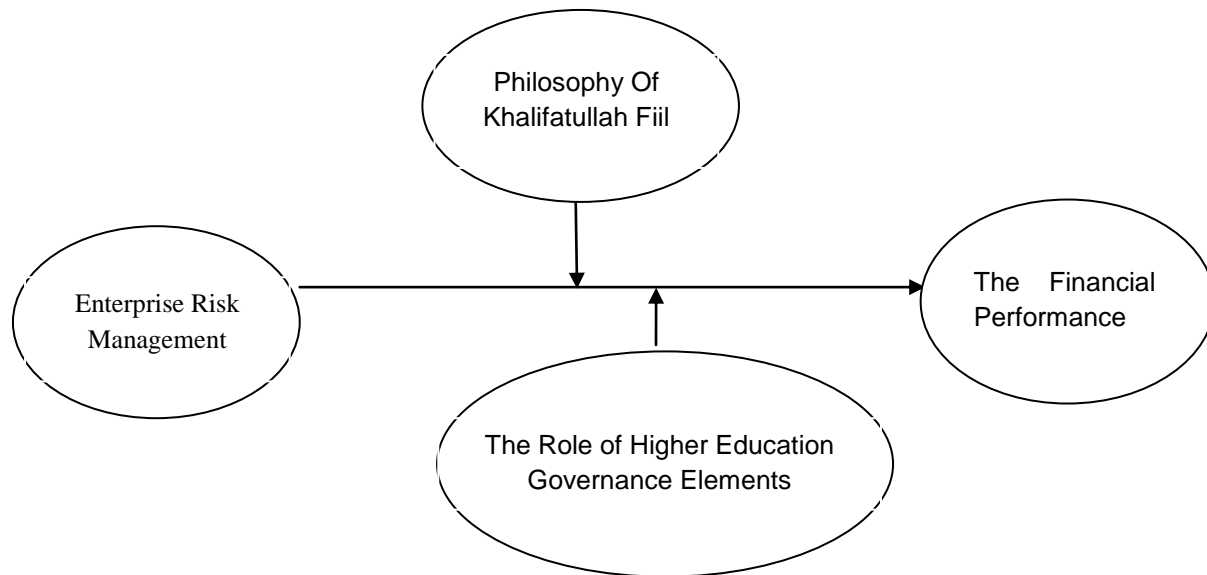


Figure 1. Conceptual Framework

RESEARCH METHOD

The type of this research from its objectives is explanatory since the main purpose of this study is to explain why an event occurs then build, elaborate and add some explanation based on the theory (Nueman, 2011, p. 40). The data collection techniques used in this research is secondary data documentation and survey using questionnaires. Secondary data sources include institutional accreditation forms and institutional financial statements. Survey is a method of collecting the primary data obtained directly from the source, Indriantoro and Supomo (2016). Data analysis technique in this study used Structural Equation Modeling (SEM) and the data was processed using Smart PLS 3.0 software applications. SEM is one type of multivariate analyses in social science which is the application of statistical methods to analyze several research variables simultaneously (Sholihin and Ratmono, 2013: 4).

RESULTS AND DISCUSSION

Result

The results show that implementation of Enterprise Risk Management can affect financial performance. Enterprise Risk Management is an integrated risk-based internal control framework that gives a positive impact on the financial performance of universities. The research also provides empirical evidence that the aspect of Islamic values of a leader which is *khalifatullah fiil ard* (Islamic leadership), cannot strengthen

the relationship of ERM and financial performance. It is because the research sample used by the universities comes from diverse across religions, so it provides different perceptions between the sample of answers from Islamic Universities and Non-Islamic Universities. The number of selected samples of Islamic Universities is only 12 or (12%) out of 104 Universities in total.

Similarly, the effects of moderation of roles of university governance element cannot strengthen the relationship of ERM and financial performance. It is due to several things, that is; the majority of data distribution of Higher Education is the Private University Accredited C as many as 61 or 60% of the selected research object of 104. The results of analysis of WASDALBIN KOPERTIS Region VII of EAST JAVA states that 91% of private universities have established SPMI for formality intention only and it is not accompanied by the cycle of management, control and quality assurance of higher education as a whole.

Discussion

The findings of this study imply that an effective internal control tool positively affects the financial performance of universities in East Java, that is the COSO ERM 2004 risk-based internal control framework using the relatively new research instrument, COSO 2013, that has not been implemented on all internal control components thoroughly by previous research. The practical implications of the research are able to provide input for the management of Universities in East Java, especially the Chief/Head/Director of Internal Control Unitor Quality Assurance Agency to adopt the ERM Framework to the Institute as a risk-based internal control tool that gives a positive effect on financial performance.

The theoretical implications of the research are stewardship theory as the main foundation to describe the management ability and quality of internal control of organization (Higher Education) giving influences to the achievement of goal through financial performance. Donaldson and Davis (1991) argue that the Stewardship theory which is part of agency theory illustrates a situation where the management is not motivated by individual goals but rather, the main outcome for the sake of the institution. It means that the *Achievement* of the concept assuming that the interests of management and *principal* are convergence, meaning both aspect have the same goal. Madison (2014) stated that the integration of agency theory and Stewardship theory is empirically proven to influence organizational performance.

CONCLUSION AND FUTURE RESEARCH

Implementation of the ERM framework provides a positive response to the improvement of the financial performance of Universities. It means, risk-based internal control (ERM) is an internal control tool that is needed by the University to overcome or address the phenomenon that the Internal Quality Assurance System of Higher Education in East Java is not accompanied by the cycle of quality assurance of higher education as a whole. This research model extends the previous research model in testing the effect of implementation of ERM on Financial Performance by involving the variable of *khalifatullah fiil ard* philosophy moderation and the Roles of Higher Education Governance Elements. The results also show that moderation of KFA and PUTKPT variables has no significant effect. KFA variable fails to moderate since the research samples used by Universities comes from diverse religions, giving different perceptions between the sample of answers coming from Islamic universities and non-Islamic universities. Similarly, the effects of moderation of roles of university governance element cannot strengthen the relationship of ERM and financial performance. It is due to several things, that is; the majority of data distribution of Higher Education is the Private University Accredited C as many as 61 or 60% of the selected research object of 104. It is also supported by the results of analysis of WASDALBIN KOPERTIS Region VII of EAST JAVA that 91% of private universities have established SPMI for formality intention only and it is not accompanied by the cycle of management, control and quality assurance of higher education as a whole.

In order to improve the results of the research in a more complex manner, it is suggested for the future research to use mixed method approach to explore deeper by applying quantitative approach and qualitative approach. So that the measurement scale which is based on perception can be improved by adjusting qualitative measurement data of all variables. It is also to differentiate the research object of Islamic University and Non-Islamic University. So, it can distinguish the results of research from the two different research objects. In order to provide a broader scope of research, it is suggested that the future research will add some factors of non-financial performance as well as other factors on to the Variables Moderation PUTKPT. Hence, it is not only assessed to the extent of the roles and involvement of Governance Elements in the Higher Education governance, but also the factors of ability and structure, Diversity, and compensation that influence the financial performance.

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