The Potential Adoption of Islamic Accounting Standards Developed by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) by Islamic Banks in the United Arab Emirates

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A thesis submitted in fulfilment of the requirements for the degree of Doctor of Business Administration of the University of Canberra

July 2016
Abstract

This study investigated the potential impact of applying the accounting standards of the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) in Islamic banks in the United Arab Emirates (UAE). This study aimed to examine the International Financial Reporting Standards (IFRS) currently in use by Islamic banks in the UAE, as compared to the AAOIFI accounting standards, in order to identify the differences and determine which system may better satisfy user needs in the UAE, as judged from the perspective of respondents to a research survey. This study also provided an understanding of the roles of key personnel in developing the AAOIFI’s standards in the UAE and the factors leading to the development of these standards were explored.

Data was collected for this purpose through examination of documents, conducting a questionnaire survey with professionals and managers of Islamic banks in the UAE and conducting interviews with key personnel involved in the development of the Islamic Accounting Standards. It was found that the main participant in developing the Islamic Accounting Standards in the UAE is the Dubai International Finance Centre (DIFC).

This study found that there is a serious concern, particularly in the Islamic countries, with regard to the IFRS dealing with transactions involving interest (Riba). One implication of this study was that in the era of globalization, accounting standard setters who came from different ideological and religious backgrounds should communicate with each other because their reporting standards and their different backgrounds can have global implications beyond their jurisdictions. The study also revealed that factors such as religion, culture and local investors, may have limited influence on the current adoption of accounting standards in the Islamic banks. This contrasts with economic and political factors such as domestic regulators, foreign investment, and global financial institutions which are major influences on the Islamic banks with regard to the adoption of IFRS.

Furthermore, the study uncovered a concern among respondents of issues that may develop when Islamic banks commence the transition to AAOIFI standards. These issues include the prevention of attracting foreign direct investments, affecting the relationship with the big four accounting firms, giving rise to certain costs of time and sources and limiting the comparability with financial statements of other financial institutions. The study also indicated that there was a high level of support (61.5%) amongst respondents for the adoption of IFRS; however, the respondents’ opinion does not also reflect a perception that all IFRS
are suitable for application of *Shariah* transactions. Therefore, the findings suggest support for not replacing IFRS, but to find a way to comply with AAOIFI standards as well as to continue using IFRS by Islamic banks in the UAE.
Acknowledgments

In the name of GOD, the merciful, the beneficent

Thanks for God “Allah” for giving me patience and strength during my studies, the ability to finish this thesis and granting me success in this long-term endeavour.

I would like to express the most sincere gratitude to my chair advisor, Dr. Jesmin Islam, who provided me with friendly and efficient supervision and advice during my studies, and provided guidance throughout this endeavour. I would like also to extend my thanks to my distinguished supervisory panel members, Professor Monir Mir and Dr Mohobbot Ali who provided assistance and advice during my studies. My special thanks also to those people who assisted me during the data collection period.

Finally, I am deeply grateful to my Mum & Dad, who are an example of the great parents of this life, for their support and encouragement. My warm love and thanks go to my wonderful wife Rasha for her support, encouragement and sacrifice while I completed my DBA.
## Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>AAIOFI</td>
<td>Accounting and Auditing Organization for Islamic Financial Institutions</td>
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<tr>
<td>AICPA</td>
<td>Institute of Certified Public Accountants</td>
</tr>
<tr>
<td>CFA</td>
<td>Confirmatory Factor Analysis</td>
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<tr>
<td>CIPA</td>
<td>Certified Islamic Professional Accountants</td>
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<tr>
<td>CSAA</td>
<td>Certified <em>Shariah</em> Advisors and Auditors</td>
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<tr>
<td>DFSA</td>
<td>Dubai Financial Service Authority</td>
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<tr>
<td>DIFC</td>
<td>Dubai International Financial Centre</td>
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<tr>
<td>EFA</td>
<td>Exploratory Factor Analysis</td>
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<tr>
<td>ERM</td>
<td>Enterprise Risk Management</td>
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<tr>
<td>FASB</td>
<td>Financial Accounting Standards Board</td>
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<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
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<tr>
<td>GAAP</td>
<td>Generally Accepted Accounting Principles</td>
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<td>GCC</td>
<td>Gulf Cooperation Council</td>
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<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
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<tr>
<td>IAH</td>
<td>Investment Account Holders</td>
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<tr>
<td>IAS</td>
<td>International Accounting Standards</td>
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<tr>
<td>IASB</td>
<td>International Accounting Standards Board</td>
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<tr>
<td>IASC</td>
<td>International Accounting Standards Committee</td>
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<tr>
<td>IFIs</td>
<td>Islamic financial institutions</td>
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<td>IFRS</td>
<td>International Financial Reporting Standards</td>
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<td>IFSB</td>
<td>Islamic Financial Services Board</td>
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<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
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<tr>
<td>MEC</td>
<td>Middle Eastern Countries</td>
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<tr>
<td>MENA</td>
<td>Middle East North Africa</td>
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<tr>
<td>MoU</td>
<td>Memorandum of Understanding</td>
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<tr>
<td>PLS</td>
<td>Profit &amp; Loss Sharing</td>
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<tr>
<td>SAC</td>
<td>Standard Advisory Council</td>
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<tr>
<td>SCF</td>
<td><em>Shariah</em> Compliant Financing</td>
</tr>
<tr>
<td>SEC</td>
<td>Securities and Exchange Commission</td>
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<td>UAE</td>
<td>United Arab Emirates</td>
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Glossary

Fatwa: Islamic religious rules. Religious decree or a legal ruling made according to Shariah.

Fiqh: Islamic jurisprudence. The science of the Shariah. An important source of Islamic economics.

Gharar: Speculation. An exchange transaction in which one or both parties remain ignorant of an essential element of the transaction.

Haram: An act or product which is unlawful or prohibited in Islam.

Ijara: Lease financing or Islamic mortgage. The purchase of the leased asset at the end of the rental period is optional.

Istisnah: Advance purchase of goods or buildings. Contract of sale of goods to be manufactured or constructed in a fixed time for an agreed price.

Mudharaba: Profit sharing. An investment on your behalf by a more skilled person. It takes the form of a contract between two parties – one who provides the funds and the other who provides the expertise. The division of any profit is agreed in advance.

Mudarib: Entrepreneur in a Mudharaba contract. The entrepreneur or investment manager in a Mudharaba who puts the investor’s funds in a project or portfolio in exchange for a share of the profits.

Murabaha: Cost-plus financing. A contract for purchase and re-sale for cost plus profit, which allows the customer to make purchases without having to take out a loan and pay interest.

Musharaka: Partnership. A contract involves a person placing their capital with another person's capital and them both sharing the risk and reward.

Qard Hasan: Benevolent loan. Non-interest bearing loan or benevolent loan which refers to a loan given by a person (lender) to the borrower without any expectation of extra returns.

Riba: Interest or usury. An increase, addition, unjust return, or advantage obtained by the lender as a condition of a loan. Prohibited in Islamic law.

Shariah: Islamic law. Islamic law derived from three sources: the Quran, the Hadith and the Sunnah.

Sukuk: Islamic bond. Shariah-compliant financial certificates similar to bonds.

Sunnah: Practice and traditions of the Prophet Muhammad (peace be upon him).
<table>
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<tr>
<td>Takaful</td>
<td>A form of Islamic mutual insurance based on the principle of mutual assistance. Known as ‘Islamic insurance’.</td>
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<tr>
<td>Zakat</td>
<td>A religious levy as a fundamental duty. An obligatory contribution where every wealthy Muslim is required to pay a proportion of his/her wealth every year.</td>
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<td>Hawala</td>
<td>Remittance or bill of exchange. A contract which allows a debtor to transfer his debt obligation to a third party who owes the former a debt. The mechanism of <em>Hawala</em> is used for settling international accounts by book transfers, thus obviating the need for a physical transfer of cash.</td>
</tr>
<tr>
<td>Kafalah</td>
<td>Guarantee. <em>Shariah</em> principle governing guarantees. It applies to a debt transaction in the event of a debtor failing to pay.</td>
</tr>
<tr>
<td>Hesab</td>
<td>Account.</td>
</tr>
<tr>
<td>Shirkah</td>
<td>Partnership. A contract between two or more persons who launch a business or financial enterprise to make a profit.</td>
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Chapter 1 – Introduction

1.1 Introduction and motivations for this study

Islamic finance is one of the fastest growing branches of the global financial services industry. In the year 1993 it was estimated that the global total assets under the control of Islamic banks was around US$60 billion and this figure increased to US$100 billion in 1997 with an estimated growth rate of 15% per annum (Iqbal, Ausaf & Tariqullah 1998). Islamic finance has grown at over 10% per annum in the decade 2000–2010 (Austrade 2010). Recently, Islamic banking assets have grown at an average 19% per annum over 2009–2012, which was 50% faster than the overall banking sector (Ernst & Young 2012). This growth is being driven by four primary factors; petrodollar liquidity, Muslim population growth, ethical character and financial stability of Islamic financial products and the low penetration levels of depth across asset classes and products signifying untapped potential. It is generally accepted that the main reason for the growth in recent years is the high price of oil, leading to increased wealth in the Gulf Cooperation States (Austrade 2010).

Shariah-compliant finance, also known as Islamic Banking and Islamic Finance allows Muslim consumers to participate in financial transactions in a manner that is in accordance with their belief systems (KPMG International 2006). Shariah (Islamic law) refers to a body of law which applies to all aspects of a Muslim’s life, including economics and business life. The Islamic banks’ practices are based on the same principles which are used in Islamic teachings and Islamic business principles which are enshrined in Shariah laws (Van de Ven & Ferry 1980). The main reason for adopting Islamic accounting standards for Islamic banks is the principle that the Islamic banking system has to follow strict Islamic Shariah rules (Van de Ven & Ferry 1980). Islamic banks’ clientele are not confined to citizens of Muslim countries, but are spread over Europe, the United States of America and the Far East (KPMG International 2006).

The Islamic banks are now wide-spread over the world and these Islamic banking institutions are not limited to the Muslim countries. More than 600 Islamic financial institutions are operating worldwide (Yaacob & Donglah 2012). Measured by Shariah-compliant assets of financial institutions, the global Islamic finance assets were estimated at US$1.9 trillion in 2014 with an estimated growth rate of 20% per annum in the recent years, with around 75% of the industry located in the Middle East North Africa (MENA) region where the Gulf Cooperation Council (GCC) countries accounted for 96% of it (Hussain, Shahmoradi & Turk
Shariah Compliant Financing (SCF) constitutes financial practices that conform to Islamic laws. SCF institutions are similar to conventional financial intermediaries in that they are profit-maximizing institutions and offer traditional banking services, but differ in respect of some of the principles under which they operate (Imam & Kpodar 2010).

Currently, the United Arab Emirates (UAE), Bahrain and Malaysia are the leading Islamic finance centres (Savona & Mofakhami 2009). Islamic finance has considerable potential to become an important element in the UAE’s aspirations to be a global financial service centre in the region. It has the potential to facilitate further innovation and competition in the wholesale and retail banking sectors and to support the UAE government’s commitment towards credit market diversification.

The research underpinning this thesis is primarily concerned with the adoption of accounting standards by the Islamic banks in the UAE. The researcher’s conversations with customers of Islamic banks in the UAE, before this research study began, revealed that the majority believed that Islamic banks should adopt Islamic accounting standards to be considered as Islamic institutions that correctly complied with Shariah. They agreed that the only reason which leads them to invest in the Islamic banks is that there are no alternative Islamic financial institutions.

It is generally accepted that Islamic accounting standards have been developed because in some cases, Islamic financial institutions encountered accounting problems due to International Financial Reporting Standards (IFRS), or practices being perceived as inadequate to account for and report Islamic financial transactions. The Islamic finance industry in the UAE is under significant pressure to protect investors, enhance practices and improve risk management systems (Deloitte & Touche (M.E.) 2012). This study will focus on UAE Islamic banks and the potential impact of implementation of Islamic accounting standards developed by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).

Various issues will be discussed in this chapter including the research questions, research method, analysis of data, and expected findings. This chapter is organized as follows. Section 1 includes the introduction and section 2 explains the objectives of this research. The significance of this study is provided in section 3. The review of the relevant literature is discussed in section 4, and the research questions are developed in section 5. In section 6, the
data collection and research methodology are explained. Finally, section 7 discusses a summary of the findings, implications and conclusions.

1.2 Objectives of the research

The overall aim of this study was to investigate the feasibility of the adoption of Islamic accounting standards developed by the AAOIFI in the UAE and to explore the suitability of this potential adoption. This study aimed to examine the currently adopted IFRS as compared to AAOIFI accounting standards in order to identify the differences and determine which system could better satisfy user needs from the perspective of respondents. This study compared the specific accounting standards which have been developed by the AAOIFI and the applied IFRS in the UAE Islamic banks, to ascertain whether Islamic banks in the UAE should continue to follow the IFRS issued by the International Accounting Standards Board (IASB), or adopt the Islamic accounting standards issued by the AAOIFI.

Overall the objectives of this study were as follows:

- To examine the difficulties and problems occurring during the application of IFRS in the UAE Islamic banks.
- To provide an understanding of the factors or reasons that might lead the UAE Islamic banks to adopt AAOIFI accounting standards and the expected benefits that may flow from this adoption.
- To provide an understanding of the factors and issues that Influenced the Adoption of IFRS
- To examine the difficulties and problems during the possible transition to AAOIFI accounting standards.
- To identify and understand the role of the key players and their important roles in developing the AAOIFI’s standards in the UAE and explore the factors leading to the development of these standards adoption.

1.3 Significance and contributions of this study

This study is intended to investigate the feasibility of adoption of the AAOIFI accounting standards in the UAE Islamic banks and to identify the potential impact of the adoption of the AAOIFI accounting standards on the presentation and disclosure of financial statements of Islamic Banks. This research will lead to a better understanding of the above issues as well as
a better understanding of the similarities and differences in the application of IFRS and AAOIFI accounting standards to the UAE Islamic banks.

According to the director of technical development at AAOIFI:

…it is clear that gaps and differences exist and will continue to exist between the two set of standards. These gaps and differences are a natural result of the differing structural objectives of the IASB and AAOIFI. AAOIFI’s mandate is to develop standards where IFRS do not cater for the specificities of Islamic Banking or leads to Shariah compliance issues. As long as there are economic, legal and social differences between Islamic and conventional banking and finance practices, there will also be differences in the standards issued. (Ibrahim & Hameed 2010, p. 8)

AAOIFI have issued 26 standards on accounting, five standards on auditing and seven standards on governance, in addition to two codes of ethics and 40 Shariah standards (outlined in Appendix 1). The focus will be on the following accounting standards: Disclosure on Transfer of Assets, Deferred Payment Sale, Foreign Currency Transactions and Foreign Operation, Provisions and Reserves, Murabaha (cost-plus financing), Mudharaba (profit sharing) and Zakat (a religious levy as a fundamental duty). The potential shift from IFRS to AAOIFI accounting standards for UAE Islamic banks is expected to present significant challenges for the UAE Islamic banks’ financial report preparers, users, and auditors. This study will contribute to existing knowledge of the topic in many ways. As can be noted from the literature, there have been several calls for a separate examination for AAOIFI accounting standards. Therefore, this study attempted to fill the general gap in the literature on the relevance of AAOIFI accounting standards to Islamic banks, and a more specific gap, by studying the adoption of AAOIFI accounting standards in the Islamic banks in the UAE. As mentioned previously, the UAE has many unique features which are not found in other Islamic countries.

The UAE is a member of the GCC. Islamic banks in the GCC countries such as Bahrain and Qatar have begun adopting AAOIFI Standards. In addition, the Dubai International Financial Centre in the UAE has decided to use these standards as well. This study explored the impact of AAOIFI accounting standards on the UAE Islamic banks reporting after the assumed adoption, and contributes to an understanding of expected difficulties associated with such adoption. This study provides a clearer understanding of the factors which may also influence the adoption of AAOIFI accounting standards in Islamic banks in general, using the UAE as a case study. In this context, the study determined whether these factors may also be barriers to the adoption of AAOIFI accounting standards in the UAE. The study offered insights into the
AAOIFI organization when examining the suitability of its accounting standards to the UAE Islamic banks, and contributed to an understanding of the Islamic accountability framework with regards to accounting practice in the UAE.

Although the UAE may differ from some Islamic countries, this study may be useful for other Islamic countries in gaining a clearer picture of the differences between Islamic countries by comparing the findings of this study with other studies, and applying the results to their countries. This research contributed to existing knowledge and practices not only in Islamic countries but also in western countries in terms of a deeper understanding of the Islamic accounting standards and how the adoption of AAOIFI accounting standards could influence the Islamic banking process, activities and financial reporting.

In addition, Islamic bank managers and shareholders will gain an insight into the factors which led to the development of the AAOIFI accounting standards and how these factors could influence the Islamic institutions’ processes, activities and financial reports. Moreover, this study may provide useful material for researchers and academics with an interest in Islamic accounting research in general, and also in the UAE, as there is a dearth of studies and research regarding accounting standards and AAOIFI standards in particular. Other interested parties, such as local and foreign investors and universities in the UAE, may find this study useful if expanding their courses in Islamic accounting.

This study is unique as no study has yet explored the potential influences of the AAOIFI accounting standards on Islamic banks in the UAE. No study has yet focused on the roles of key players involved in the development of the Islamic accounting standards issued by AAOIFI.

1.4 Review of the relevant research

This section provides a structure that the researcher will be following in Chapter 2 for a literature review of the relevant studies in the area of Islamic Accounting and banking in the UAE. The review focuses on the most relevant published studies.

The literature review will be outlined in the following manner:

- studies focused on accounting standards followed in the UAE;
- studies that have evaluated Islamic banking and Islamic accounting standards and the need for accounting standards for Islamic financial institutions;
• studies focused on the objectives, characteristics, ethics and social responsibility of Islamic accounting;
• studies comparing Islamic banking and conventional banking;
• studies comparing AAOIFI accounting standards with International Financial Reporting Standards (IFRS);
• studies focused on compliance with AAOIFI accounting standards by Islamic banks and Fatwa and Shariah Supervisory Board; and
• studies critical of Islamic banking and the AAOIFI.

1.5 Research questions

The overall aim of this study is to explore the suitability of AAOIFI standards for the Islamic banks in the UAE. In order to achieve the research objectives we need to answer a series of questions related to the investigation and describe the motives, impacts and benefits, problems and difficulties associated with the adoption of the AAOIFI standards; to understand the factors or key players that might lead the UAE to adopt the AAOIFI standards; to examine the AAOIFI standards compared to IFRS; and in so doing, to identify the differences and determine which system may better satisfy user needs.

The main research questions are:

• What is the impact of applying the AAOIFI accounting standards on the UAE Islamic banks?
• What are the roles of key players in the development of the Islamic accounting standards in the UAE?
• What are the main differences and similarities between the applications of AAOIFI accounting standards and the International Financial Reporting Standards (IFRS), and which system can better satisfy users’ needs?

When looking at the possible adoption of AAOIFI accounting standards, we need to answer the following sub-questions to better clarify the key factors associated with the primary research questions:

• What are the user needs for accounting information in the UAE Islamic banks?
• Do Islamic banks in the UAE need a corresponding alternative set of Accounting Standards?
• Is the Fatwa & Shariah Supervisory Board sufficient to ensure the Islamic banks’ compliance with Shariah in the UAE?

• What are the underlying factors that may influence the adoption of AAOIFI accounting standards in the UAE Islamic banks, and which issues might act as barriers to their adoption?

• Identify the main challenges in adopting AAOIFI accounting standards? What problems and difficulties would UAE Islamic banks face when applying AAOIFI accounting standards?

• What factors can influence, and the benefits that may arise from, the adoption of AAOIFI accounting standards in the UAE Islamic banks?

1.6 Data collection methods

In order to answer the research questions and achieve the research objectives, this study used different sources of data. The data collection techniques used were both qualitative and quantitative. The researcher paid attention to the quality of the sources, and the collected data has been tested to provide assurance that all data was valid and reliable.

This study used a mixed method approach. The sources of information included IFRS, AAIOFI accounting standards, banks’ annual reports, legal standards, previous related studies, and surveys. The researcher identified the IFRS which were applied by Islamic banks in the UAE. Then the researcher investigated the potential implementation of accounting standards that have been developed by AAOIFI. The researcher critically analysed specific terms, standards and disclosure rules in order to identify the similarities and differences between IFRS and AAOIFI accounting standards. The mixed method approach helped to achieve cross-validation of data (Hussey & Hussey 1997). The combination of the two approaches permitted the shortcomings of each to be overcome.

This research also has examined the potential adoption of the AAOIFI accounting standards in the UAE Islamic banks. A qualitative method was used to generate persuasive inputs for the research study to measure and validate the underlying factors, which reported the significant impacts and challenges of the potential adoption. In order to better understand the expected impacts of this potential adoption, the researcher has conducted surveys with managers involved in the UAE banks to gain knowledge and understand the ways in which accounting standards will potentially impact Islamic Banks. There were some open-ended questions through which managers could identify barriers to adoption. The researcher also
conducted interviews with the key players involved in the AAOIFI accounting standards setting; to gain a firsthand knowledge and understanding of the processes that may challenge them when adopting AAOIFI accounting standards, and identified ways in which individuals and institutions can circumvent these challenges.

IFRS and AAOIFI accounting standards were compared in order to identify the main differences between them and use these differences to explore which system was most suitable for satisfying users’ needs, through the use of questionnaires and interviews. To analyse the differences between the systems, qualitative methods were adopted and applied at the initial stage to focus on the issues which allowed me to examine individual accounting standards.

The researcher first conducted a pre-testing of the questionnaire by meeting three managers from different banks and discussed with them the major questions in order to identify what issues needed to be included in the questionnaire survey. This allowed the researcher to construct the first questionnaire draft. After the initial questionnaire had been constructed it was pre-tested through three different managers from different banks to assess the relevance and validity of the questions.

Other data which needed to be used for the research study was obtained directly from the internet and other sources including journals, government websites, administrative public records, research projects, library databases, and private organisations’ data. The use, or analysis, of such existing materials required permission in certain circumstances.

1.6.1 Questionnaire survey

The survey method using a questionnaire helped in identifying key aspects of the study directly related to understanding the feasibility of the adoption of Islamic Banking Standards in the UAE Islamic banks. This method was based on the preparation of an appropriate questionnaire comprising of a set of questions that are related to the defined research objectives, so that required data could be collected from selected participants (Bryman & Bell 2007).

The questionnaire was administered to current managers and professionals who already apply Islamic financial transactions and methods. The questionnaire was designed to be completed within a 15–20 minute time frame so that banks would not find it burdensome. The questionnaire included closed questions scored using a Likert scale and also included some
open-ended questions which were analysed using qualitative methods for those questions where managers wanted to provide more information than a Likert scale allowed. After the final version of the questionnaire was completed, the researcher made arrangements with different Islamic banks to select managers to take the questionnaire survey in their normal work time. Islamic banks from the UAE were approached to participate.

The Likert scale used for closed questions measures the extent to which a person agrees or disagrees with a particular statement. According to Sekaran (2000), respondents typically indicate a degree of agreement or disagreement with a variety of statements about some attitudes, usually using scales containing five or seven points. The Likert scale used in this study was designed on a five point scale ranging from ‘Very Strongly Agree’ to ‘Very Strongly Disagree’. Sekaran (2000), identifies an inherent problem that arises when using an odd-numbered Likert scale as it permits respondents to choose to ‘sit on the fence’, marking the mid-point neutral answer. That is, when using a 1 to 5 rating, respondents could be tempted to mostly use 3. Such a choice could tend to artificially indicate a central tendency and kurtosis in the data that might otherwise not be present. Alternatively, an even-numbered scale could be used, but it would force respondents to make a choice either side of an imaginary mid-point, thus introducing another form of artificial bias through skewing data either side of the mid-point. Therefore in this study, the choice was made in favour of the least-problematic option, selecting an odd-numbered Likert scale ranging from 1 to 5.

1.6.2 Telephone interviews

The posted questionnaires alone were not enough to achieve all the research objectives, particularly as some of the questions required exploring in more detail and going into greater depth about key players’ experiences related to the potential adoption of AAOIFI by the Islamic banks in the UAE. For this reason primarily, telephone interviews were selected as a data collection approach for the qualitative portion of this research providing a greater volume and depth of data to enhance the research. The interviews which were used in this research phase were conducted via telephone with five of the key people engaged in accounting standards of Islamic banks in the UAE. Each interview lasted between 15 to 30 minutes.

1.6.3 Analysis of data collected

The data collected from the questionnaire survey was analysed through the SPSS statistics for windows (Version 17.0) software providing significant assistance in evaluation of the
descriptive statistics relating to the research questions. The results of this research were offered to the banks that allowed the researcher to questionnaire survey their managers. The identities of those respondent managers were kept confidential.

Qualitative analysis was used with regard to open-ended questions that were included in the questionnaire. Qualitative method was used for analysing open-ended questions, helping to make sense of the unstructured information through the provision of workspace and tools. The qualitative analysis method was also used in the telephone interviews, introductory documentary analysis for the secondary documents and a content analysis of the outcomes of the interviews. The analysis of the results relating to the potential adoption of AAOIFI accounting standards, were subjected to the Kruskal-Wallis test: level of significance, Skewness, Cronbach’s alpha and Exploratory Factor Analysis (EFA), between the variables. This research also used Confirmatory Factor Analysis (CFA).

1.6.4 Sampling

Among four major Islamic banks in the UAE, a total of 80 questionnaires were randomly distributed to managers and professionals. These managers and professionals were selected because they had been involved with Islamic banks’ transactions on a daily basis and it was expected that they would have an understanding of the accounting standards as applied in the Islamic banks.

However, the selection of interview participants was based on purposeful sampling. The five key persons engaged in accounting standards setting from four different Islamic banks in the UAE, were selected based on their known positions within the Islamic banks.

1.6.5 Limitations

In the light of the results of the research analysis, bank managers of the selected Islamic banks identified the Islamic accounting rules and differentiated them from the traditional accounting standards. However, there were some limitations related to the study that might affect the generalisability of its findings. The main limitations are as follows:

Limited access to data collection

The first limitation was in accessing the banks. Some banks initially did not allow me to interview their managers. The solution was that the researcher stressed the benefits that would
be gained from the research and demonstrated that the researcher proposed to be quite open and transparent regarding the results, offering the findings to the interviewers and their banks when the research was completed.

Data collection procedures

The second limitation was that answers to the questionnaire survey questions were dependent on the perceptions, knowledge, experience, and the truthfulness of banks’ managers and professionals. The solution was to allow survey respondents to be interviewed in a very quiet environment so that they could concentrate and be allowed ample time to recall all events and influences of relevance. The researcher asked the same question more than once, in different ways, to check on the consistency of answers received.

Limited number of relevant studies

The third limitation was the challenge of starting a research study of accounting standards in the UAE, because most literature relevant to the UAE had been related to finance rather than accounting. The greatest difficulty the researcher faced was finding literature about the banks’ application of accounting standards in the UAE, as most of the researcher’s readings were based on the adoption of accounting standards for banks worldwide. The availability of literature about UAE’s banks was rare.

1.6.6 Ethical considerations

Approval to conduct research with human subjects was granted for this study by The Human Research Ethics Committee of the University of Canberra. This study was subject to primary ethical issues for humans in accordance with the national statement on ethical conduct in research involving humans and the policies of the University of Canberra. Confidentiality procedures were compliant with the University of Canberra’s policy for responsible practice of research. The questionnaires were anonymously completed and the participants’ privacy was protected as far as possible. The information sheets and consent forms explained to participants that any information that they provided would be kept confidential. Unlike the data collected from publicly available secondary data, a questionnaire survey involved ethical requirements, since it required individuals’ information regarding their beliefs and behaviours. Respondents were expected to be concerned about the potential risks to positions and reputations of both respondents and companies, if the supplied information were to be
made public. Therefore, privacy, anonymity and confidentiality of information were paid close attention to for the respondents and their companies at all stages of this research in order to minimize respondents’ risks and discomfort. The ethical considerations as well as the intention of the questionnaire survey were informed to respondents. The researcher provided references to prevent plagiarism, avoid any misleading, or false reporting of research findings. The data collected was treated confidentially.

1.6.7 Quality control

The researcher applied a strong focus on ensuring that the research conformed to the research standards required for both quantitative and qualitative methods, as the validity and reliability of the research process was essential as it influenced the accuracy and credibility of the findings.

1.6.8 Validity

The process of validation is to confirm that a measurement scale is properly calibrated and correctly measured the target phenomenon. A measurement scale is valid if it executes what it is supposed to do. The different forms of validity comprise content validity; construct validity, and criterion validity (Davis 2005). The validity of the methodology construct was tested through ensuring the variables used were appropriate. The researcher also tested which research methodology could satisfactorily address the research questions. So, internal validity focused on the relevance and the internal coherence of the analysis and results. External validity focused on the possibility of applying these results to other elements to ensure and verify that the different variables used in the research study would be able to be repeated in other studies.

1.6.9 Reliability

According to Davis (2005) the purpose of reliability is to confirm that the measurement scale is scoring consistently and is stable. For a measurement scale to be considered valid it also needs to be reliable. Measurement scales that are considered to be reliable must be accurate in their measurement. Therefore if the measuring scale is not accurate, it cannot be considered valid. The reliability of the research study was established through the structured methods embedded in the collected data. In particular, the researcher carefully designed the data
collection method and used different techniques for the analysis in a controlled research process.

1.6.10 Confidentiality and privacy

The researcher acted in a professional manner when interacting with participants in the conduct of interviews and the execution of questionnaire survey. Participation was voluntary with informed consent. The researcher ensured anonymity of the information provided, and the researcher made the purpose and the methodology of the research available to the participants before they decided to participate. Participants were offered an introductory letter to the surveys that described the purpose of the research and procedures, and the researcher explained the benefits and right of participants to cease their participation at any time without reason. Confidentiality of participants’ information was ensured, so organizations’ specific data and individual names were protected. The researcher ensured that the utmost level of confidentiality was observed. So, the results or disclosures would not jeopardise participants’ positions and their relationships with each other.

All surveys had a policy of absolute privacy. Managers’ names, or any form of identification were not requested in the survey. The primary objective of the survey was to seek an analytical basis for comparison between the Islamic accounting standards and the traditional accounting standards. There was a zero tolerance policy to exploit managers’ information and any bank that tried to use duress over this study was not part of the research.

Under all circumstances it was the obligation of the researcher, not to disclose the identity of participants, so that they felt confident in providing answers to the study in full knowledge that answers were completely private. All identifying personal and commercial information was coded. Should hard copies of the data have been stolen or copied, there was no identifying information attached to that data collected that could disclose an individual’s name or bank identity.

1.6.11 Accessing data

Data was stored by ACCESS using a security password to access the data. Data entered by the primary researcher remained as temporary data until finalized for approval for final storage. The primary researcher was the only person who had full authority over, and control of, the data for extracting, printing, editing and any other research-related processing.
1.6.12 Backup of data

Data entry was conducted on one machine (A) by the researcher. Data backup occurred on (Laptop A) everyday, then copied and stored on another storage device, both owned and controlled by the primary researcher. The primary researcher was the only person who did the backup and made copies.

1.7 Findings, implications and conclusions

Clear and precise findings allowed the researcher to conclude what was discovered and learnt from the study. This gave rise to a set of implications and in turn formed the basis of recommendations. The conclusions, and the rationale for them, were clearly stated. As described by Davis (2005, p. 490):

The logical steps should be detailed enough that the reader can see how the conclusions were arrived at and why the recommendations were made. The researcher should assess and reassess this section to ensure perfect clarity and meaning for the reader.

According to Staniback & Stainback (1988),

The research needs to identify for the reader why and how the analyses and interpretations were made and the way key concepts in the analyses evolved. In addition, the researcher needs to inform the reader of any unexpected findings or patterns that emerged from the data and report a range of evidence to support assertions or interpretations presented. (pp. 80–81)

The results of the research were easily understood and a clear line of reasoning revealed comprehensive conclusions as the basis for recommendations. Qualitative and quantitative approaches were used in the study as a consequence of the mixed method research approach adopted. The combination of the strengths of different approaches to test the results enhanced the comprehensiveness of the scope, reliability and validity of the research study.
1.8 Structure of the thesis

This research study contains seven chapters as shown in Table 1.1.

Table 1.1: Thesis structure

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<tr>
<th>Chapter</th>
<th>Topic</th>
<th>Structure</th>
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<tbody>
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<td>1</td>
<td>Introduction</td>
<td>Providing a short outline of this research study including; introduction,</td>
</tr>
<tr>
<td></td>
<td></td>
<td>objectives of this research, significance of this study, review of the</td>
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<td></td>
<td></td>
<td>relevant literature, research questions, data collection and methodology</td>
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<td></td>
<td></td>
<td>for the research and a short summary of the findings.</td>
</tr>
<tr>
<td>2</td>
<td>Literature review</td>
<td>Surveying the relevant published studies, concentrating on the Islamic</td>
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<td></td>
<td></td>
<td>accounting, Islamic banking, and Islamic accounting standards.</td>
</tr>
<tr>
<td>3</td>
<td>Background of this research</td>
<td>Providing a background and a brief history of IFRS &amp; AAOIFI accounting</td>
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<td></td>
<td>study</td>
<td>standards and their objectives.</td>
</tr>
<tr>
<td>4</td>
<td>Theoretical framework</td>
<td>Explaining the theoretical background of the research study.</td>
</tr>
<tr>
<td>5</td>
<td>Methodology</td>
<td>Explaining the research method and data collection process.</td>
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<tr>
<td>6</td>
<td>Data Analysis</td>
<td>Describing the analysis of the collected data.</td>
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<td>7</td>
<td>Results of Analysis &amp;</td>
<td>Discussing the results of data analysis, conclusions, limitations,</td>
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<td></td>
<td>Conclusion</td>
<td>research contributions and recommendations.</td>
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</tbody>
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Chapter 2 – Literature Review

2.1 Introduction

The aim of this literature review is to analyse various research studies related to Islamic accounting standards. It focuses on the most relevant published studies to provide a brief overview of Islamic accounting beginning with the accounting standards applied in the UAE. A detailed discussion of literature is provided to identify the principles and standards of Islamic accounting and the compliance of Islamic banks and the Fatwa and Shariah Supervisory Board with Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) accounting standards. The literature is divided into seven broad categories covering a review of the UAE’s adoption of accounting standards; evolution of Islamic banking and Islamic accounting standards; the objectives, characteristics, ethics and social responsibility of Islamic accounting; comparing Islamic & conventional banking; comparison of AAOIFI accounting standards with International Financial Reporting Standards (IFRS); compliance with AAOIFI accounting standards by Islamic banks and the Fatwa and Shariah Supervisory Board; a critique of the Islamic banking and AAOIFI standards; and the regulatory theories compiled about Islamic accounting.

2.2 The UAE’s adoption of accounting standards

This section has reviewed studies which highlighted the main factors which influenced the adoption of accounting standards in the United Arab Emirates. In their study, Joshi and Ramadhan (2002) argued that the main influence on whether or not a firm adopted IFRS was exerted by their external auditors.

Irvine and Lucas (2006) indicated that developing countries and emerging economies seek to enter global capital markets by adopting IFRS, and faced difficulties in doing so. Irvine and Lucas (2006) concluded that the UAE as one of a number of developing economies adopting IFRS, faced challenges of culture, regulation and transparency, which were threats to the process of implementation of IFRS. They suggested that the UAE will need to develop suitable regulatory systems to overcome issues relating to confidentiality and fraud.

Hassan (2009) highlighted that there is no legislation in the UAE to compel the financial institutions to adopt specific accounting principles. However, most financial institutions
adopted IFRS especially given that the UAE central bank regulations required banks and financial institutions to prepare their financial statements according to the IFRS format.

Al-Qahtani (2005) remarked that there was a federal law promulgated in February 1999 in the UAE requiring that financial institutions and banks prepare their financial statements using the IFRS format from 1 January 1999. However, he agreed with Hassan that there is no enforcement system for auditing and accounting processes in the UAE. Zoubi and Al-Khazali (2004) also acknowledged that all companies and banks in the UAE have to prepare their financial statement in accordance with the IFRS since 1999 onward. However, they commented that the adoption of IFRS facilitates processing of transactions and increases the capital. The financial statements of companies in the UAE prepared in accordance with IFRS will be readily comparable to foreign firms which will encourage foreign investments.

Aljifri and Khasharmeh (2006) investigated the suitability of the IFRS to the UAE financial environment with regard to the relevant items that might affect the adoption of IFRS in the UAE. They evaluated the corporate annual reports issued by the UAE companies with reference to using IFRS and analysed the perceptions of preparers and users of financial information to examine the suitability of adoption of the IFRS and its impact on corporate reporting practices in the UAE. Their sample comprised 326 listed and unlisted companies in the UAE. They found that 87% of the examined firms published their financial information in English which can be considered a robust factor for adopting IFRS. They also indicated that the effective factors for adoption of the IFRS are the English language and the company’s size, while the company’s market-listed status and the category of the financial sector have no significant impact on the adoption of IFRS in the UAE.

The main finding by Aljifri and Khasharmeh (2006) was to address the advantages of adoption of IFRS in the UAE such as to develop an understanding of financial reporting by international experts, support foreign investments, improve comparability and transparency of financial statements and supply the government with information to prepare appropriate economic plans. Aljifri and Khasharmeh (2006) claimed that 95% of the UAE firms which adopted IFRS indicated a high level of consistency with IFRS. However, 53% of the participating experts agreed on the need to modify IFRS to suit the UAE environment.
2.3 Evolution of Islamic banking and Islamic accounting standards

Islamic banking recently has grown and expanded globally after gaining support and endorsement from the oil-rich Gulf countries (Henry & Wilson 2005). Islamic banking has achieved further success after multinational and conventional banks such as Citibank, HSBC, American Express and Banque Nationale de Paris began providing Islamic products to millions of Muslims around the world with investments and saving opportunities marketed and promoted under the banner of Islam (Pollard & Samers 2007). The main reason for the success of these banks is in fulfilling the needs of Muslims to invest their money in ways which are compatible with their religious beliefs and cultural values (Iqbal 1997; Murtuza 2000).

Hameed (2000) states that many reports (income statement and balance sheet) prepared in accord with conventional accounting principles are useful for Islamic accounting and could be used in Islamic accounting processes as well. However, a complete acceptance of conventional accounting standards would not well serve Islamic businesses. Hameed (2000) recommends a mixed approach in developing Islamic accounting standards consisting of Islamic and conventional accounting principles.

Zaini (2007) commented that due to the lack of proper accounting standard Auditing Islamic financial institutions (IFIs) rely on different accounting methods for the preparation of financial reports. IFIs faced problems in the preparation of various accounting reports such as profit and loss account, balance sheet because conventional accounting standards do not satisfy the needs of Islamic business entities. However, accounting standards developed by AAOIFI have helped in serving the accounting requirements of Islamic financial institutions (Ziani 2007).

Shadia (2007) stated that Islamic accounting standards, which can be adopted by all Islamic business entities, will help in the comparisons of financial statements of peer financial institutions so that true valuations of these companies may be judged by investors and society.

Lovett (2002) documented that, with financial statements prepared under different accounting standards a problem possibly will exist in comparability, creditability and reliability of financial statements prepared globally. Lovett (2002) argued that the concept of a single set of Islamic accounting standards is not appropriate given the different business environment. However many researchers in different Islamic countries have claimed that a single
accounting standard will increase the number of companies complying with AAOIFI standards. Abongwa (2006) claimed that accounting standards reflect the culture of the particular country so it should be made accordingly. On the same issue, Karim (2001) pointed out that AAOIFI accounting standards applied Shariah laws and issued accounting standards which could be easily interpreted by users.

2.4 Objectives and characteristics of AAOIFI accounting standards

The objective of the AAOIFI standards is to promote the Islamic banking system and organize the transfer of Islamic banking and finance activities across national and regulatory contexts (Maurer 2002). The AAOIFI has been successful in promoting its standards to Islamic financial institutions globally.

Papers by the AAOIFI have proposed various objectives such as decision usefulness, stewardship, accountability of organizations towards society as main objectives of Islamic accounting standards (AAOIFI n.d. (b)). Authors such as Kahf, Ahmed and Humod (1998) have indicated that the basic principles of Islamic banking originate in the axioms of justice, harmony and human nature. They added:

> Islamic banking provides financing in the form of equipment, machinery, and other procedures and consumers’ good for deferred payment. It also provides means of payments and procedures’ principal on projects on the basis of sharing the actual, real-life outcome of production process. (Kahf, Ahmed & Humod 1998, p. 11)

Many researchers have the view that the objective of conventional accounting is not in full harmony with Islamic socioeconomic objectives. In particular, Adnan and Gaffikin (1997) state that some conventional accounting standards are contradictory to the principles of Islamic accounting. Principles such as conservatism and the concept of historical cost have no importance in Islamic accounting. Adnan and Gaffikin (1997) further affirm that the matching concept of conventional accounting standards contradicts principles of Shariah because it considers revenue-expenses rather than the asset-liability approach. One of the main objectives of accounting in Islam is to uphold the accountability through Zakat, which is a concept in Islam that deals specifically with the measurement of assets. The Holy Qur’an stated:

> And establish prayer and give Zakat and bow with those who bow [in worship and obedience]. (Qur’an 2:43)
Hameed (2000) and Adnan and Gaffikin (1997) have also expressed views on the objectives of Islamic accounting. They argued that putting objectivity in the context of qualitative characteristics indicates that it is related more to the secondary objectives of accounting information which is to facilitate accounting users in making economic decisions for their own interests.

Many researchers such as Čihák and Hesse (2008) argued that the Islamic finance industry has a bright future. Their study discussed the current trends in Islamic finance, which has become mainstream and a floating market for Sukuk (Islamic bonds). They argued that this extraordinary asset base raises many challenges, particularly in the areas of banking, capital markets and regulation. The challenges they identified are notably the economic and legal bottlenecks of Sukuk, banking-specific issues, such as liquidity risk management and business models, as well as disharmonized financial regulation (Čihák & Hesse 2008).

However, many researchers such as Iqbal (1997) recognized that Islamic finance is emerging as a rapidly growing part of the financial sector in the Islamic world. He argued that Islamic finance is not restricted to Islamic countries, but is spreading wherever there is a sizable Muslim community. Furthermore, he stated that the basic framework for an Islamic financial system is a set of rules and laws, collectively referred to as Shariah, governing economic, social, political, and cultural aspects of Islamic societies. Iqbal (1997) identified that the basic principles of an Islamic financial system which should be addressed by AAOIFI accounting standards can be summarized as follows:

a) Interest prohibition;
b) Money as potential capital;
c) Risk sharing;
d) Prohibition of speculative behaviour;
e) Sanctity of contracts;
f) Shariah approved activities.

Gambling (1974) and Gambling and Karim (1991) pointed out the accounting practices which are specific in the Islamic environment. These were factors such as the prohibition of Riba (interest or usury) and the payment of Zakat (a religious levy as a fundamental duty).
Ray (1995) examined the application of the values of traditional Islamic culture to Islamic banking. He provided an overview of Islamic banking, its development, participants, structure, and aims. He focused on the advantages and disadvantages of Islamic banking as well as the specific areas where problems are encountered and gave a brief account of transactions such as Mudharaba (profit sharing), Musharaka (Partnership) and Murabaha (Cost-plus financing). Ray (1995) was very positive in his overall assessment of the past achievements and future prospects of Islamic banking especially with regard to the efforts of Islamic bankers to turn Islamic banking into a model of rational and dynamic compromise between modernity and fundamental Islamic religious values.

The study by Ahmad (1987) surveyed Islamic financing techniques used by Islamic financial institutions in different countries. Ahmad (1987) noted the similarities and dissimilarities of these financing techniques in various institutions and she claimed that Islamic banking is more interesting and complex than conventional banking as the practices of Islamic banks are more diverse and complex than those of conventional banks. For example, Islamic banking has been able to offer various kinds of financial products even though it is in the area of assets rather than liabilities. Ahmad (1987) added that Islamic banking has been able to offer various types of financial techniques such as Murabaha which is the most widely used technique in Islamic banking. Ahmad (1987) also commented that the greater part of the financing provided by Islamic banks goes to short-term trade and the financing of real estate.

The progress of Islamic banking in both theoretical and practical respects has been reviewed by Ahmad (1995). He described the operational details of Islamic banks and the effects of Islamic banking on savings, investment, growth, efficiency and stability. He also highlighted the basic principles on which Islamic banking is based such as Mudharaba financing, Musharaka, profit and loss sharing basis, and Qard Hasan (Benevolent loan).

Ahmad (1995) analysed the socioeconomic consequences of adopting the Islamic system of banking and finance. He illustrated that with the theoretical developments, the practice of Islamic banking has been growing rapidly, and there have been a number of contributions shedding light both on the operating procedures of Islamic banks as well as the results achieved in terms of deposit mobilization, profitability and achievement of Islamic socioeconomic objectives.
Explanatory factor analysis was employed by some studies such as Dusuki and Abdullah (2007). They examined the main factors that motivate customers to deal with Islamic banks particularly in a dual banking environment by using factor analysis. They examined two aspects: the quality of services in Islamic banks while maintaining its Islamic credential and reputation; and, the customer services policies of Islamic banks to reap its potential as a strategic tool to achieve competitive advantage, enhance reputation and secure customers’ allegiance. They commented that,

The selection of Islamic banks appears to be predominantly a combination of Islamic and financial reputation and quality service offered by the Islamic bank. Other factors perceived to be important include good social responsibility practices, convenience and product price. (Dusuki & Abdullah 2007, p. 142)

They added that Islamic bankers can no longer rely on the marketing strategy of attracting religious customers who might only be concerned about Islamic financial product.

Various modes of Islamic finance and their risk and other characteristics were examined by Anjum (2008). He commented that Islamic banks have shown good performance with respect to the returns on their assets and equity and have also demonstrated better risk management and maintenance of adequate liquidity than commercial banks Siddiqui (2008).

Another study conducted by Sufian (2006) analysed the efficiency of the Malaysian Islamic banking sector during the period 2001–2004. He attempted to provide evidence of the returns to scale of the Malaysian Islamic banking sector. His results suggested that the domestic Islamic banks could have produced the same amount of outputs by only using 83.5% of the inputs they currently employed, and the number of Malaysian Islamic banks experiencing economies of scale has increased dramatically from 26.7% in year 2001 to 60.0% in year 2004. He confirmed that during the period of study, the majority of Malaysian Islamic banks have been operating with the wrong scale of operations. His study also suggested that scale inefficiency dominates the pure technical inefficiency effects in determining Malaysian Islamic banks’ technical or overall inefficiency.

Islamic business entities are recommended to use market value of assets contrary to the earlier concept of using historical cost. In a study paper by Haniffa and Hudaib (2001), they argued for the need for a change in the Islamic principle of measurement of assets, arguing that accounting principles are largely targeted for the welfare of society instead of business perspectives. They provided an analysis of the stages in the modern Islamic finance history
from the 1940s to the present time and suggested the need for a change to Islamic principles of measurement of assets. Given the recent instances of corruption and accounting fraud they suggested that including Islamic ethics into accounting education is a current requirement. Haniffa and Hudaib (2001) explained that an organization or an accountant is not only accountable for internal stakeholders as they are equally accountable to the society at large. Islamic principles emphasize that humans are accountable to god and that human beings should follow steps which have been guided by the prophets. Mahdavikhoua and Khotanloub (2012) asserted the need for imbuing Islamic ethics into accounting. They believe that the existence of mere accounting standards and regulatory purpose will not curb an increase in fraud cases. For developing ethics in accounting, Islamic principles need to be incorporated. An accountant is accountable to not only the internal stakeholders like shareholders and employees but also to the other external stakeholders such as creditors, customers and the like. Ethics in accounting has gained importance after the demise of very well-known organizations such as Enron and Arthur Anderson.

A rise in Islamic finance has forced Islamic organizations to follow a code of conduct. Ethical values of an accountant are very important because an organization’s future depends on the financial reports prepared by its accountant (Mahdavikhoua & Khotanloub 2012). They added that accountability in Islam means human beings are answerable to God for their actions. The accounting profession in Islamic law is called Fardkifayah meaning collective religious duty. An accountant is responsible for his/her actions, so inculcating ethics in accounting education will help in shaping an ethical accountant (Mahdavikhoua & Khotanloub 2012).

Huss and Patterson (1993) have presented six objectives that need to be met if the principles of ethics are included in a study of accounting. These objectives relate to, recognizing issues with ethical implications in accounting, developing a sense of responsibility, developing the abilities needed to deal with ethical dilemmas, learning to deal with uncertainties, developing the ability to alter ethical behaviour and understanding the relationship of accounting ethics with the general ethics field.

Huss and Patterson (1993) have also suggested that to imbue ethics in an accounting student it is necessary to develop an attitude to the sharing of knowledge among teachers and students. Improvements can be effected only if students are encouraged to share their views and teachers allow them to do so whenever it requires being implemented. They have also pointed
out in their paper that the sheer identification of an ethical situation is not enough; people should be encouraged to voice their views when situations need actions.

Kamla (2009) discussed the contradictions between the ethical claims of contemporary manifestations of Islamic accounting practices and their actualities. She explored the potential of the contemporary Islamic accounting to join the critical accounting agenda. Kamla (2009) indicated that manifestations of Islamic accounting fall significantly short of realizing the enabling praxis of a more emancipated accounting and constitute little departure from conventional accounting and finance. She claimed that Islamic accounting research is diverting from its primarily proclaimed social and moral roles due to the minimal critical theorizing and the narrow instrumental emphasis of the majority of Islamic accounting research.

On the other hand, Kamla (2009) identified ways forward for Islamic banking to recognize a more emancipated praxis. She discussed the Islamic teachings such as holism, social justice and knowledge development which may shift Islamic banking and accounting practice to an emphasis on social justice, working with local communities, and the provision of business opportunities for the poor. She added that Islamic banking, in order to broaden its social agenda and realize its ethical claims, Islamic banking needs to build more on the Islamic teachings of holism and justice, and engage and cooperate with other religious and non-religious institutions focused on social justice and community empowerment. Kamla (2009) suggested that Islamic banks can learn from the successful experience of the Grameen Bank to empower the poor and the community to face the global business expansion by contributing to expand the microcredit systems to the extremely poor in Muslim societies.

Kamla (2009) also suggested that the role of accounting regulatory bodies should be changed to adopt a more holistic approach. She added that AAOIFI, in order to properly claim to operate and develop accounting standards according to Shariah, should play the role of regulating business organizations in the interest of public, equality, sustainability and social justice.

2.5 Comparing Islamic and conventional banking

Another group of studies include those which compare Islamic banking with conventional banking. The focus of the majority of these studies is on comparing the principles and the performance of these banks by using financial ratios and constrained by the time span and the
number of Islamic banks. According to Haroun (1998), the principles of Islamic banking based on Shariah used by the Islamic banks have been categorized in four areas, namely profit and loss sharing principles, fee-based principles, free-service principles, and ancillary principles. The principles in these categories were universally used by all Islamic banks regardless of the country in which their operations are based (Tricker 1976). Some Islamic banks have adopted principles in all four categories. However, not all Islamic banks have listed all four categories of Shariah principles. Some Islamic banks in different countries only employed three of the above-mentioned four principles (Haron 1998). Some studies such as Lewis (2001) focused on the nature of Islamic accounting, banking and finance. Lewis’s study (2001) addressed the unique characteristics of Islamic accounting. He argued that Islam has formulated a comprehensive system of ethics governing how businesses should be run, how accounting ought to be undertaken, and how banking and finance is to be arranged. He suggested that the development of Islamic accounting theory should be based on the provisions of Islamic law. Lewis (2001) pointed out that objectives should be first established based on the teachings of Islam and then need to be considered in relation to contemporary accounting thought.

The widespread adoption of IFRS according to Choi & Mueller (1992), will increase understandability of financial statements, save time and money, ease interpretation and improve the credibility of the financial reporting process and profession. But the domain of international accounting standard-setting is dominated by the Anglo-American model. Some of the IFRS do not reflect Islamic practices particularly in regard to interest transactions (Bhattacharjee & Islam 2009). On the other hand, El-Din (2004) indicated that the objectives of financial accounting for Islamic banks and institutions were to verify the rights and obligations of all interested parties in accordance with the principles and concepts of fairness, clarity and business ethics of Shariah principles; participate in the preservation of Islamic banks’ assets, the rights of Islamic banks and the rights of others in an appropriate manner. Also, El-Din (2004) added that the financial reports of Islamic banks provide useful information to report users, and consequently enable them to make legitimate decisions in their dealings with Islamic banks; and Participate in the enhancement of management and Islamic banks’ productive capabilities, and encourage compliance with the established goals and policies, of Shariah principles, in all transactions and events.
Related to the concept of social accountability in Islam is the principle of full disclosure. Lewis (2001) recognized that truthful and relevant disclosure of information is important in different aspects of Islamic life. He illustrated that there are responsibilities such as paying Zakat which is a religious obligation to assist the poor and its calculation requires disclosure of the worth of assets and liabilities. Lewis (2001) believed that full disclosure is necessary for predicting future obligations and assessing investment risk in Islamic partnership arrangements. However, substantial doubt must arise whether compliance with the conventional accounting practice of being conservative regarding asset valuation and income measurement can conform to Shariah. Adequate disclosure requires that a financial statement should contain all material information necessary to make it useful to its users, whether it is included in the financial statements, the notes accompanying them, or in additional presentations. Lewis (2001) argued that the disclosure of all required information for the accomplishment of faithful obligations and the making of economic and business decisions consistent with that ethos is the most important principle of an Islamic accounting system. Dedicated Islamic financial institutions have been established to allow Muslims to conduct their financing in religiously acceptable ways which conform to these requirements as referred to by Lewis (2001). The author indicated that the Islamic system of banking revolves around the substitution of profit and loss sharing principles for interest-based borrowing and lending activities. Apart from the common principles of Shariah there are specific countries that listed some principles which are mandated for use by the Islamic banks operating in the specified countries (Van Knippenberg 2000). Though, these principles are familiar within the country in which they are used and reported, this does not imply that other countries not applying these principles, are unaware of these principles (Haron 1998). Due to the different regulatory requirements and legislation, the relevance and comparability of financial statements were the foundations upon which accounting standards were predicated (Sarea 2012). The main objectives of financial accounting are to assist a company to analyse the type and nature of information which should be a part of their financial reports in order to provide assistance to the users of these reports in making informed and sound decisions (Hoggett, Edwards & Medlin 2003). The government agencies usually have the power and right to directly obtain the specific information that best serves their requirements. However, other external users (such as equity holders, holders of investment accounts, current and savings account holders, other depositors, other dealers with Islamic banks, Zakat agencies and regulatory agencies) of information can only obtain the common information contained in the Islamic banks’ financial reports (El-Din 2004).
The development of the AAOIFI accounting standards is most importantly underpinned by the theoretical requirements of the Shariah principles. Khan (1994) stated that AAOIFI accounting standards did not allow the application of the principle of time value of money with respect to a contract of exchange where there are deferred payments involved. There is a strict prohibition on transactions based on debt and interest payments in the AAOIFI standards. Khan (1994) argued that not all of the accounting standards of IFRS are suitable for the Islamic banks’ environment as certain standards may be difficult to apply, or at least difficult with regard to Shariah principles, and claimed that IFRS removed the essence of Shariah principles by emphasizing the concepts of time value of money and interest.

Another study which compared Islamic with conventional banking is by Hasan (2005) who examined the reasons for a widening gap between the conventional theory and current practice of Islamic banks. He argued that it is not always valid to say that Islam is averse to granting of a time value for money. He added that some structural changes in Islamic financial arrangements are suggested to create a balance in the use of profit and loss sharing and deferred contracts in Islamic banking. His study concluded that Islamic banks have mostly been designed using the same model of commercial banks in terms of their outlook, objectives, procedures, training and modus operandi. They are required, on the other hand, to undertake project financing of risky ventures, and address social aspirations for development and wealth creation. As well, Islamic banks hardly have the aptitude, support or personnel to do what we expect them to do (Hasan 2005).

Shariah plays a main part in Islamic finance and according to Islamic scholars; Shariah is simply God-ordained sacred Islamic law that rules each and every aspect of a Muslim’s life. Shariah is the constitution of the Islamic world (Khan et al. 2011). Islamic economic principles underpin the Islamic banking system and financial accounting in the Islamic banking system. Islamic economics has been defined as the application of economic knowledge and facts according to the principles of Shariah (Malik, Malik & Waqas 2011). There are a number of Islamic financial instruments which can provide Shariah compliant finance such as Murabaha, Mudharaba and Shirkah which were designed to follow Islamic principles. Some studies focused on the Islamic contracts which can provide Shariah compliant finance such as Murabaha, Gharar, Mudharaba and Shirkah which were designed to follow Islamic principles. El-Gamal (2000) distinguished between credit sales and Murabaha. He illustrated that rarely is Murabaha used by Islamic banks with the price paid
immediately by the customer. So, there would be no financing included, and the Islamic bank would simply be a middle-man or broker-agent. When a customer approaches an Islamic bank to finance a purchase through Murabaha the payment of the price is usually deferred, and most commonly paid in instalments. According to Shofawati (2014), Islamic law prohibits the charging and paying of interest but allows the earning of profits (Murabaha) on the basis of participation in the market. This legal injunction has motivated the establishment and successful operation of a number of Islamic financial institutions. Islamic finance involves structuring financial instruments and financial transactions to satisfy traditional Muslim strictures against the payment of interest and against engaging in gambling. It is a field of growing importance for conservative Muslims, who are uncomfortable with the western style bonds and banking that involve payments of interest (Shofawati 2014). Shariah also attempted to refrain from Gharar (speculation). Al-Suwailm (1999) explained Gharar as a sort of gambling, and it is forbidden by Shariah principles because it uses other’s wealth for nothing. Islamic economic principles and Islamic laws give priority to Mudharaba (a type of limited liability business alliance where capital is entrusted by one or more investors to an agent-manager) and Shirkah (an agreement of association made by two or more parties) forms of business partnership (Sulaiman 2003).

One of the main differences between conventional banking and Islamic banking is a prohibition on interest. Islamic law emphasizes that Riba is not allowed. The general rule for accumulating wealth in Islamic economics was to earn a profit by assuming the risk of doing so whilst strictly condemning Riba (Ahmad, Rehman & Saif 2010). According to Adeniran (2014), Islamic banks have found ways to make money from lending. Islam encourages Muslims to invest their money and to become partners in order to share profits and risks in the business instead of becoming creditors. As defined in the Shariah principles, Islamic finance is based on the principle that both the provider and the user of capital are supposed to equally share the risk of business ventures. Instead of demanding interest, they buy the asset outright on behalf of the borrower. The borrower pays off the loan and a fee for using the asset until the amount is repaid and ownership transfers to the borrower. The rights to loan repayments can be sold as an Islamic bond (Sukuk), similar to mortgage backed securities but instead of a yield, the bondholder receives repayments on the loan, and some rent. Consequently, Islamic lenders have not yet entered money markets that have recently emerged (Yeates 2008).
Another important difference is between Islamic rules permitting leasing and conventional financial leasing. El-Gamal (2000) indicated that a leasing agency must own the leased object for the duration of the lease, and leasing an automobile from a car manufacturer or dealership may in principle be permitted. Furthermore, El-Gamal (2000) illustrated that the difference between leasing and *Ijarah* will be in the form of the contract. The lease is structured in accordance with the various conditions detailed in books of jurisprudence; it will contain no interest (*Riba*). El-Gamal (2000) believed that Islamic law puts many restrictions on contracts to attain maximum justice in a financial transaction, minimizing the potential for legal disputes, and building a healthy and stable financial and economic system.

According to Dar and Presley (2000), Islamic banks mainly differentiate their activities and products from conventional banks by sharing profit and loss with their investors and depositors. They defined Profit and Loss Sharing (PLS) as the ‘contractual arrangement between two or more transacting parties, which allows them to pool their resources to invest in a project to share in profit and loss’ (Dar & Presley 2000, p. 4).

Rates offered by Islamic banks or financial institutions are different from conventional banks on the basis of risk involved. To avoid any transaction that may fall in the usury category, risk needs to be calculated. This is also the reason behind the profit rates of the banks being calculated according to the interest accrued from one year to another instead of changes in rates. This concept has been mentioned in the paper by Gafoor (1995).

Ariff (1988) analysed the difference between interest rates offered by an Islamic bank and by conventional banks. This study argues that Islamic savings and investments banks are highly motivated by the return rate. Hence it was concluded that if banks want to retain old customers and attract new ones, they have to provide a high rate of return.

Ahmad & Mansor (2003) conducted a study in Malaysia through the procedures of the Granger causality test and unit root test, in order to find the causal relationship between Islamic and conventional banking instruments. They concluded that Islamic banking should consider the interest rate first then they should adjust the profit rates.

Chong and Liu (2009) also conducted a study to find the differences between the conventional banks and Islamic banks. They concluded that there is not much difference between the two; however, one point of differentiation is interest rates (*Riba*).
Harahap (2002) discussed the differences between Islamic accounting and conventional accounting in terms of the issues of disclosure in annual report. He illustrated that conventional accounting provides both mandatory and voluntary criteria concerning the level of disclosure in an annual report. On the other hand, he described Islamic accounting as an emerging model prominently represented by AAOIFI including a somewhat different set of disclosure requirements for the banking sector. Yudistira (2004) suggested that the interdependence of Islamic banks or other financial system is significant and any regulator, especially where the bank operates, should consider Islamic banking in the search of global financial stability. He indicated that Islamic banks in the Middle East countries are less efficient than their counterparts in other countries which are relatively new and very much supported by their regulators. Hassan and Lewis’ (2007) paper dealt with Shariah concerns related to product development in Islamic finance. They pointed out that Islamic banks, like other banks operating in a much more competitive environment, seek to boost their performance and profitability, but unlike their competitors they must do so in a way that complies with Shariah.

Another researcher, Mariani (2010), emphasized that the Islamic banking activities follow Shariah law which is within the scope of socially responsible and ethical banking activities and different from that based on interest-based banking. His paper attempted to measure the input data required by Shariah-compliant banking in comparison with conventional banking to estimate their relative efficiencies and economies and returns to scale. His results showed that Shariah-compliant banking has higher input requirements relative to interest-based banking, but exhibits superior average efficiency only in Malaysia but inferior average efficiency in cross-country analysis.

Hamid, Craig and Clarke (1993) considered the influence of culture and religion on accounting practices. They reflected upon how Islamic cultures have typically failed to embrace western accounting practices and they considered how issues of religion had previously occupied a small space in the accounting literature. They stated:

The existing literature dealing with the interaction of business activity and Islam needs extending to capture the particular effects which compliance with Islamic beliefs have on the structure of business and finance within an Islamic framework. In particular, the incompatibility of many Western accounting practices with Islamic principles requires explanation. For jurisprudential Islamic law influences the conduct of businesses in a manner not accommodated automatically by Anglo-American accounting practice. (Hamid, Craig & Clarke 1993, p. 134)
Ahmad and Luo (2010) study compared Islamic banking efficiency to conventional banking efficiency in three European countries, namely Germany, Turkey and the United Kingdom. The study found lower cost efficiency for Islamic banks in comparison to the more conventional banks in Europe. They also stated that Islamic banks are technically more efficient than conventional banks. Rashid, Hassan and Ahmad (2008) highlighted the gaps in demand and supply in Islamic banks for satisfying customers. Islamic banks must incorporate the spirit of Islam in their work with effective governance and social development activities. On the other hand, to survive against competition and earn a respectable return for the owners and depositors, they recommended that Islamic banks must plan customer friendly, technologically assisted products and conduct widespread distribution of the product from different branches both in rural and urban markets.

Rashid, Hassan and Ahmad (2008) pointed out that Islamic banks have ample opportunities for engaging in social development in view of their profitability being dependent on profit-sharing equity partnerships.

Taufiq et al. (2009) found that there is no significant difference between the cost and profit efficiency of conventional banks versus Islamic banks, regardless of size and location of banks in both streams. They added that Islamic banks in the Middle East and Turkey scored the highest in cost efficiency while African Islamic banks scored the lowest in cost efficiency. Taufiq et al. (2009) indicated that Islamic banking performs the same intermediary functions but does not receive a predetermined interest from borrowers and does not pay a predetermined interest to the depositors. However, the amount of profit is based on the profit sharing agreements with the depositors and also with the borrowers (Taufiq et al. 2009). In addition, there are fee-based banking services that are similar to the conventional banks as long as there is no predetermined interest payment in the transaction (Taufiq et al. 2009). Therefore, Islamic banking is considered as a different banking stream as it prohibits the accrual of interest and replaces it with profit sharing which depends on the extent of the risk participation of the parties (Taufiq et al. 2009).

Hassan and Bashir (2003) utilized bank level data and examined the performance indicators of Islamic banks’ worldwide to analyse how bank characteristics and the overall financial environment affect the performance of Islamic banks. They used a variety of internal and external banking characteristics to predict profitability and efficiency. Hassan and Bashir (2003) also studied the effects of controlled and uncontrolled variables on Islamic banks’
profitability. While factors such as capital, overhead, gross domestic product and conventional interest rates were positively related to profitability, loan ratios, reserves taxes, and size were adversely related.

It was also found that Islamic banks’ profitability measures responded positively to increases in capital and negatively to loan ratios (Hassan & Bashir 2003). Their results revealed that a larger equity to total asset ratio leads to higher profit margins. They indicated that adequate capital ratios play a weak empirical role in explaining the performance of Islamic banks. Their results also pointed out the importance of consumer and short term funding, non-interest earning assets, and overhead in promoting banks’ profits. Hassan and Bashir (2003) suggested that the regulatory tax factors are important in the determination of bank performance. However, their findings suggested that reserve requirement does not have a strong impact on the profitability measures. They also indicated that the macroeconomic environment seems to stimulate higher profits. The size of the banking system has a negative impact on the profitability except the net non-interest margin (Hassan & Bashir 2003).

Baydoun and Willett (2000) indicated that the current value balance sheet be included as part of the reporting requirements of firms operating in an Islamic economy. In addition, they added that Shariah accounting reveals a stronger concern for social accountability and full disclosure. They illustrated that the focus in Islam is on the Unity of God. Given this focus, the entire community and the affected environment require accounting information that focuses on social accountability rather than the more narrowly focused personal accountability found in Western accounting information. They argued that it is not the same as modern accounting which is based on a secular philosophical foundation and which has focus on the owners of the entity in their financial accounting statements.

Baydoun and Willett (2000) summarized several key differences which exist between western financial system and Islamic financial system as follows:

- Philosophical viewpoint of western financial system is economic rationalism. However, philosophical viewpoint of Islamic financial system is unity of god.
- The principles of western financial system are secular, individualistic profit maximization, survival of fittest and process. However, the principles of Islamic financial system are religious, communal, reasonable profit, equity and environment.
• The criteria of western financial system are based upon modern practices, commercial law, limited disclosure and personal accountability. However, the criteria of Islamic financial system are based upon ethical law, originating in the Holy Qur’an, full disclosure public and accountability.

In addition, Baydoun and Willett (2000) asserted that the focus in Islam on the Unity of God, the community, and the environment need a degree of social accountability rather that the personal accountability found in Western societies. Also, the principle of full disclosure of accounting information is needed for the consensus to operate effectively; the disclosure should be based upon what ought to be disclosed in order to serve the objective of social accountability not upon the outcome of a political process. Baydoun and Willett (2000) remarked that the principle of full disclosure is interpreted to mean the disclosure of any information that should be made available to members of the community under the Muslim system of law. However, their paper was limited to emphasizing accounting under Shariah.

2.6 Comparison of AAOIFI accounting standards with IFRS

Another group of studies focuses on Islamic Accounting Standards and International Financial Reporting Standards (IFRS) Ashbaugh and Pincus (2001) investigated two issues. First, whether the variation in accounting standards across national boundaries relative to IFRS has an impact on the ability of financial analysts to forecast non-US firms’ earnings accurately; and second, whether analyst forecast accuracy changes after firms adopt IFRS. They found that the convergence in the accounting policies brought about by adopting IFRS decreases the analyst forecast errors.

Kamla, Gallhofer and Haslam (2006) focused on the notion of accounting for the environment through engagement with Islamic principles. They illustrated that this constitutes a contribution to a more substantive appreciation of the relevance of Islamic principles for the re-orientation of dominant accounting thought and practice. They added that Islamic principles considered are indicative of diversity in accounting practices at the macro- and micro-societal levels, whether in external or internal accounting. Kamla, Gallhofer and Haslam (2006) also commented that western transnational corporations have sought to promote their particular brand of corporate social and environmental responsibility accounting in Arab countries. They pointed out that accounting would not be limited to a financial or materialistic basis and there is nothing to restrict the form of accounting. They also believed
that from an appreciation of the *Tawheed* (Unity of God) accounting would be concerned to monitor and act upon changes usually at a macro level in flora and fauna and ecological phenomena.

Khan (1994) commented that the scope of disclosure is another unresolved issue of accounting discipline and that whether disclosure of accounting policies or treatments was judged material is critical in determining the results for a financial period. The regulating authorities in most countries are trying to raise the scope of disclosure. Khan (1994) argued that there is not only one international financial reporting standard to provide treatment for a particular Islamic transaction; for instance, any treatment which is not approved from the viewpoint of *Shariah* principles, should be replaced by AAOIFI accounting standard treatment.

Ahmad and Haron (2002) explored conventional and Islamic banking facilities, respondents’ understanding of the Islamic banking system, and their personal opinion regarding various aspects of Islamic banking products. They wanted to investigate the perceptions of persons responsible for the financial affairs of publicly listed companies in Malaysia. They also wanted to provide useful information to both policy makers in the government and also to those who manage Islamic banks in Malaysia. They indicated that providers of Islamic banking products and services have not done enough in educating customers about their products. In their study they highlighted that the most important factor perceived by corporate customers in selecting their banks is the cost of the services and products. They suggested that the cost of Islamic bank products should be lower than those of the products of the conventional banks to be attractive.

According to Maurer (2002), the demand for consistent accounting standards for Islamic business enterprises is advocated at least in part, on the need for standardization in the financial reporting practices of Islamic business organizations and Islamic financial institutions, to meet the needs of users. He described Islamic banking and finance as a worldwide phenomenon created not just within the Muslim nations of the countries of the Gulf Cooperation Council (GCC), but also Malaysia, Indonesia, Great Britain and the United States of America.

There are some researchers who studied Islamic Accounting Standards and explained the differences between these standards and International Financial Reporting Standards (IFRS).
Lewis and Algaoud (2001) argued that the demand for Islamic accounting standards is a response to the significant growth in Islamic banks and financial institutions that has occurred in recent years. They illustrated that the Holy Qur’an is a source of principles and guidelines, containing ‘approximately 500 injunctions of a legal nature, 20 of which are on economics’ (Lewis & Algaoud 2001, p. 21). For instance, ‘the injunction against Riba is derived directly from the Holy Qur’an, where the prohibition is mentioned four times’ (Lewis & Algaoud 2001, p. 29). Another important consideration for Islamic accounting standards is the requirement enshrined in the Holy Qur’an requiring the payment of Zakat (Lewis & Algaoud 2001, p. xii).

Sulaiman (2001) specified two essential principles underlying the concept of accountability in Islam; full disclosure and social accountability. She explained that from an Islamic perspective, the emphasis on social accountability would mean that financial reports should enable Muslims to determine Zakat liability. She added that there is a little support for the suggestion that Muslims ought to be provided with financial information of a different character from what is normally disclosed in Western-based accounting systems.

In terms of the number of Shariah principles followed by Islamic banks, Haron (1998) indicated that Islamic banks in many countries (especially Middle Eastern countries) operate with a minimum number of principles. Many additional principles have been introduced in countries such as Malaysia, Bangladesh, Pakistan and Iran. Haron (1998) mentioned that there are fourteen Shariah principles followed in Islamic banks in Malaysia and all these principles bear Arabic names.

Hassan (2008) stated that Islamic Banks are trying to adopt Basel-II but facing different kinds of impediments such as liquidity risk, a complex mechanism of profit and loss, product standardization, and the absence of Shariah-compliant short term instruments for the management of mismatched assets and liabilities. He argued that Islamic banks face a challenge in adopting IFRS and some of the risk models may expose Islamic banks to other risks that are not apparent for conventional banks.

2.7 Compliance with AAOIFI accounting standards by Islamic banks and Fatwa and Shariah Supervisory Board

Another line of research, the sixth category of studies reviewed in this chapter, assesses the AAOIFI accounting standards and Fatwa and Shariah Supervisory Board. AAOIFI’s
framework is generating debate and discussion in the Islamic world. AAOIFI’s standards try to legitimize Islamic banking operations to the Muslim public (El-Gamal 2006; Kuran 2004). In earlier times banks used to take advice from in-house Shariah consultants. These consultants also provided necessary guidance to ensure banks are compliant with the Shariah law. Globalization and an increased demand for integration of the Islamic economy with the world economy led to the formation of the Accounting and Auditing Organization of Islamic Financial Institutions. Experienced professionals, scholars and bankers combined to form this regulatory authority. Vinnicombe (2013) provides an insight into the compliance of Bahraini banks with accounting standards set by AAOIFI. Vinnicombe (2013) surveyed accountants regarding their ideas on the compliance of banks with accounting standards by AAOIFI, and found that compliance is higher for some Islamic issues than for others.

Rahman (2003) stated that in a Muslim society, accounting is expected to be influenced by the way the economic system is organized and the philosophy underpinning its system. He added that according to AAOIFI’s statement of financial accounting, the need for accounting objectives for Islamic financial institutions stemmed from the role of accounting. Rahman (2003) asserted that the role of financial accounting is to provide information which users of the financial statements of Islamic banks depend on in assessing the bank’s compliance with the precepts of Shariah.

Besar et al. (2009) examined whether there is any expectation of gaps between the standards issued by the AAOIFI and the actual Shariah review practice in those Islamic banks. They provided some recommendations for the improvement of Shariah review practised in Malaysia. Besar et al. (2009) concluded that the Shariah committee report issued by the committees of Islamic banks in Malaysia is only satisfying the minimum requirement for such a report as has been provided by Bank Negara Malaysia. They added that it needs more development and disclosure to provide a deeper assurance to the stakeholders regarding the Shariah compliance of the institution. Moving towards a more transparent disclosure would require more proactive involvement of the regulators as it seems that the respective institutions will only follow the minimum requirement as provided by the regulators.

There was a debate whether financial reporting affects the Shariah validity of the financial transaction or not. Some researchers considered the financial reporting as a recording function that does not affect the permissibility of a transaction. Deloitte & Touche (2012) stated that it is simply an endorsement of the banks’ Shariah compliance in general without any emphasis
on the actual operations or conduct of the respective banks. The strong commitment from the Fatwa and Shariah Supervisory Boards and management is required to improve Enterprise Risk Management (ERM) in Islamic Finance. It is the responsibility of the bank’s executive management and Board of Directors to ensure that the bank operates in accordance with the principles and rulings of the Islamic Shariah (Deloitte & Touche 2012).

According to ADIB (2010), Fatwa and Shariah Supervisory Board has the right to submit written objections to the Board of Directors with respect to any of the bank’s activities which it considers to be not complying with any of the principles and rulings of the Islamic Shariah. In addition, it reviews all forms of contracts and agreements relating to any of the bank’s business to ensure their compliance with Islamic principles.

Che Pa (2006) commented that the Fatwa and Shariah Supervisory Board has played a significant role in ensuring that Islamic banks strictly comply with the Shariah law. Che Pa (2006) investigated the Sukuk and the acceptability of the AAOIFI FAS 17 investment in Sukuk products among bank managers in Malaysia. The study found that AAOIFI FAS 17 is well accepted by the Malaysian bank managers and may be considered applicable in Malaysia even though they have not referred to the AAOIFI standards. However, he indicated that Malaysian bank managers who are involved directly in investment in Islamic bonds have relatively moderate levels of understanding of the AAOIFI FAS 17.

Also, El-Gamal (2006) pointed out that the Fatwa and Shariah Supervisory Board in the Islamic banks has played a significant role in ensuring that Islamic banks strictly comply with the Shariah law, and their statements in Islamic banks’ annual reports are addressed to see if these comply with Shariah principles and are considered as an important legitimizing tool.

However, the Fatwa and Shariah Supervisory Board’s responsibility is limited to expressing an independent opinion based on its review of the bank’s operations and to prepare a concise report for the bank (Deloitte & Touche 2012). This report is important in ensuring the bank’s compliance with Shariah. But, the report issued by the Fatwa & Shariah Supervisory Board doesn’t review all applications of Islamic banks (Deloitte & Touche 2012).

While other researchers emphasized that there is a connection between Shariah validity and accounting recording. Lewis (2001) argued that all factual and true information, as well as information which presents the institution in an unfavorable light, needs to be disclosed according to Shariah principles. Shariah plays a main part in Islamic finance and according to
Islamic scholars; *Shariah* has formulated comprehensive ethics governing how business should be run, how accounting ought to be undertaken and how banking and finance is to be arranged (Khan et al. 2011).

Ainley (2007) believed that creditors and investors were the most frequent users of financial reports. This was one of the key objectives being targeted by IFRS is to improve financial reports to be most useful for decision making by creditors and investors. However, in accordance with the Islamic framework of accountability, this did not apply in Muslim societies as each and every single user comprising the society is supposed to be considered, and hence it is relevant that there must be disclosure of information to the society as a whole (Lewis 2001). Additionally, all factual and true information, as well as information which presents the institution in an unfavourable light, needs to be disclosed according to *Shariah* principles (Lewis 2001).

Pomeranz (1997) and Shadia (2007) examined the problems of compliance the Islamic Financial Institutions (IFIs) with *Shariah* principles and the need for different accounting standards to be implemented by IFIs. Pomeranz’s (1997) paper covered auditing and the formation of accounting standards. He pointed out that it could probably solve the problem of compliance of Islamic banks with AAOIFI accounting standards or Islamic and Arab social and religious objectives.

Karim (2001) suggested that the perspective adopted by the supervisory authorities to regulate Islamic banking tended to influence the accounting treatment of investment accounts adopted by Islamic banks, although most of the countries in which these banks operate either look directly to IFRS as their national standards, or else develop national standards based primarily on IFRS. This has rendered the financial statements of Islamic banks non-comparable. Karim (2001) also emphasized the need to implement the accounting standards promulgated by the AAOIFI. According to Karim (2001, p. 173), ‘AAOIFI’s pronouncements are intended to serve Islamic banks in the various countries in which they operate’. He added that,

Islamic banks should be asked to implement AAOIFI’s standards, as is currently the case in some countries. This would render the financial statements of these banks comparable because AAOIFI’s standards are specifically developed to cater for the unique characteristics of the *Shariah* contracts that govern the Islamic banks’ financial instruments. (Karim 2001, p. 174)
Islamic banking literature represents studies from emerging markets and less developed countries. Few studies in this area cover comparisons between AAOIFI and the *Fatwa* and *Shariah* Supervisory Board in many countries perhaps due to the limitations that are associated with information accessibility. Vinnicombe and Park (2007) indicated that moving towards the international harmonization of accounting standards has coincided with the development of Islamic financial institutions and accompanying accounting standards. They concluded that a brief comparative overview of provisions and contingent liabilities in conventional western accounting standards versus those published by the AAOIFI, may be insufficient to draw firm conclusions regarding the implications of Islamic accounting for international accounting harmonization. Vinnicombe and Park (2007) were of the opinion that the pragmatic approach of the AAOIFI is based on its efficiency in that work already commenced by western and other accounting bodies was used, and this minimized the time and costs associated with the development of *Shariah*-compliant accounting standards.

In their study, Vinnicombe and Park (2007) examined liabilities and contingent liabilities. They found that there are clear differences in the requirements for measurement, recognition and presentation between the AAOIFI standards and the IFRS, and noted that there may be some practical difficulties arising from different underlying beliefs and requirements compared with conventional western arrangements. They added that these differences may result in the process of adaptation actually leading to quite different standards, in order to achieve *Shariah* compliance.

Vinnicombe and Park (2007) also suggested that further studies need to provide a more comprehensive comparative analysis of the standards issued by the AAOIFI relative to standards for similar matters issued by the IASB. This is necessary to better understand whether in modifying conventional standards to meet the requirements of Islamic jurisprudence, the subsequent standards will differ substantially from their original format and purpose. They also recommended studying the AAOIFI standards in order to see if there is actually any reason to believe standards developed on the differing bases would differ substantially in reality.

#### 2.8 Critique of Islamic banking and AAOIFI standards

The limitations of Islamic banking have been identified by several authors. Bokhari (2007) indicated that Islamic banking is facing various challenges and difficulties in which the main
and significant challenge is the lack of skilled and trained professionals to fulfil the requirements of this fast growing industry. Iqbal (1997) also tried to address the issues and challenges affecting Islamic banking, arguing that western accounting procedures are not adequate because of the different nature and treatment of Islamic financial instruments. Different procedures and standards are required for information disclosure, investors’ confidence, monitoring and surveillance. Proper standards will also help the integration of Islamic financial markets with international markets.

On the other hand, Kuran (2004) criticized Islamic banks. He claimed that they failed to employ profit and loss sharing techniques due to their lack of experience in finding the right investment opportunities, so they may end up with more losses than profits. He added that Islamic banks give priority to long-term investments over short-term investments and they do not offer opportunities of the cash poor investments. Kuran (2004) also stated that Islamic banks were the same as conventional banks and the only difference between them is in appearance. Both do not focus on social dimensions and they are paying very little attention to non-financial considerations such as health investments.

Kuran (2004) also, criticized AAOIFI’s standards, stating that AAOIFI harmonized their standards with western accounting bodies, mainly focusing on financial operations related to interest prohibition and Zakat calculation, and promoted Islamic banking products and activities.

Arguing along similar lines, Maurer (2002) claimed the objectives of the AAOIFI standards are the same as any other standards issued by international or local accounting bodies. AAOIFI’s standards have relied on standards issued by western and international accounting bodies especially the International Accounting Standards Committee (IASC). Maurer (2002) claimed that AAOIFI standards take the spirit of the dominant capitalism and market ideology and failed to suitably find a substitute culture of accounting complying with both Islamic values and modern culture.

El-Gamal (2006) described Islamic banking in practical terms as replicating conventional banking. He argued that Islamic finance is not built from classical jurisprudence; rather, it is a modification of conventional practice where that practice is deemed forbidden. Saleem (2007) claimed that Islamic banks need to move away from the misleading modes of financing they currently use and step towards the Western style. He claimed that this has two advantages:
first, the principles of Islamic banking favouring profit and loss sharing over interest are very similar to the financing techniques; second, the banks can support in promoting innovation and the creation of new jobs and industries by providing money to entrepreneurs with smart ideas.

This issue is also raised by Wilson (2007), who recognized that the market for investment banking is highly competitive and the top European investment banks have much expertise and more assets than organizations such as the European Islamic Investment Bank. On the other hand, Wilson (2007) added that several leading European investment banks have supplied the services of Shariah advisors, or appointed Shariah boards, so that they can compete for investment banking opportunities in the countries of the Gulf Cooperation Council (GCC) which involves Muslims clients and institutions concerned with Shariah compliance (Wilson 2007).

In another study, the same author claimed that the main reason some Western institutions are not involved in Islamic banking is the complexity of Islamic finance, and a lack of understanding (Wilson 1999). He said that even though some financial institutions such as HSBC and Goldman Sachs have become interested in Islamic finance, there appear to be significant barriers to new entrants. Wilson (1999) illustrated that the most significant barrier is the steep learning curve, as it does not merely require an understanding of the technicalities and legal concepts underlying the Islamic financing instruments, but requires a real appreciation of the diverse Muslim cultures and a respect for Islam.

2.9 Summary

To summarize, this literature review has examined the theories, models, strategies and processes regarding Islamic Banking. Studies were reviewed to identify differences between Islamic banks and traditional banks. Many authors compared AAOIFI accounting and IFRS. The literature also discussed Islamic Accounting Standards and explained the differences between these standards and International Financial Reporting Standards (IFRS). Some authors tried to identify the need for accounting standards for Islamic financial institutions. Other authors tried to explain the objectives, characteristics, ethics and social responsibilities of Islamic accounting. Some authors have tried to criticize Islamic banking and AAOIFI Accounting Standards.
However, in the different studies mentioned above, no researcher has yet surveyed or interviewed Islamic banking managers in the UAE to identify influences of the AAOIFI accounting standards on Islamic banks. This research study aims to fill this gap in knowledge in this area.
Chapter 3 – Background of this Research Study

3.1 Introduction

This research deals with the accounting standards adopted by Islamic banks in the United Arab Emirates (UAE). This chapter explores the background of the currently adopted International Financial Reporting Standards (IFRS) and the potential adoption of Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) accounting standards by Islamic banks in the UAE. The discussion in the first section of this chapter provides a brief discussion about the accounting standards foundation in the UAE. The second section of this chapter discusses the background of the IFRS and involves the historical development of IFRS around the world for the periods of the 1960s, 1970s, 1980s, 1990s and 2000s. This is followed by a discussion of the application of IFRS in the Islamic countries and the application of the Fatwa and Shariah supervisory board among the adoption of IFRS in the Islamic banks. Finally, the third section of this chapter focuses on the background of the AAOIFI, and explores its framework, structure and objectives. This is followed by discussions of the history of the development of Islamic accounting standards, primary reasons behind the launching of Islamic accounting standards issued by the AAOIFI, key parties involved in the preparation of AAOIFI accounting standards, the problems with the AAOIFI accounting standards and the proposed solutions to the problems.

3.2 Accounting standards foundation in the UAE

The UAE is one of the most progressive countries in the world. The UAE houses the world’s seventh largest oil resources and also has huge reserves of natural gases, again ranked as the seventh-largest (IMF 2012b). Due to these vast reserves of natural resources and sophisticated industrial infrastructure, the UAE is one of the most developed countries in Western Asia. The per capita income of UAE is above the regional average and currently stands at a significant amount of US$48,158 (IMF 2012b).

The UAE has a host of Islamic banks and the country boasts an extensive banking network. It is important to know that Islamic banks are now operating in a number of countries in South-East Asia, Africa and the Middle-East. However, they are facing difficulties in coping with unique accounting standards due to the lack of a sophisticated legal framework and inconsistency of financial reporting. Even the UAE has its own share of concerns.
The UAE does not have an accounting law, nor does it legally mandate accounting standards (IFRS Foundation 2013). The International Monetary Fund (IMF) recommended that the UAE endorse an accounting law that would adopt IFRS for public companies and introduce national accounting standards for other companies (Solé 2007). The companies law in the UAE sets forth that accounting principles and practices should be in line with the generally accepted practices and principles of accounting. In practice, companies in the UAE generally follow the IFRS. For instance, companies listed on the Abu Dhabi securities exchange are required to apply IFRS, but there are no specific guidelines as to their application (IFRS Foundation 2013). Whereas, the listing rules of the Dubai international financial exchange (NASDAQ Dubai) require listed companies to prepare IFRS financial statements. However, the listing rules of the Dubai Financial Market PJSC do not nominate a specific accounting framework to be used in the financial statements of listed companies. Therefore, IFRS are permitted and are used by most listed companies and some financial institutions use financial Accounting Standards issued by the AAOIFI. All other regulatory bodies require IFRS adoption except for certain government bodies (IFRS Foundation 2013). The AAOIFI standards are now adopted in the Dubai International Financial Centre (DIFC) (AAOIFI n.d.(e)).

Research from the IMF indicates that Islamic banking appears to be complementary to conventional banks, rather than being a substitute (Imam & Kpodar 2010). The central bank has made it mandatory for all commercial banks in the UAE to prepare their accounts according to International Accounting Standards Board (IASB) (Essays, UK 2013). According to circular No. 20/99 issued by the central bank, financial institutions and investment companies in the UAE are required to prepare their financial statements in accordance with IFRS with effect from 1 January 1999 (Essays, UK 2013).

The central bank of The UAE was formed in 1980 and replaced the currency board which was set up in 1973 (Essays, UK 2013). The establishment of the central bank was to bring about control and discipline to the banking sector in the UAE and to provide greater control of national and foreign banks operating within the country in addition to regulating various financial institutions. Article 5 of law No. 10 of 1980, as outlined in (Appendix 2), provides that the central bank of the UAE will direct monetary, credit and banking policy and supervise its implementation in accordance with the country’s general policy and in such ways as to help support the national economy and the stability of the currency.
Article 1 of the UAE federal law No. 6 of 1985, as outlined in (Appendix 2), defines Islamic banks, financial institutions and investment companies as “those companies whose Articles and Memorandum of Association include an obligation to apply the Islamic Shariah Law and that their operations would be conducted pursuant to Islamic Shariah Law”. The Fatwa and Shariah Supervisory Board of the Ministry of Religious Endowments centrally regulates the Islamic banks in the UAE. Higher Shariah Authority in the UAE supervises Islamic banks, financial institutions and investment companies (Art. 5, Federal Law No. 6 of 1985). This Authority is given the final authority in Shariah matters in Islamic banking and finance and the formation of Shariah supervision authority at the financial institution level in the UAE (Art. 6, Federal Law No. 6 of 1985).

3.3 Background of international financial reporting standards (IFRS)

Accounting is the language of business, while the accounting standards are the set of rules to guide accounting practices in the corporate world, and the trend is now towards the adoption of IFRS (Bhattacharjee & Islam 2009). The IFRS are issued have guidelines on issues of presentation of financial statements, inventories, cash flow statement, income taxes, consolidated and separated financial statements, earnings per share, intangible assets, impairment of assets, share-based payments, insurance contracts, financial instruments and financial instrument disclosure amongst others (IFRS 2011). There has been a movement in the accounting world to systematically apply IFRS due to the increasing globalization of markets and economies. The need for the adoption of IFRS arose due to different accounting standards applied by different companies in different countries which made a comparative analysis of the accounting information almost impossible (Haskins, Ferris & Selling 1996).

The widespread adoption of IFRS will increase understandability of financial statements, save time and money, ease interpretation and improve the credibility of the financial reporting process and profession (Choi & Mueller 1992). But the domain of international accounting standard-setting is dominated by the Anglo-American model. Some of the IFRS do not reflect Islamic practices particularly in regard to interest transactions (Bhattacharjee & Islam 2009).

The International Accounting Standards Board (IASB) is the independent standard-setting body of the IFRS. Foundation based in London, UK (IFRS 2011). Before the establishment of the IASB, international standards were issued by the IASB’s predecessor organization, the International Accounting Standards Committee (IASC), a body established in 1973 through
an agreement made by professional accountancy bodies from Australia, Canada, France, Germany, Japan, Mexico, Netherlands, United Kingdom, Ireland and the United States of America (Bhattacharjee & Islam 2009). The need for the IFRS arose when globalization of business evolved and companies started opening businesses in other countries (Mechell 2009).

The most commonly known set of principles are Generally Accepted Accounting Principles (GAAP) (Mechell 2009). The GAAP are guidelines for the preparation of financial reports such as the organization’s balance sheet, income statement and cash flow statement. The GAAP incorporates many principles (such as historical cost accounting, materiality, principle of prudence, etc.) which are applied in many countries such as the United Kingdom (UK), Australia and the United States (US) (Mechell 2009).

### 3.3.1 Conceptual framework of IFRS

A background of the framework of the IASB is necessary to understand and compare the AAOIFI accounting standards and IFRS. The IASB is an independent and self-regulatory body, adopted a framework in 2001 to serve as a guide to the board in developing accounting standards. The main purposes of IASB’s framework are as follows (Cellucci 2010):

- The IASB formulates and publishes accounting standards for the presentation of financial information and defining the objectives of financial statements, and is also responsible for promotion these accounting standards around the world.
- The IASB undertakes continuous improvement of the accounting standards and identifying characteristics which are related to the presentation of financial information and financial statements for companies worldwide.
- The IASB does not have the power to enforce its standards on countries or companies but IASB provides concepts of capital maintenance.

The IASB defines the basic elements to ensure high quality and the universal acceptability of financial statements. There are around 154 professional accounting bodies in 112 countries who were members of the IASB in September 2002 (Mustafa 2003).

The IASB developed a framework for the preparation and representation of financial statements (Sheikh & Kartio 2006). This framework is known as the conceptual framework. The basis of the framework is to provide general guidelines for accounting practices. The
framework includes the objectives of financial statements, recognition criteria and the qualitative characteristics which are parts of this framework, namely relevance, understandability, comparability and reliability (FASB n.d.).

### 3.3.2 History of the development of IFRS

In the past few decades, the accounting profession has been facing the demands of globalization and increasingly looking for a way to present financial statements using a single set of accounting standards which can be understood by the entire business community (Bae, Tan & Welker 2008).

This section divided the historical development of IFRS into four parts:

- The period of the 1960s when the requirement for the international accounting standard harmonization was recognized.
- The period of the 1970s to 1980s during which an international body named the International Accounting Standards Committee (IASC) started working on the harmonization process.
- The period of the 1990s when formalization and expansion of the international activities of IASB took place.
- The period of the 2000s when IFRS convergence gained speed. Many big capital market countries have accepted the IFRS. A detailed discussion of these historical developments is provided below.

### 3.3.2.1 Development of international accounting standards in the 1960s – need for harmonization of international accounting standards

The harmonization of international accounting standards is defined as “the process of bringing International Accounting Standards (IAS) into some sort of agreement so that the financial statements from different countries are prepared according to a common set of principles of measurement and disclosure” (Haskins, Ferris & Selling 1996, p.29). Harmonization of accounting standards was not easy because many developing and developed economies faced problems in accepting the IAS. Islamic countries faced problems in applying these accounting standards (Bhattacharjee & Islam 2009). This is mainly because the international accounting standards are based on the GAAP of western countries such as the UK and Australia (Bhattacharjee & Islam 2009). Countries which have adopted the IAS mainly include
Australia, Canada, European Union, Japan, India, Russia, Pakistan, Singapore and South Africa (FASB n.d.).

The need for harmonization of accounting standards started after World War II in the 1950s. After World War II the emergence of economic integration led to cross-border capital flows (FASB n.d.). International financial transactions required common accounting standards so that investors across the world could easily compare the financial performance of companies in different countries to make informed investment decisions (Shil, Das & Pramanik 2009). Initially the main focus of the harmonization of accounting standards was commonality between the accounting principles used in many countries which were involved in international business (Shil, Das & Pramanik 2009). The World Bank and the IMF are tying their loans to the use of IAS. They also agreed with the Big Four accounting firms (Deloitte & Touche, Ernst & Young, KPMG Peat Marwick and PricewaterhouseCoopers) that international accounting standards are the standards that should be used by financial institutions in the countries in which the World Bank and IMF are intending to foster economic stability (Gillis 2011).

The 1960s was the period when the need for harmonization of accounting standards was recognized due to the cross-border capital flow. Some early steps were taken at this time (FASB n.d.). The Eighth World Congress of Accountants was hosted by the American Institute of Certified Public Accountants (AICPA) in 1962 in which many participating members urged the harmonization of international accounting standards. As a result of the Congress, AICPA reviewed accounting standards internationally in 1964 (FASB n.d.). A group was formed to study the differences between the accounting standards of main capital market economies. This group included AICPA and its counterparts in Canada and the UK. After a study of almost 10 years the group published a book on international accounting in 1967, titled ‘International accounting standards in Europe: a comparative study’ authored by Professor G.G. Mueller (Alves & Antunes 2011).

### 3.3.2.2 Development of international accounting standards in the 1970s and 1980s

In 1973, an international body, the IASC was established, with the objective being to develop common, clear and understandable accounting standards for all countries (FASB n.d.). IASC became the first international organization for accounting standards setting, and was the main body which played an important role in the harmonization of the accounting standards.
The international institutions such as the United Nations, World Bank, European Union, Organization of Economic Cooperation and Development, and the Basle Committee supported the IASC as the only credible world harmonizer of accounting standards (Nobes 1996).

In 1979, the Financial Accounting Standards Board (FASB) formed the first task force which included representatives from the international accounting standard setters. The main representatives included the UK accounting standard board, the accounting standard board of Canada, and the IASC. The objective of this task force was to revise the accounting standards on foreign currency (FASB n.d.). This trend of accounting standard harmonization was also followed in the 1980s. The IASC issued 25 accounting standards in 1987, which covered various accounting topics. The IASC decided to improve the standards by undertaking a comparability and improvement project (FASB n.d.).

### 3.3.2.3 Development of international accounting standards in the 1990s

Harmonization is also sometimes referred to as “convergence” of accounting standards. In the early 1990s the objective of harmonization was changed to convergence (FASB n.d.). The concept of ‘convergence’ refers to the application of one common set of accounting principles which would be of a high quality, understandable and acceptable by most of the major capital markets of the world (Cellucci 2010).

FASB and the Accounting Standards Board (Canada) undertook a joint project in 1993 on segment reporting. This project resulted in an improved set of segment reporting standards. In the same year, a group of four members was formed to work further on the convergence process (FASB n.d.). This group of four members was known as the ‘G4’, including the FASB, the Accounting Standards Board (Canada), and relevant bodies representing the United Kingdom and Australia (FASB n.d.). Later New Zealand also joined the group and it was renamed the ‘G4 + 1’. In this effort IASC acted as an observer (FASB n.d.). In the next year, both the IASC and FASB undertook their first collaborative action. They worked on the accounting standard of earnings per share and narrowed the differences between them. In 1995, the FASB took the initiative to compare the US GAAP and IASC accounting standards (Harris & Mueller 1999).

In the meantime, the International Organisation of Securities Commissions (IOSCO) undertook that if the core set of standards were acceptable then it would support the IASC’s
standards (Zeff 2012). In 1998, the international accounting convergence process received a boost due to the financial crisis in the Asian Countries. The IMF, World Bank, G7 ministers and other countries called for rapid completion of the accounting convergence process. They asked for the global adoption of common accounting standards (Zeff 2012).

3.3.2.4 Development of international accounting standards in the 2000s

The 2000s have been the most important period for the international convergence of accounting standards. The IASC became IASB in April 2001, committed to making common accounting standards that can be accepted globally, are understandable and of high quality to improve its governance, funding and independence of the IASC (Moussa 2010). The IASB issued IFRS, which brought rapid changes in the use of accounting standards by major capital market countries (FASB n.d.). Since 2001, more than 100 countries in the world have now accepted the IFRS developed by IASB (FASB n.d.).

At the time of the establishment of the IASB there were 14 board members (Zeff 2012). Just one year after the formation of the IASB a major decision was taken by the members of the European Union to use the IFRS. Only a few countries had decided to apply the accounting standards established by IASC until 2002 (Zeff 2012). Many of these countries had to discard their own accounting principles to follow the principles set by IASC. Another important step was taken by the authorities in 2002 was issued a Memorandum of Understanding (MoU) which is known as the Norwalk Agreement. In this agreement IASB and FASB decided to collaborate for improvement and convergence of the US GAAP and IFRS (Zeff 2012).

In 2006, another MoU was issued by the FASB and the IASB. In this MoU FASB and IASB described the goals that they decided to achieve in the international accounting convergence by 2008 (Zeff 2012). In 2007, the United States Securities and Exchange Commission (SEC) proposed and eliminated the reconciliation requirements and also published the concept release in which it focused on possible optional use of IFRS by issuers in the US (FASB n.d.). The FASB and the IASB also issued the converged standards on business combination. In 2008, the MoU was updated (Zeff 2012). In the same year, a roadmap was issued by the SEC for adoption of the IFRS by the US. Two years after the update of the MoU, the SEC issued a statement in support of the global convergence of accounting standards (Zeff 2012). The convergence process proceeded and in 2011 the IASB and FASB published a progress report on the convergence work (FASB n.d.).
From 2002 to 2013, the path toward convergence has been the collaborative efforts of the Financial Accounting Standard Board (FASB) and the IASB, both working together to converge the Generally Accepted Accounting Principles (GAAP) of the US and IFRS (Zeff 2012). In 2009, Japan and China also started working on the convergence of their accounting standards with the IFRS standards (FASB n.d.).

3.3.3 Application of IFRS in the Islamic countries around the world

The adoption of accounting standards by a country depends on many factors such as the culture, legal system, taxation, business organizations, accounting profession and ownership in the country (Askary 2006). Some international standard setters argued that cultural and economic differences from country to country will not affect the accounting standards for similar business activities in large organizations (Carsberg 1995). It has also been argued that the accounting issues in the international field are not basically different from those in national fields (Wyatt 1992).

The financial institutions of Islamic countries are represented by the Islamic Financial Services Board (IFSB) and AAOIFI. IFSB deals with the financial issues and AAOIFI deals with issues of accounting standards in Islamic nations. These institutions are represented in international organizations such as the Standard Advisory Council (SAC) in its review and the merging efforts of the IFRS; the IASB has to consider the accounting policies and practices in the Islamic countries (Bhimani 2008).

Some environmental factors are unique in the Islamic countries. Islam has the potential to extend a cultural influence in the quest for the international harmonization of accounting (Hamid, Craig & Clarke 1993). It is generally understood that Islamic banking started to impact after the boom in the oil prices in 1973–1974 (Moore 1997). Besides cultural factors, economic factors are also important in the development of the IAS for the Islamic countries. Islam considers economy as a matter of morality and is subject to the principles of the Shariah. The economic contribution of the Islamic countries to the world Gross Domestic Product (GDP) is very significant. Economic growth of the Islamic countries in the Middle East is high and will increase further in the future. In its latest assessment the IMF stated that the region’s oil exporters were expected to post solid growth in 2012 and most of the region’s oil-exporting countries were growing at healthy rates. GDP growth in the oil exporting
countries of the Middle East and North African region is expected to rise to about 6½% in 2012 (International Monetary Fund 2012a).

These factors enable the Islamic countries in this region to be represented as an important group in the development of IFRS by IASB. The stock market is also growing in these Islamic countries, with Saudi Arabia having the largest listed foreign stock market in the Middle Eastern countries with a market capitalization of around US$325 billion (International Market Advisor 2015). The growing economic importance of the Islamic countries requires consideration of the interests of this group in the IASB standardization of the IAS (International Market Advisor 2015).

There are many differences in the accounting standards set by IASB and AAOIFI. The accounting standards in the Islamic countries are a reflection of the different financial instruments, insurance, contracts, interest laws, ethical standards, and types of business organizations in the Islamic countries (El-Razik 2009). These accounting standards differ from the IAS mainly with regard to leases, restricted contracts, and specialty investment accounts areas (El-Razik 2009). If these issues are addressed by the IASB then it will help improve the IAS convergence of standards in the Islamic countries (Shadia 2007).

Islamic countries are facing challenges in the implementation of IFRS as it will replace their own accounting standards and they are concerned that they have to abandon their particular issues. They perceive a threat that they will lose control over the standard-setting process. The Islamic countries are also facing the problem of unavailability of high quality IFRS auditors who can represent the issues of Islamic countries in IASB’s meetings. To get better accounting standards and apply them all over the world, the IASB needs to consider the interests and issues of Islamic countries (Dore 2007).

Islamic countries are still facing problems with the implementation of the IFRS. The reason behind this is the set of issues which are of particular concern of the Islamic countries. These factors mainly include taxation laws, ethical standards, business ownership and disclosure of accounting information (Dore 2007). The increasing importance of the Islamic countries in the world economy and its contribution to international trade has required the IASB to consider factors which affect Islamic countries, while implementing convergence of the IFRS (Hossain 2003).
3.3.4 Role of the Fatwa and Shariah Supervisory Board among the adoption of IFRS

The consolidated financial statements of Islamic banks in the UAE are currently prepared in accordance with IFRS, general principles of the Shariah as determined by the Fatwa and Shariah Supervisory Board and applicable requirements of the UAE Federal Law No. 8 of 1984.

According to the Abu Dhabi Islamic Bank ‘Annual Report’ (2010), the Fatwa and Shariah Supervisory Board, whose members are not Board Directors of the Islamic bank, has a term of three years and all members are required to form a quorum, whether by principal or by proxy. It has the following mandate (ADIB 2010):

a) It issues Fatwas (Islamic religious rules) pertaining to the bank’s activities at the request of the bank’s executive management or Board of Directors. It also supervises and controls the validity of the bank’s activities to ensure that they comply with principles and rulings of the Islamic Shariah, and provides its recommendations.

b) It has the right to submit written objections to the Board of Directors with respect to any of the bank’s activities which it considers to be not complying with any of the principles and rulings of the Islamic Shariah. In addition, it reviews all forms of contracts and agreements relating to any of the bank’s business to ensure their compliance with Islamic principles.

c) It has the right to review, at any time, the bank’s books, records and documents, and request any information it may deem necessary. In the event of its inability to discharge its duties, it will report this formally to the Board of Directors.

It is the responsibility of the bank’s executive management and Board of Directors to ensure that the bank operates in accordance with the principles and rulings of the Islamic Shariah (Deloitte & Touche 2012). The Fatwa and Shariah Supervisory Board’s responsibility is limited to expressing an independent opinion based on its review of the bank’s operations and to prepare a concise report for the bank. This report is important in ensuring the bank’s compliance with Shariah. But, the report issued by the Fatwa & Shariah Supervisory Board doesn’t review all applications of Islamic banks in the UAE. It is simply an endorsement of the banks’ Shariah compliance in general without any emphasis on the actual operations or conduct of the respective banks. The strong commitment from the Fatwa and Shariah
Supervisory Boards and management is required to improve Enterprise Risk Management (ERM) in Islamic Finance (Deloitte & Touche 2012).

3.4 Background of Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)

As mentioned earlier, the financial statements of the Islamic banks in the UAE currently must be presented in accordance with IFRS. The UAE Islamic Banks need to apply Islamic accounting standards because of their different nature, activities and functions from conventional banks (Karim 2001). In addition, the differences arising between the two types of banking systems, the Islamic and the conventional, are due to differences in business environments, the economic system, culture and the development stage of a country’s economy, which affects the type of accounting standards required (Karim 2001).

Islamic financial institutions are required to use the system of accounting standards which is mandated by the financial services regulator of the country in which they are based. Accordingly, Islamic financial institutions based in the USA must use FASB accounting standards, while almost everywhere else they account under IFRS. The following table shows the applications of accounting standards by the Islamic institutions in different countries of the Gulf Cooperation Council (GCC) (Amin 2011).

<table>
<thead>
<tr>
<th>Country</th>
<th>Islamic financial institutions</th>
<th>Accounting standards used</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kuwait</td>
<td>Kuwait Finance House KSC</td>
<td>IFRS</td>
</tr>
<tr>
<td>Bahrain</td>
<td>Al Salam Bank-Bahrain BSC</td>
<td>AAOIFI</td>
</tr>
<tr>
<td>Qatar</td>
<td>Qatar Islamic Bank SAQ</td>
<td>AAOIFI</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>Al Rajhi Banking and Investment Corporation</td>
<td>IFRS</td>
</tr>
<tr>
<td>Dubai-UAE</td>
<td>Dubai Islamic Bank PJSC</td>
<td>IFRS</td>
</tr>
<tr>
<td>Abu Dhabi-UAE</td>
<td>Abu Dhabi Islamic Bank PJSC</td>
<td>IFRS</td>
</tr>
</tbody>
</table>

AAOIFI accounting standards are used by only two countries in the GCC, Bahrain and Qatar. All other GCC countries use IFRS. The standards set up by the AAOIFI have become the core component of the re-engineering of Islamic finance. The AAOIFI attempts to come up with a conceptual framework for Islamic accounting or accounting for Islamic financial institutions, which comprises qualitative characteristics and elements of financial statements, is much like the IASB’s framework (Amin 2011).
The AAOIFI is an international organization which sets standards for Islamic financial institutions and banks. This organization was set up in 1991 for Islamic financial institutions which were established under an agreement of association. This agreement of association was signed by the Islamic financial institutions on 26 February 1990 in Algiers. This agreement of association was registered on 27 March 1991 in the state of Bahrain (AAOIFI n.d. (e)). AAOIFI’s standards have been adopted in the Kingdom of Bahrain, Dubai International Financial Centre, Jordan, Lebanon, Qatar, Sudan and Syria; such adoptions supported the implementation of AAOIFI’s standards (AAOIFI n.d (b)).

Islamic investors frequently require additional information which is not mandated by IFRS, such as the amount of Zakat on which they should pay in respect of their shares. In most cases Islamic financial institutions are likely to provide this information voluntarily. For example, the UK’s European Islamic Investment Bank provided a figure computed using AAOIFI’s standards in its 2009 accounts (Amin 2011). In particular, the United Kingdom has become the leading non-Muslim Islamic finance centre after introducing regulatory changes, including changes to the taxation of Islamic finance products (Sadiq & Black 2012).

Also, some relevant authorities in different countries such as Australia, Indonesia, Malaysia, Pakistan, Kingdom of Saudi Arabia, and South Africa have issued guidelines based on AAOIFI’s standards and pronouncements which include accounting, auditing, governance, ethics and Shariah-compliance (Ullah 2013). International financial institutions have some liberty when implementing the opinions of their Shariah advisors, and the advice itself can be different between advisors. In this context, Austrade’s (2010) publication on Islamic finance and the government’s growing interest in accommodating Islamic financial products and services in Australia, recommended that interpretation by individual scholars will always play a role and the AAOIFI will help guide rule standardization and convergence (Austrade 2010).

The AAOIFI establishes, prepares and issues accounting standards according to Shariah and their exposure drafts and composition with the help of a system which has a due process and uses the expert knowledge of the industry’s practitioners (Ahmed 1994). The AAOIFI is an Islamic non-profit organization. It develops accounting standards, governance standards, auditing standards and ethics standards. It is regarded as an independent international organization (Deloitte n.d.). The AAOIFI has been supported by many institutional members, including 200 members from approximately 45 countries so far. The members list is inclusive of central banks, Islamic financial institutions, and it also includes other members such as
Islamic banks and Islamic financial institutions that are serving the public all around the world (AAOIFI n.d.(b)).

The AAOIFI provide training for Certified Islamic Professional Accountants (CIPA). The CIPA program covers technical subjects that are essential to equip candidates with the requisite technical understanding and professional skills in accountancy for international Islamic banks and financial institutions. The AAOIFI also provide training for Certified Shariah Advisors and Auditors (CSAA). The CSAA program covers technical subjects that are essential to equip candidates with the requisite technical understanding and professional skills in Shariah compliance and review processes for the international Islamic banking and finance industry. These programs are presented now by the AAOIFI in its efforts to enhance the industry’s human resources base and governance structures (AAOIFI n.d.(b)).

Today, AAOIFI is credited with a lot of responsibilities. Some of them being as follows (AAOIFI n.d. (b)):

a) Issuance of accounting governance and auditing authorities;

b) Implementation of Shariah principles in banking and financial operations of large Islamic institutions; and

c) Introduction of professional qualification programs such as CIPA, Shariah Adviser & Auditor ‘CSAA’ and the corporate compliance program in an effort to increase the industry’s human resource base and governance structures.

The AAOIFI’s standards now include 86 standards in total in the areas of accounting, auditing, ethics, governance and Shariah (AAOIFI n.d. (b)). The AAOIFI’s standards have emphasized that the Shariah committee is entrusted with the duty of directing, reviewing and supervising the activities of the Islamic financial institutions in order to ensure that they comply with Islamic Shariah rules and principles. Their role in financial accounting is to present the information which users of the financial statements of Islamic banks depend on to assess the bank’s compliance with the precepts of Shariah. Thus, in order for the Islamic financial institutions to perform their role successfully, accounting standards need to be developed and complied with by Islamic banks. The progress of such standards must be based on clear objectives of financial accounting and established upon definitions of its concepts (Abdul Rahman 2010). AAOIFI carries out these objectives in accordance with the Shariah
Law. This activity is intended both to enhance the confidence of users of the financial statements of Islamic financial institutions in the information that is produced about these institutions, and to encourage these users to invest or deposit their funds in Islamic financial institutions and to use their services (AAOIFI n.d (b)). The adoption of accounting standards depends on the nature of banks’ transactions as to where those standards are to be applied. In Islamic banking there are four functions which are: investment management, investment, financial services, and social services. Based on these functions, AAOIFI designs its standards which are also consistent with the Shariah Law (Al-Abdullatif 2007).

The Islamic accounting board has also published a number of accounting standards. The board not only publishes the accounting standards but also publishes the following (AAOIFI n.d. (b)):

- Auditing standards; there are five auditing standards which govern auditors’ conduct of their audits.
- Governance standards; in total there are seven governance standards available with the AAOIFI. The main aim of using governance standards is to enhance and intensify the security and sensitivity of accounting and financial reporting of the institutions.
- Ethics standards; there are only two ethics standards which are present in the ethics standards developed by the AAOIFI. Ethics are standards which are regarded as codes of conducts, including a code of ethics especially for accountants and auditors of IFIs, and a code of ethics for employees of Islamic financial institutions (IFIs).
- Shariah standards; to date the auditing and accounting organization for Islamic financial institutions has published and developed around 44 Shariah standards, as for example, Hawala (remittance), Kafalah (guarantee) and Mudharaba (profit sharing).

The AAOIFI has developed different Islamic accounting and other standards due to the existence of specific issues. The Islamic financial institutions face accounting and transactional problems that are unable to be satisfactorily dealt with using ongoing or current accounting practices in accordance with the prevailing conventional accounting standards (Cerf 1961). Accounting standards such as international financial reporting standards, and generally accepted accounting policies more specifically known as GAAP, are structured with Western commercial institutions in mind, dealing with their problems and solutions. In other words we can say that these liberal accounting standards and accounting policies are not able to be applied to Islamic financial transactions (Hidayat 2011). For example, transactions
conducted under *Shariah* are prohibited from carrying interest charges, though no such prohibition exists in conventional accounting standards and policies, giving rise to a significant accounting problem.

The standards for the AAOIFI have been created and developed in consultation with, and guided by, many well-known *Shariah* scholars, and has been accepted and implemented in several countries. Although the standards established by the AAOIFI are not binding on its members, over the last few years the organization has made significant progress in encouraging the widespread adoption of the standards (Hellriegel & Slocum 1974).

Moreover, IFRS have been implemented and adopted by various Islamic banks. However, the Islamic banks specific requirements were not met by the IFRS (Khan & Hussin 2013). As a result, in order to provide support to Islamic banking institutions, AAOIFI standards were developed. The Islamic banking system is considered to be very fragmented. It is believed and expected that with the development and creation of AAOIFI standards, these could easily promote convergence in *Shariah* standards leading to further growth in this nascent market (El-Din 2004).

### 3.4.1 Framework of the AAOIFI

The framework of the AAOIFI is displayed in the structure below. In this hierarchy there is a series of downward links from top-to-bottom with a corresponding downward flow of information.
Figure 3.1: Structure of the AAOIFI (AAOIFI (a))

3.4.2 Structure of the AAOIFI

1. **General assembly**: The general assembly consists of all those members who are founders, observers, associates, and supporters, the regulatory authority and the supervisory authority. The observers and supporting members are allowed to take part in the meetings conducted by the general assembly. The members observe and support and they can only attend the meeting but they do not have a right to vote in meetings they attend. The General Assembly is the peak authority and it convenes at least once a year (AAOIFI n.d. (d)).

2. **Board of trustees**: According to AAOIFI, there should be 20 positions on the Board of Trustees, including team members appointed by the general assembly (Dhaliwal 1982). The constituent membership of the Board of Trustees is appointed every five years. Selection of the members of the Board of Trustees depends on various factors including geographical representation and specific categories of members (AAOIFI n.d. (c)):
   - regulatory and supervisory authorities such as the reserve bank, authorities which have treasury departments such as money, and so on
• Islamic financial institutions
• financial statement users and financial institutions
• scholars of *Shariah Fiqh* (Islamic jurisprudence).
• firms which are engaged in auditing and accounting and are related to the Islamic financial institution

There are certain terms and conditions provided by the AAOIFI for the selection of members of the Board of Trustees (AAOIFI n.d. (c)). The selection of members must be conducted according to Article 12 of the AAOIFI. Article 12 states that if there is a vacant seat on the Board of Trustees it shall be filled by a vote in the General Assembly. The member being appointed must gain a majority of the votes in the General Assembly. The new member so appointed must be from the same category of membership as the person who had vacated the seat. The Article also states the term of the office to be served upon filling of any vacancy. Article 12 states that the period of office of the member who fills any vacancy will be the term remaining of the officer who vacated the seat. The Board of Trustees meets at least once in every year (AAOIFI n.d. (c)).

The following are the powers of the Board of Trustees (AAOIFI n.d. (c)):

• The Board of Trustees have the power to appoint members of the AAOIFI board and also to terminate that membership.
• The Board of Trustees has the responsibility for funding arrangements for the AAOIFI, and also the responsibility to dispose of these funds.
• The Board has the right to appoint two members of the Board of trustees to the executive committee of the AAOIFI.
• The Board of Trustees can also appoint the Secretary General.

The above stated list of powers which are granted to the Board of Trustees is not an exhaustive list. The Board of Trustees and any subcommittee which are included in the executive committee do not have any right or the authority to interfere with or to intervene in, either directly or indirectly, in the work of the AAOIFI. The Board of Trustees and its subcommittees cannot also influence the members of AAOIFI in any matter or in any manner (AAOIFI n.d. (c)).
3. **Accounting and Auditing Standard Board (AASB):** It is also known as the Standard Board. The AASB is constituted with 20 part-time members; these members are appointed by the Board of Trustees of the AAOIFI. The term of service of AASB members is five years. The members of the AASB represent various institutions and people such as Islamic financial institutions, regulatory bodies and supervisory bodies, *Shariah* boards, professors in universities, the organizations and firms that are responsible for the regulation of the accounting profession, or the auditing profession, or both. These members also include certified accountants, practicing accountants, and also the users of financial reports who use Islamic financial institutional outputs, or financial information which is related to the Islamic financial institution (AAOIFI n.d. (a)).

The following are the powers of the AASB (AAOIFI n.d. (a)):

- The main power of the AASB is to develop and publish accounting standards and auditing standards and guidelines for their usage in Islamic financial institutions. The AASB also publishes interpretations from time to time so that the relevant standards are understood and applied in the same sense as they were originally developed and issued.
- The AASB also prepares a code of ethics and educational standards, developed in accordance with the activities conducted, or will be conducted, by the Islamic financial institutes.
- The AASB has the power to review the standards of accounting and auditing. The review may be conducted with a view to making necessary additions, deletions or amendments or modifications as appropriate.
- AASB also has the power to set up the process for preparing standards, and the rules and regulations and the by-laws of the AASB.

The AASB meets at least twice each year and its resolutions are accepted or rejected by a majority of votes of the members (Hamoud 1996).

4. **Accounting standards committees:** The accounting standards committees comprise a chairperson, four members and a reporter (AAOIFI n.d. (a)).
5. **Auditing and governance standard committee**: The auditing and governance standard committee consists of one chairperson and seven members (AAOIFI n.d. (a)).

6. **The AAOIFI Shariah Board**: The constitution of the Shariah Board is effected by the Board of Trustees. It is constituted of a maximum twenty members and the term of service of the members of the Shariah Board is a maximum of four years. There are *Fiqh* scholars who are representatives of *Shariah* supervision boards in the Islamic financial institutions (Kahf 1994). These *fiqh* scholars are the members of the accounting and auditing organization representing Islamic financial institutions and the *Shariah* supervision board in the reserve banks (AAOIFI n.d. (a)).

The following are the powers of the Shariah Supervisory Board (AAOIFI n.d. (a)):

- The main aim of the Shariah Supervisory Board is to maintain harmony and consistency between the concepts and their application to *Shariah* supervisory boards of Islamic financial institutions and other convergent institutions. The *Shariah* Supervisory Board helps to avoid any contradiction and conflict among the fatwa and applications which are made by these institutions. This provides an active role for the *Shariah* Supervisory Board in the Islamic financial institutions and the reserve banks.

- The *Shariah* Board also helps in developing financial instruments which are approved by the *Shariah* Board. This enables the Islamic financial institutions to deal with changes, and evolutions which take place in the design of financial instruments and the development of formulae which are released in the field of finance, commerce and other banking sectors and banking services.

- The *Shariah* Board also helps in settling inquires which are related to giving an opinion on matters which may require further reasoning or settle inquiries which relate to the settlement of differences of opinion. The *Shariah* Board also acts as an arbitrator.

- The accounting standards issued by AAOIFI can also be reviewed by the *Shariah* Board. These standards may include accounting, auditing, and code of ethics or educational standards. The *Shariah* board has the power to review all the above standards at any stage of their choosing (Khan 1991). This power of review is granted to the *Shariah* Board so that the *Shariah* Supervision Board may ensure that issues are taken up in accordance with the rules and principles developed by Islamic *Shariah*. 
3.4.3 Objectives of the AAOIFI

There are four major objectives of the AAOIFI. These are as follows (AAOIFI n.d. (b)):

- to develop standards related to accounting and auditing and ensure that the standards are relevant to Islamic financial institutions;
- to publish policies of accounting and auditing which are relevant to Islamic financial institutions. This process is conducted through training selected employees who require these standards and policies in their businesses, such as employees of Islamic financial institutions and reserve banks. The implementation of these accounting and auditing polices is achieved through formal training, seminars, publications, newsletters, and is underpinned by research and other means;
- to develop, interpret and promulgate the accounting and auditing standards for Islamic financial institutions;
- to exercise the right to review and modify the accounting and auditing standards as per the requirements of Islamic financial institutions.

The major aim of the AAOIFI is to boost the confidence of the users of financial statements and financial information prepared by Islamic financial institutions. The AAOIFI also encourages the users of financial statements of Islamic financial institutions to make investments and invest their money in the Islamic financial institutions and avail themselves of services which are provided by the Islamic financial institutions (AAOIFI n.d. (b)).

3.4.4 Conceptual framework of AAOIFI accounting standards

The AAOIFI has a framework similar to the IASB’s conceptual framework. The AAOIFI framework (AAOIFI 1993) provides general rules for the Accounting Standards, which are more or less applicable to the Islamic banks and Islamic financial institutions. The framework of the AAOIFI includes coverage of objectives of financial accounting for Islamic banks and for the Islamic financial institutions (Kelly 1982).

According to AAOIFI’s accounting statement and standard (SFA 2); the statement of concepts is a definition of all the basic elements of the financial statements, which are as follows (AAOIFI 1993):

- statement of financial position
- the income statement
- the statement of changes in the owners’ equity
- the statement of retained earnings
- the statement of cash flows, or the cash flow statement
- the statement of changes in the restricted investments
- the statement of sources and the uses of funds in Zakat, and
- the statement of sources of funds in the Quard (loan) fund.

The AAOIFI statement of concepts has four basic accounting assumptions, as follows (AAOIFI 2012):

- the going concern
- the accounting unit concept
- the periodicity, and
- the stability of purchasing power of the monetary unit’s concept.

The statement of concepts has defined that the revenues, expenses, and gains and losses shall be added in the income statement of banks. Profits and losses will be recognized in statements of changes in restricted investments (AAOIFI 1993). The statement of concepts also provides measures for the measurement of the financial instruments, cash and its equivalent. The statements of concepts also provide that there are five qualitative characteristics, including reliability, understandability, relevance, consistency and timeliness (AAOIFI 1993). All these elements are also present in the framework of the IASB.

3.4.5 History of the development of AAOIFI accounting standards

This section focuses on the development of Islamic accounting standards. In order to gain insights into details of the history of Islamic accounting standards, we should first familiarize ourselves with the Islamic banking, as these accounting standards primarily find their use in the banking systems. Islamic banking encompasses all the banking activities that show compliance with Shariah law (Islamic law) (Khan & Hussin 2013). Prior to the introduction of international accounting principles and GAAP in the Islamic countries, Shariah law dictated financial proceedings in the Islamic countries. Shariah law is the backbone of Islamic teachings. It prohibits those practices that are unacceptable and forbidden in Islam; for example, payment or acceptance of interest (Ribā) or making money out of a business that’s illegal and sinful ‘Haraam’ (prohibited in Islam) (Khan & Hussin 2013).
3.4.5.1 First attempts at developing an Islamic accounting standard

The development of an Islamic accounting standard has a unique history and is closely related to the development of the Islamic financial institutions. Prior to the introduction of international accounting principles and GAAP in the Islamic countries, Shariah law dictated financial proceedings and still does in some Islamic countries both financially and politically (Khan & Hussin 2013). The importance of the Islamic countries has increased in the global economic context as the Islamic countries account for more than 25% of the world’s population, and there are 10 Muslim countries among 18 oil producing countries that account for 40% of the world’s total oil production. As well is the increasing contribution of Islamic countries to world trade and hence their emerging strategic position (Cooper & Yue 2008).

There are many large financial institutions and banks in the Islamic countries which are involved in international activities including the Amana Mutual Fund Trust, the Islamic Bank of Britain, the American Finance House, MSI financial services and so on. Most of Islamic countries are also members of many large international organizations such as the World Bank, the World Trade Organization and the United Nations. The increasing contributions of the Middle Eastern Countries (MEC) in international financial activities have become a reason for recognition of the MEC while developing international accounting standards (Cooper & Yue 2008).

In light of the facts, the need for a separate Islamic accounting system was thought of by the financial experts of the Islamic countries. The banking, insurance and capital market structures of these countries were also quite different from the European and other developed western world markets. Islamic accounting standards were necessary for the establishment of a financial structure that could emulate several economic principles laid down by the Shariah law (Khan & Hussin 2013).

3.4.5.2 Primary reasons for introducing of Islamic accounting standards

As we have previously noted, the emergence of Islamic countries’ economies in the late 1980s and 90s necessitated the need for a separate accounting standards system. Though Islam doesn’t mandate any particular form of accounting, it does stress the need to comply with established Islamic beliefs (El-Din 2004). However, there are some forms of accounting that show incompatibility with Islamic principles. The Islamic principles that condemn Riba and such other practices were the primary reasons behind the modification of several banking
operations’ and rules regarding accounting treatments and disclosure requirements for international financial institutes such as the World Bank and International Monetary Fund (Abdullah 2010).

There are three key issues with Islamic accounting that have attracted the attention of all Islamic financial experts. These are as follow (Yusoff 2009):

a) Exclusivity – addresses the following two key concerns:
   1. Should Islamic accounting co-exist with the conventional accounting (IFRS)?
   2. Should all the financial transactions be exclusively recorded by means of Islamic accounting standards?

b) Harmonization – has been defined in the previous segments of this section and stands as a very important issue in the context of Islamic and conventional accounting. Once again, it asks two questions:
   1. Are the IFRS’ and IASB’s accounting guidelines compatible with Islamic accounting principles?
   2. Can certain exemptions be allowed or disallowed in Islamic accounting standards?

c) Convergence – the issue of convergence is the most troublesome as far as the financial experts’ opinions are concerned, and the main reason behind such concern is the ever-increasing pressure on the Islamic countries for adapting conventional accounting norms. The simple question that needs answering in this section is whether IFRS should be applied in every aspect of Islamic financial transactions (Hidayat 2011).

The Islamic accounting standards became necessary for Islamic nations because of the non-applicability of some IFRS in Islamic countries since IFRS were designed primarily for addressing the accounting problems of European and other western countries (Hidayat 2011). The IFRS were oriented more towards the conventional institutions, conventional product structures and practices and thus were inadequate in addressing the problems related to typical Islamic financial transactions (Karim & Tomkins 1987).
An important point to note is that from the very beginning, Islamic banking suffered from their inability to handle the accounting irregularities, launch proper risk management practices and protection of investors’ rights. So in order to safeguard these practices, Islamic banking did feel the need for a new accounting standards system (Khan 1994). It is assumed that the primary objective of accounting should be to help users make important investment decisions. Accounting can be regarded as a religious duty and in order to perform this duty, one must use divine accounting methods. Thus Shariah is considered as very important for an Islamic accounting system (Khan 1994).

Islam heavily emphasizes the concepts of Riba and Zakat. They both are regarded as important religious rules and need separate accounting treatments which was impossible through the use of conventional accounting methods and which need to be completed through Islamic accounting principles and methods. The Holy Qur’an laid down the basic principles of Riba and Zakat by stating the duty of paying Zakat and the prohibition of Riba in different verses such as:

Righteousness is not turning your faces towards the east or the west. Righteous are those who believe in GOD, the Last Day, the angels, the scripture, and the prophets; and they give the money, cheerfully, to the relatives, the orphans, the needy, the traveling alien, the beggars, and to free the slaves; and they observe the Contact Prayers (Salat) and give the obligatory charity (Zakat); and they keep their word whenever they make a promise; and they steadfastly persevere in the face of persecution, hardship, and war. These are the truthful; these are the righteous. (Qur’an 2: 177)

O you who believe! Fear Allah, and give up what remains of your demand for (Riba), if you are indeed believers. (Qur’an 2: 278)

Shariah principles which found their root in the Holy Qur’an verses suggested that Islamic financial institutions need to comply with the Islamic principles of Riba and Zakat. So Islamic Accounting standards needed to be developed to meet the requirements of Shariah law.

3.4.6 Key parties involved in the preparation of AAOIFI accounting standards
As we have noted in the previous sections, the development of Islamic accounting standards only became possible due to the collaboration of the many parties involved. Islamic communities, Islamic financial institutions, and AAOIFI were some of the key groups involved in the development of the Islamic accounting standards (Mustafa 2003). Also, the existence of IASB contributed indirectly to the development of international Islamic accounting standards. If this institution was not in existence, there would have been no
foundation and no groundwork for the development of Islamic accounting standards (Chua & Taylor 2008). However, the Islamic accounting standards came into existence to fulfil the void which was there is the IASBs which did not follow the requirements of Shariah Law (Mustafa 2003).

AAOIFI in particular, is responsible for changing the face of Islamic banking and accounting. AAOIFI is an international autonomous not-for-profit Islamic corporate body that devises and sets accounting standards for various Islamic central banks and Islamic financial institutions. AAOIFI takes into account the advice and suggestions conveyed to it by its institutional members. It then issues guidelines, principles and standards pertaining to accounting, auditing and ethics (AAOIFI n.d. (b)). The Kingdom of Bahrain was the main supporter and authority figure behind the launching of Islamic accounting standards and then later it was supported by the governments and financial experts from countries such as Jordon, Lebanon, Syria, Pakistan, Sudan, Malaysia and Indonesia (AAOIFI n.d. (e)).

3.4.7 AAOIFI accounting standards and persistent problems

There are many differences in the accounting standards set by IASB and AAOIFI. AAOIFI accounting standards differ from the IFRS on issues such as leases, restricted contracts, and specialty investment accounting (Pomeranz 1997). Differences between IASB and AAOIFI give rise to issues related to Islamic principles. Islamic financial institutions emphasize the fact that in order to carry out Shariah-compliant transactions, they need to follow an Islamic accounting system and standards as these are based on religious beliefs and principles (Pomeranz 1997).

The two main issues that create problems in the application of conventional accounting standards for Islamic financial institutions are (Mustafa 2003):

a) differences in the objectives of the users of accounting information; and

b) differences in the contractual relationship between financial institutions and their stakeholders.

In addition to these two prominent issues, there were some other problems with the application of IFRS. They are as follow (Hamid 2012):

a) IFRS require the entry of those incomes that are generated in friendly transactions but Shariah contradicts them;
b) IFRS don’t require entries of Zakat or any other charity income; and

c) conventional accounting does not take into account ‘socially responsible financing’.

3.4.7.1 Proposed solutions of the problems

AAOIFI introduced its own accounting standards on 30 September 2012 (Islamic Banker 2011). In addition to these standards, AAOIFI has also introduced its first Financial Accounting Standard No. 1 (FAS 1) and a Statement of Financial Accounting (SFA 2) to address the concerns, issues and problems posed by the IASB (Hamid 2012).

AAOIFI closely followed Shariah principles while devising the accounting principles for Islamic countries. AAOIFI, in particular, tackled the following four issues (Abdullah 2010):

a) misperception and unanimity in understanding Shariah law;

b) the lack of knowledge of in-depth finance opportunities;

c) inadequate number of Islamic financial experts on accounting subjects and interested candidates; and

d) shortage of literature and research on Islamic accounting and banking.

AAOIFI not only identified these four troublesome issues but also suggested the solutions to all of them. These solutions are as follow (Abdullah 2010):

a) develop a right understanding of the Islamic Shariah law;

b) articulate the values and propositions that arise from investing in the Islamic countries;

c) provide proper education and training to interested candidates on subjects of Islamic accounting and banking principles; and

 d) develop a lot of reading content and study material regarding Islamic accounting principles by encouraging more research work on these subjects.

An overview of Islamic finance suggested that Islamic finance is based on basically four issues. They are as follows (Karim 1990):

a) there should be compatibility with the religious laws and Shariah principles;
b) risk & profit sharing strategies; such as fiduciary risk: the Mudharaba contract places the liability for the loss on the Mudarib (Entrepreneur in a Mudharaba contract); and displaced commercial risk: where Islamic banks ‘smooth’ the returns received by Investment Account Holders (IAH) by varying the percentage of profit taken as the Mudarib share.

c) real economic transactions and asset-backed transactions; and
d) ethical values and social justice. Islam forbids the use of unethical practices and the use of prohibited financial instruments.

So the equation that best defines the Islamic finance viewpoint may look like this:

![Image of an equation]

**Figure 3.2: Structure of Islamic finance: research model**

The four main issues regarding Islamic accounting are substance versus form, liability & equity, interest & dividend and ownership in Sukuk & Sukuk default (Karim 1990).

The parties that work for the solutions to these problems are AAOIFI, the local Shariah board and local regulators. The AAOIFI, in particular, has gained a lot of support in the meantime from a number of institutions and countries such as Dubai International Finance Centre, Lebanon, Qatar, Pakistan, Sudan, Jordan and Syria. Kingdom of Saudi Arabia, Australia, South Africa, Indonesia and Malaysia etc. have also acknowledged the importance of AAOIFI’s standards and pronouncements (AAOIFI n.d. (b)).

However, there is pressure on Islamic countries for adhering to the norms and standards set by IFRS as they will bring unanimity, harmony and clarity to all the financial transactions taking place worldwide. Increased pace of globalization has also come up with its own set of challenges further pressurizing Islamic community to conform to the International accounting standards (‘Pressure on Islamic finance’ 2013).
Chapter 4 – Theoretical Framework

4.1 Introduction

The purpose of this chapter is to describe the key features of the conceptual and analytical framework of accounting standards of the Islamic banks and to explain some of underlying guiding principles and decisions that formed their development. This section also explains the philosophical basis on which the research project took place, and establishes the relationship between the theoretical aspects and practical components of this research investigation regarding AAOIFI accounting standards.

This chapter is divided into two main sections; the discussion in the first section provides a brief discussion about the main features of the Shariah principles. This is followed by a discussion of the principles of Islamic banking in Shariah. The second section of this chapter discusses the Regulatory theories and involves the Public Interest, Economic Interest Group, Economic Regulation and Institutional theories.

4.2 Main features of Shariah principles used by Islamic banking

There are many features of Shariah principles that are adopted by Islamic banks in different countries. The principles of Islamic banking based on Shariah used by the Islamic banks have been categorized in the following areas (Haron 1998):

a) Profit and loss sharing principles;

b) Fee-based principles;

c) Free-service principles; and

d) Ancillary principles.

The principles in these categories were universally used by all Islamic banks regardless of the country in which their operations are based (Tricker 1976). Some Islamic banks have adopted principles in all four categories such as the Islamic Bank Bangladesh Limited, Jordan Islamic Bank, Bank Islam Malaysia Berhad, and Faisal Finance Institution of Turkey. However, not all Islamic banks have listed all four categories of Shariah principles. Some Islamic banks in different countries only employed three of the above-mentioned four principles such as Islamic Bank of Bahrain, Bank Melli Iran, Kuwait Finance House, Muslim Commercial Bank
of Pakistan, El Gharb Bank of Sudan, Beit Ettamwill Tounsi Saudi of Tunisia, and Dubai Islamic Bank of the United Arab Emirates (Haron 1998).

Apart from the common principles of Shariah there are specific countries that listed some principles which are mandated for use by the Islamic banks operating in the specified countries (Van Knippenberg 2000). Though, these principles are familiar within the country in which they are used and reported, this does not imply that other countries not applying these principles, are unaware of these principles (Haron 1998). Due to the different regulatory requirements and legislation, the relevance and comparability of financial statements were the foundations upon which accounting standards were predicated (Sarea 2012).

The development of the AAOIFI accounting standards is most importantly underpinned by the theoretical requirements of the Shariah principles. Shariah plays a main part in Islamic finance and according to Islamic scholars; Shariah is simply God-ordained sacred Islamic law that rules each and every aspect of a Muslim’s life. Shariah is the constitution of the Islamic world (Khan et al. 2011).

Hesab (account) refers to the accountability to Allah (God) that necessitates compliance with Shariah (Lewis 2001). Hesab is the main basis for the Islamic system and all relationships within any Islamic society (Al-Jirari 1996). It is the root of accounting; every Muslim has a responsibility to carry out the duties described in the Qur’an including all the actions of the business enterprise (Kamla 2005). Hesab has been mentioned more than eight times in the holy Qur’an (Askary & Clarke 1997). The Holy Qur’an has stated that everyone will be asked to account for their actions, as mentioned in the following Ayat (verses):

And stop them; indeed, they are to be questioned. (Qur’an, 37:24)

So by your Lord, We will surely question them all, about what they used to do. (Qur’an, 15:92–93)

The tenets of Shariah are absolute, not subject to any change or interpretation, and valid for all times and places. This ideology also covers Islamic financial systems. Islam has formulated comprehensive ethics governing how business should be run, how accounting ought to be undertaken and how banking and finance is to be arranged (Khan et al. 2011).

A global network of Islamic banks, investment houses and other financial institutions has started to take shape based on the principles of Islamic finance as laid down in the holy
Qur’an and the Sunna (Practice and traditions of the Prophet Muhammad; peace be upon him) (Falgi 2008). In this context, Shariah principles should be practised in all the Islamic bank’s transactions, including the important features of Islamic economics such as the concepts of Riba (Interest or usury), Zakat (A religious levy as a fundamental duty), and Gharar (speculation). One of the main differences between conventional banking and Islamic banking is a prohibition on interest. Islamic law emphasizes that Riba is not allowed. The general rule for accumulating wealth in Islamic economics was to earn a profit by assuming the risk of doing so whilst strictly condemning Riba (Ahmad, Rehman & Saif 2010). The Holy Qur’an states the prohibition of Riba several times, such as the following Ayat (verses):

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

And whatever you give for interest to increase within the wealth of people will not increase with Allah. (Qur’an, 30:39)

The concept of Zakat provided a wider circulation of wealth in the Islamic society (Al-Mogbel 2003). It is a requirement of Shariah principles that Zakat be paid by every Muslim. Zakat is a religious tax levied at a minimum rate of two and a half percent of total income or assets which must be paid at the end of every year. The money goes towards charity and the relief of the poor (Al-Mogbel 2003). Zakat also must be paid on the owned shares of profit. Thus, companies should disclose information that enables users to calculate the appropriate amount of Zakat, which represents one of the main transactions of accountability of Shariah principles (Adnan & Gaffikin 1997). The disclosed information in the financial reports must be reliable, true and comprehensive to enable users to specify the correct amount of Zakat and fulfils their religious accountability (Lewis 2001). The Holy Qur’an states the duty of paying Zakat in different Ayat (verses) such as:

And be steadfast in prayer; give Zakat, and bow down your heads with those who bow down [in worship]. (Qur’an 2: 44)

And be steadfast in prayer and given Zakat: and whatever good ye send forth for your souls before you, ye shall find it with Allah; for Allah sees well all that ye do. (Qur’an 2: 110)
Islamic economic principles underpin the Islamic banking system and financial accounting in the Islamic banking system. Islamic economics has been defined as the application of economic knowledge and facts according to the principles of *Shariah* (Malik, Malik & Waqas 2011). There are a number of Islamic financial instruments which can provide *Shariah* compliant finance such as *Murabaha*, *Mudharaba* and *Shirkah* which were designed to follow Islamic principles.

Islamic law prohibits the charging and paying of interest but allows the earning of profits (*Murabaha*) on the basis of participation in the market (Shofawati 2014). This legal injunction has motivated the establishment and successful operation of a number of Islamic financial institutions. Islamic finance involves structuring financial instruments and financial transactions to satisfy traditional Muslim strictures against the payment of interest and against engaging in gambling. It is a field of growing importance for conservative Muslims, who are uncomfortable with the western style bonds and banking that involve payments of interest (Shofawati 2014). *Shariah* also attempted to refrain from *Gharar* (speculation). *Gharar* is a sort of gambling, and it is forbidden by *Shariah* principles because it uses other’s wealth for nothing (Al-Suwailem 1999).

The key features of an Islamic economic system are to ensure an equitable distribution of money and wealth among the people. The main principles guiding Islamic banks are partnership, justice, and opposition to excessive risk. *Shariah* principles encourage a society where an individual or a person is not dependent on others; *Shariah* principles state that every individual actualizes his/her own abilities in a society. So, Islamic economic principles and Islamic laws give priority to *Mudharaba* (a type of limited liability business alliance where capital is entrusted by one or more investors to an agent-manager) and *Shirkah* (an agreement of association made by two or more parties) forms of business partnership (Sulaiman 2003). For depositors, putting their money into an Islamic bank is more like being a shareholder. The depositors receive a share of any profits instead of receiving interest. Islamic Banks also share profits with customers by providing equity finance instruments (*Mudharaba*), as the bank provides the capital, and the borrowers, using their expertise and knowledge to invest the capital. Profits will be shared according to the finance agreement (Sulaiman 2003). With equity finance there is no assurance that there will not ever be any profits, nor is there an assurance that the capital will be recovered (Sulaiman 2003).
Another Islamic financial instrument is the Islamic lease finance agreement (Ijara), whereby the bank buys an item for a customer and then leases it back over a specific period at an agreed amount. Ownership of the item or property remains with the bank, which will seek to recover the capital cost of the equipment plus a profit margin out of the rentals payable (Tabash & Dhankar 2014). For example, Emirates Airlines use Ijara to finance their expansion (Garrett 2011). Under the Ijara (Islamic mortgage); the bank purchases a property then leases or rents it back to the customer. The customer makes regular payments to cover the rental for occupying or otherwise using the property, insurance premiums to safeguard the property, and also amounts to pay back the sum borrowed. At the end of the mortgage, title to the property can be transferred to the customer. The demand for Islamic mortgages has shown considerable international growth. For instance, HSBC was the first UK clearing bank to offer mortgages in the UK designed to comply with Shariah under HSBC’s Islamic mortgage (Garrett 2011).

Islamic banks have found ways to make money from lending. Islam encourages Muslims to invest their money and to become partners in order to share profits and risks in the business instead of becoming creditors. As defined in the Shariah principles, Islamic finance is based on the principle that both the provider and the user of capital are supposed to equally share the risk of business ventures. Instead of demanding interest, they buy the asset outright on behalf of the borrower. The borrower pays off the loan and a fee for using the asset until the amount is repaid and ownership transfers to the borrower (Adeniran 2014).

The rights to loan repayments can be sold as an Islamic bond (Sukuk), similar to mortgage backed securities but instead of a yield, the bondholder receives repayments on the loan, and some rent. Consequently, Islamic lenders have not yet entered money markets that have recently emerged (Yeates 2008).

The main objectives of financial accounting are to assist a company to analyse the type and nature of information which should be a part of their financial reports in order to provide assistance to the users of these reports in making informed and sound decisions (Hoggett, Edwards & Medlin 2003). The government agencies usually have the power and right to directly obtain the specific information that best serves their requirements. However, other external users (such as equity holders, holders of investment accounts, current and savings account holders, other depositors, other dealers with Islamic banks, Zakat agencies and
regulatory agencies) of information can only obtain the common information contained in the Islamic banks’ financial reports (El-Din 2004).

The objectives of financial accounting for Islamic banks and institutions were to achieve the following (El-Din 2004):

a) Verify the rights and obligations of all interested parties in accordance with the principles and concepts of fairness, clarity and business ethics of Shariah principles;

b) Participate in the preservation of Islamic banks’ assets, the rights of Islamic banks and the rights of others in an appropriate manner;

c) Financial reports provide useful information to report users, and consequently enable them to make legitimate decisions in their dealings with Islamic banks; and

d) Participate in the enhancement of management and Islamic banks’ productive capabilities, and encourage compliance with the established goals and policies, of Shariah principles, in all transactions and events.

It can be seen from the above that there is a need for AAOIFI accounting standards to deal with the procedures and mechanisms involved in Shariah compliant financial transactions in Islamic banks, and to meet the needs of Muslim users.

4.3 Regulatory theories

An understanding of different regulatory theories and the regulatory environment, have important roles to play in the formulation of an effective regulatory regime. This was especially the case in rationalizing and implementing AAOIFI accounting standards in the UAE. Walker and Robinson (1993, 1994a, 1994b) used a critical discourse analysis in their studies to identify the key players involved in the accounting standard-setting process and to analyse their discourse and its implications. They concluded that there are possible roles played by key participants in the rule-making process. It has been suggested by Sarea (2013) and others that the regulators in Islamic countries should provide full support to the application of AAOIFI accounting standards by making them mandatory for adoption in all Islamic institutions.

In the following sections, various theories of regulation are considered, to explain the existence of Islamic accounting regulation and to understand why some of the Islamic
accounting prescriptions become formal regulations, while others do not. These sections also explore perceptions of the economic and social consequences of potential Islamic accounting requirements, and how these may influence the decisions of the UAE accounting standard-setters in the context of the local laws, culture and religion. The theories, namely Public Interest theory, Economic Interest group theory of regulation, Economic Regulation theory and Institutional theory, are discussed below.

4.3.1 Public interest theory

This theory focuses on the reasons for the existence of a particular regulation, and is fundamentally rooted in the concept of the public interest. The theory lays down that the primary focus in formulating, drafting and implementing regulations should be on the need to meet the perceived public interest and not the personal or private interests of regulators and other officials (Posner 1974). The underlying reason for the existence of regulations is to provide social and economic support to the society as a whole and not to particular groups or entities. The legislative backbone of the regulatory regime must serve the public interest and ensure economic justice and welfare optimization (Deegan 2009). There are two major assumptions that need to be considered in applying the public interest theory, namely (Deegan 2009):

a) The regulator and the public have the same objective in formulating the regulation. The regulations were the outcome of the public’s desired intentions.

b) The public interest was clearly and equitably defined.

The formation of the US Sarbanes-Oxley Act of 2002 was a very good example of the public interest theory at work to protect the interests of investors caught up in the large-scale corporate fraud and corruption uncovered in the US during 2000–2002. A number of corporate governance issues were faced by US regulators in the failures of companies such as Enron and Arthur Anderson. Such failures motivated the US government to legislate, and the regulator to initiate processes, to protect the public interest, hence the Sarbanes-Oxley Act was formed to enhance standards of corporate governance (Deegan 2009). Some studies have used the public interest theory to explain the development of regulation. The study by Hu et al. (2013) explored the application of public interest theory on the creation of the water accounting board by the Australian government. They indicated that public interest theory
affected the water accounting standards, whereas the capture theory highlighted the relevant business groups ultimately controlling the threat of the water board.

The theory’s principal focus is public interest and welfare. To protect against any biased regulation formation and to eliminate malpractices, it was suggested by Adams and Tower (1994) that the following parties should be involved in the formation of regulatory frameworks:

a) Legislative body

This body constructs the initial legislative framework and has the overall role of coordinating resource allocation.

b) Regulatory body

This body has the function of observing and supervising the application of the legislation through a regulatory framework, and acting as mediator to resolve disputes arising as a consequence of the resource allocation. This body may be considered a control mechanism for the legislation.

A general view of public interest theory was that it improved competition and eliminated avoidable monopolies which tended to act as a detrimental power where consumers were concerned (Cardoso 2008). Public interest theory was also considered pivotal for resolving temporary imbalances which could become permanent without intervention. The formation of regulations has to achieve a balance between social benefit and the costs associated with the implementation of the regulations (Deegan 2009).

If this theory is applied to Islamic practice in relation to accounting standards, it can be said that the Islamic community has their own belief system and Shariah principles, which ultimately govern and guide financial transactions. It is noted that all practicing Muslims wish to avail themselves of a banking service subject to the regulation of Shariah principles. However the current IFRS are not based on Islamic culture and related local law, but represent the requirements of conventional banking. Given the terms of the public interest theory, the development of the Islamic accounting standards is an inevitable consequence. The proper regulatory body must be formed with a well-defined objective to provide clear-cut reporting and accounting guidelines in conformance with Shariah principles. The adoption of
the IFRS did not support Islamic regulations as it is very different from the relevant cultural and belief system.

Islamic banks in the UAE can provide efficient banking services to the nation if they are supported with appropriate banking laws and regulations. This would aid them to adopt Islamic accounting standards. Islamic banking may face the hurdle of different accounting standards. It can be a big obstacle in the way of development of Islamic banking because it creates the problem for local and foreign investments. It is also difficult for investors to take decisions about their investment. So, Islamic banking will need to work hard to harmonize the Islamic accounting standards. Also, Islamic banking should have proper regulatory and institutional framework in the UAE. The AAOIFI could play important role to develop the uniformity in Islamic accounting standards (Shanmugam, Perumal & Ridzwa 2004). Thus, the uniformity of financial reporting will improve the Islamic banking services and it will really be helpful to all stockholders especially customers and investors.

The IFRS have been framed in accordance with generally accepted practice world-wide, but the culture of the UAE is different from most other countries. Islamic principles are very different from those of other religions. So it was very important to mould Islamic accounting standards accordingly, as in a number of cases the principles of Islam, conflict with the principles of IFRS. Corporate governance of an Islamic institution also has to be promoted in accordance with the Islamic religious roots. Thus, the development of Islamic accounting standards arose due to a need for standardized accounting disclosure for the reporting of Islamic corporate enterprises, as the end user of the financial statement was Islamic society as a whole.

4.3.2 Economic interest group theory of regulation

The economic interest group is also known as the private interest theory. This theory states that a particular group generally tries to formulate regulations to reflect their interest (Deegan 2009). In society it may be the case that many groups are not in alignment with each other’s interests and objectives and hence they generally try to convince the regulatory body to frame regulations which are favourable to a particular group (Deegan 2009). The economic theory of regulation assumes that groups will seek to promote their self-interest (Posner 1974).

In concern of the financial accounting; it assumed that particular financial groups may lobby the accounting standards setter to adopt particular accounting standards. Some studies paid
attention to political activity in terms of broad interest group categorizations and their role in affecting regulatory outcomes. Puro (1984) said that the groups of standard setters make a broad range of lobbying activity in a socio-political environment to employ outcomes well-matched with their interests. She also recognized that a complex set of interactions influence the position adopted by audit firm respondents to draft accounting rules. According to Dyckman (1988), the political environment has been created due to the concern of the public and the private sector for maintaining their interests. Hope and Briggs (1982) investigated the impact of political performance on the application of accounting regulation. Their study focused on the political environment in which the standard-setting body operates. They also examined the deferred taxation accounting issue in the United Kingdom and provided evidence of the impact of the political activities. As a small group of aerospace companies were effectively changed the UK accounting standards on research and development in favour of their personal interest, despite the greater part of participants in the discussion process didn’t agree with the objections that had been made to the proposals by the aerospace companies (Deegan 2009). The study by Hail, Leuz and Wysocki (2010) argued that there is political pressure on the IASB to make sure that accounting regulation meets the international need. They added that because of the replacement of national accounting standards by IFRS, the national accounting standard-setting bodies lost power to involve the decision-making processes in their accounting regulations. Martinez-Diaz (2005) stated that different public and private groups, such as the international organization of national securities regulations and the World Bank give the IASB a political influence in the international and national accounting standard-setting processes.

The extraction industry also can be considered a perfect example of an economic interest group, as it was in need of specific regulation with regard to reporting and the treatment of pre-production cost-related transactions. The IFRS 6 has made it compulsory to follow the expense pre-production cost which is the result of demands by the major regulators of this industry (Cortese, Irvine & Kaidonis 2009). A more recent example of lobbying of accounting setters by a financial group, some banks in European countries had successfully lobbied against full endorsement of IAS 39 by the European commission. However, unlike their European counterparts, Australian banks were unable to force the local regulator into amending the requirement of IAS 39. In Australia some banks argued that some of provisions of IAS 39 (AASB 139 within Australia) will result in their accounts showing significant volatility that don’t reflect the underlying economic reality, and this can be damaging to a
bank’s perceived financial stability. In response to the banks concerns; the IASB made some changes but refused to change IAS 39 substantially and the full requirement of IAS 39 were incorporated with AASB139 (Deegan 2009).

Almost all the UAE financial institutions were following IFRS. The central bank is the regulator for all such financial institutions. However, it should be noted that the Dubai International Financial Center (DIFC) was the first organization in the UAE to decide to implement and follow AAOIFI standards subject to its own regulatory body known as the Dubai Financial Service Authority (DFSA). The DFSA, with the support of the other authorities, has tried to lobby the regulatory body to set the AAOIFI standards to encourage solid growth. The DSFA has played a very major role in consulting the central bank for the setting of Islamic accounting standards and has tried to have the standards set for its own benefit.

4.3.3  Theory of economic regulation

This theory was developed by Stigler in 1971 (Stigler 1971). It stated that the existence of the regulation was a type of economic product based on the equation of demand and supply. The economic product was handled by two major groups, one being the industry leader or stakeholders and other being the regulatory authority (Posner 1974). The industry stakeholders were considered to be on the demand side and the regulatory authority, typically a government body, was on the supply side. The regulator has the power to act in the best interest of the public if demanded by the industry stakeholders (Posner 1974). When the number of dominant players in the industry is greater there will be a group lobby, and at such a time demand for regulation would be high. However, when the markets were monopolized and the industry players constituted a strong cartel, the demand for regulation was less. Mitnick (1980) illustrated theories of power and capture of the standard setting process. He explained regulatory processes and identified the factors that contribute to a predisposition of regulatory bodies to take actions consistent with the preferences of the industry they were intended to regulate. Mitnick (1980) identified lobbying behaviour, control over information and financial dependency factors to enable the industry to capture the regulatory body.

Cortese, Irvine and Kaidonis (2009) used regulatory capture theory to show that the Financial Accounting Standards Board (FASB) failed to apply their accounting methods to the oil and gas industry which still adopts different accounting practices. They also provided evidence of
the politicization of the accounting standard-setting process by the FASB to standardize oil and gas accounting in the 1970s. The theory of economic regulation was predicated on the idea that regulations were not formulated to reflect a position of market efficiency, but were used by market players as a medium for acquiring economic benefits which may be affected by political factors (Adams & Tower 1994). A pictorial representation of the relationship among different participant is mentioned below:

![Diagram](diagram.png)

**Figure 4.1:** Theories of regulation: reflections on statutory supervision of insurance companies in Anglo-American countries (Adams & Tower 1994)

### 4.3.4 Institutional theory

Institutional theory provided the rationale for why particular organizations adopt their operating structures based on other organizations structures in the same industry (Deegan 2009). The principal reason behind this was that every organization tries to convince outsiders that they have a legitimate organizational structure and have legitimate operations for survival in the industry (Deegan 2009). A number of researchers have adopted this theory in their accounting research, including Covaleski and Dirsmith (1988), Broadbent, Jacobs and Laughlin (2001) and Brignall and Modell (2000). It has been stated by Dillard, Rigsby and Goodman (2004) that institutional theory has become a leading theoretical framework within organizational research. The accounting practice of each organization is reflective of an industry culture (Deegan 2009). There were two major components of this theory: institutional isomorphism and institutional decoupling. Both concepts are important in analyzing independent corporate practice (Deegan 2009).

This study is focused on the theory of institutional isomorphism which helps in knowing the political and ceremonial forces that exist within an organization. The theory states that each organization tries to follow the principles and operating modes as other organization
For example, if a new organization started business in a particular country, this organization would definitely follow and copy the operational structure and other practices of existing similar organizations. This was considered necessary to convince outsiders of the existence of the company’s legitimate business (Deegan 2009).

Institutional theory also gave support to legitimacy theory and stakeholder theory. These theories stated that the manager is pressured into adopting and acting in compliance with widely accepted corporate practice (Deegan 2009). The study by Hu et al. (2013) also explored the application of legitimacy and stakeholder theories on the creation of the water accounting board by the Australian government. They argued that these theories are important in explaining the establishment and the development of the water accounting board and a water reporting standard.

Three types of pressures were involved, namely coercive isomorphism, mimetic isomorphism and normative isomorphism. In real life it is very difficult to differentiate the above three types (Carpenter & Feroz 2001). The study tried to provide a brief on these types as follows below.

### 4.3.4.1 Coercive isomorphism

This theory stated that a manager may experience both formal and informal pressures, largely as a result of other organizations functioning within the same industry environment (DiMaggio & Powell 1983). These types of pressures were generally a consequence of the dependence of one organization on another for survival (Deegan 2009). For example, rules and regulations imposed by government on the companies to abide by the environmental norms and failure leads to serious ramifications (Mir & Rahaman 2005).

### 4.3.4.2 Mimetic isomorphism

This theory states that managers try to improve the perceptions of external stockholders for the legitimacy of their organization. The organization that fails to follow the procedures adopted by other organizations in the same sector will possibly lose their legitimacy (George & Bennett 2004). Under the terms of this theory managers will be constantly pressured to make efforts to convince external stakeholders that the organization is a legitimate business.
4.3.4.3 Normative isomorphism

This theory outlined the pressures placed on employees and/or managers due to the expectations of a certain professional group (Deegan 2009). For example, an accounts manager working in an organization can be under pressure to comply with accounting practices adopted and followed by other professional accountants within the same professional society (DiMaggio & Powell 1983). Equally, there exists pressure on managers to follow the same reporting practices as adopted by other similar professionals (DiMaggio & Powell 1983). Such practice is considered as generally accepted practice.

An example of normative isomorphism that executive officers who attended elite business schools were likely to adopt an approach to organising a business known as the multi divisional form of organisation. The multi divisional form of organization was taught as part of conventional perception in elite business schools. This prominence was similarly trained executives resulted in organizational similarity within specific types of organizational fields (Palmer, Jennings & Zhou 1993).

The UAE has a number of competent and skilful professionals who are interested in Islamic banking. As there are a greater number of experts currently employed in the conventional banking, the Islamic banking sector can benefit from the availability of such expertise by encouraging them to transfer from conventional banking to Islamic banking systems and subjecting them to professional training and development in the practices of Islamic accounting standards. In the context of isomorphism’s three theory types, this supports the view that local Islamic experts’ religion and culture will help the experts implement Islamic accounting standards in a better and more effective way, as the AAOIFI accounting standards will have a background of Islamic banking practice, culture and religious laws. Such managers and experts can create uniform practices for accounting treatments and reporting, and can thus help in the growth of the Islamic financial and banking institution.
Chapter 5 – Research Design and Methods

5.1 Introduction

Previous chapters presented literature review, background and theoretical framework on which the research and is based. This chapter discusses the research methods employed in this study to achieve the research objectives. Description and understanding of the methodology is required for scientific research, in order to achieve the results (Gauch 2003). This study used questionnaire surveys and interviews, in addition to a comparison between AAOIFI accounting standards and IFRS. This chapter is organised as follows: first, there is a discussion of the research objectives and questions; the research methodology is then presented, followed by a discussion of the research methods, including the justification for research philosophy – its design and administration, and the selection of the sample. This is followed by a description of the data collection and a discussion of the analytical procedures which also includes a consideration of issues such as validity, reliability, and ethics that arose during the research design and quality control processes.

5.2 Research objectives and questions

The overall aim of this study was to explore the suitability of AAOIFI standards for Islamic banks in the UAE. This study aimed to examine the currently adopted IFRS as compared to AAOIFI accounting standards in order to identify the differences and determine which system could better satisfy user needs from the perspective of respondents and to investigate the feasibility of adoption of the AAOIFI accounting standards in the UAE Islamic banks and to identify the potential impact of the adoption of the AAOIFI accounting standards on the presentation and disclosure of financial statements of Islamic Banks.

A comparison between AAOIFI standards and IFRS was made to help determine the main differences between them. This comparison was made by analysing the content and requirements of each set of standards in terms of the information that must be disclosed, and the different accounting treatments, if any, between them. The gaps and differences between the two set of standards exist and will continue to exist. These gaps and differences are a natural result of the differing structural objectives of the IASB and AAOIFI. AAOIFI’s mandate is to develop standards where IFRS do not cater for the specificities of Islamic Banking or leads to Shariah compliance issues. As long as there are economic, legal and
social differences between Islamic and conventional banking and finance practices, there will also be differences in the standards issued.

This study compared the specific accounting standards which have been developed by the AAOIFI and the applied IFRS in the UAE Islamic banks, to ascertain whether Islamic banks in the UAE should continue to follow the IFRS issued by the International Accounting Standards Board (IASB), or adopt the Islamic accounting standards issued by the AAOIFI. AAOIFI have issued 26 standards on accounting, five standards on auditing and seven standards on governance, in addition to two codes of ethics and 40 Shariah standards (outlined in Appendix 1). The focus will be on the following accounting standards: Disclosure on Transfer of Assets, Deferred Payment Sale, Foreign Currency Transactions and Foreign Operation, Provisions and Reserves, Murabaha (cost-plus financing), Mudharaba (profit sharing) and Zakat (a religious levy as a fundamental duty).

This research will lead to a better understanding of the similarities and differences in the application of IFRS and AAOIFI accounting standards to the UAE Islamic banks. This study will also examine the relevant AAOIFI accounting standards, to gain an understanding of the factors that must be taken into account when considering the adoption of AAOIFI by the Islamic banks in the UAE, and to also understand the factors that may prevent the complete adoption of AAOIFI in the UAE.

The potential shift from IFRS to AAOIFI accounting standards for UAE Islamic banks is expected to present significant challenges for the UAE Islamic banks’ financial report preparers, users, and auditors. This study will contribute to existing knowledge of the topic in many ways. As can be noted from the literature, there have been several calls for a separate examination for AAOIFI accounting standards. Therefore, this study attempted to fill the general gap in the literature on the relevance of AAOIFI accounting standards to Islamic banks, and a more specific gap, by studying the adoption of AAOIFI accounting standards in the Islamic banks in the UAE. As mentioned previously, the UAE has many unique features which are not found in other Islamic countries.

The UAE is a member of the GCC. Islamic banks in the GCC countries such as Bahrain and Qatar have begun adopting AAOIFI Standards. In addition, the Dubai International Financial Centre in the UAE has decided to use these standards as well. This study explored the impact of AAOIFI accounting standards on the UAE Islamic banks reporting after the adoption, and
contributes to an understanding of expected difficulties associated with such adoption. Although the UAE may differ from some Islamic countries, this study may be useful for other Islamic countries in gaining a clearer picture of the differences between Islamic countries by comparing the findings of this study with other studies, and applying the results to their countries.

This research contributed to existing knowledge and practices not only in Islamic countries but also in western countries in terms of a deeper understanding of the Islamic accounting standards and how the adoption of AAOIFI accounting standards could influence the Islamic banking process, activities and financial reporting. In addition, Islamic bank managers and shareholders will gain an insight into the factors which led to the development of the AAOIFI accounting standards and how these factors could influence the Islamic institutions’ processes, activities and financial reports.

Moreover, this study may provide useful material for researchers and academics with an interest in Islamic accounting research in general, and also in the UAE, as there is a dearth of studies and research regarding accounting standards and AAOIFI standards in particular. Other interested parties, such as local and foreign investors and universities in the UAE, may find this study useful if expanding their courses in Islamic accounting.

This study is unique as no study has yet explored the potential influences of the AAOIFI accounting standards on Islamic banks in the UAE. This study also determined the roles of key players in the development of AAOIFI standards and ascertains their possible influence on Islamic banks in the UAE regarding the adoption of AAOIFI standards. No study has yet focused on the roles of key players involved in the development of the Islamic accounting standards issued by AAOIFI.

This study also provides a clearer understanding of the factors which may also influence the adoption of AAOIFI accounting standards in Islamic banks in general, using the UAE as a case study. In this context, the study determined whether these factors may also be barriers to the adoption of AAOIFI accounting standards in the UAE. The study offered insights into the AAOIFI organization when examining the suitability of its accounting standards to the UAE Islamic banks, and contributed to an understanding of the Islamic accountability framework with regards to accounting practice in the UAE.

Overall the objectives of this study were as follows:
• To examine the difficulties and problems occurring during the application of IFRS in the UAE Islamic banks.

• To provide an understanding of the factors or reasons that might lead the UAE Islamic banks to adopt AAOIFI accounting standards and the expected benefits that may flow from this adoption.

• To provide an understanding of the factors and issues that Influenced the Adoption of IFRS

• To examine the difficulties and problems during the possible transition to AAOIFI accounting standards.

• To identify and understand the role of the key players and their important roles in developing the AAOIFI’s standards in the UAE and explore the factors leading to the development of these standards adoption.

To explore the overall objective, it is necessary to seek answers to a series of questions related to the research investigation and describe the motives, impacts, benefits, problems and difficulties associated with the adoption of the AAOIFI standards. For this purpose, the researcher divided the overall objective into several specific objectives with related research questions, as outlined in the following.

5.2.1 Understanding the factors that may influence the adoption of AAOIFI standards

First objective was the need to examine the relevant AAOIFI accounting standards, to gain an understanding of the factors that must be taken into account when considering the adoption of AAOIFI by the Islamic banks in the UAE, and to also understand the factors that may prevent the complete adoption of AAOIFI in the UAE. The extant literature showed that several factors should be taken into account, e.g. culture, market economy, and political system, which vary greatly from country to country, thus presenting obstacles to the establishment of an accounting system that can function equally well in all Islamic countries (Nobes & Parkar 2006). From the discussion of the background and theoretical framework, it seemed that the application of an appropriate accounting system by the Islamic banks in the UAE would help to increase their level of accountability (see Chapters 3 & 4). Therefore, this study attempted to examine and evaluate the potential adoption of AAOIFI standards, their relevance to the Islamic banks in the UAE and their ability to meet the accounting needs of Islamic banks.
• The principal question here is: *What would be the impact on the UAE Islamic banks of applying the AAOIFI Accounting Standards?*

This question is divided into three subsidiary questions:

• *Do Islamic banks in the UAE need a corresponding alternative set of Accounting Standards?*

• *What are the underlying factors that may influence the adoption of AAOIFI Accounting Standards in the UAE Islamic banks, and which issues might act as barriers to their adoption?*

• *Identify the main challenges in adopting AAOIFI Accounting Standards – What problems and difficulties would UAE Islamic banks face when applying AAOIFI Accounting Standards?*

The answers to these questions were initially sought from key professionals engaged in the UAE Islamic banks regarding the influences that may affect the potential adoption of AAOIFI standards. Their opinions were also sought about factors that might prevent the complete adoption of AAOIFI by Islamic banks in the UAE and to the internal or external influencing factors that might arise during the adoption of the AAOIFI standards.

### 5.2.2 Identifying the roles of key players

Second objective, was to determine the roles of key players in the development of AAOIFI standards and ascertain their possible influence on Islamic banks in the UAE regarding the adoption of AAOIFI standards. According to Boolaky (2004), some Muslim countries have adopted IFRS in its complete form, without modification, whereas some countries have only partially adopted these standards, making modifications based on local needs, such as Malaysia (Deloitte 2010). Saudi Arabia is the only country in the Gulf Cooperation Council (GCC) with a professional accountancy body, namely, the Saudi Organization for Certified Public Accountants (SOCPA). This body used IFRS as a point of entry in issuing local standards and the IFRS are used only when the national standards do not offer provisions for particular cases (Mirghani 1998). However, the IFRS have been adopted as the national accounting standards in the UAE.

According to Tyrrall, Woodward and Rakhimbekova (2007), IFRS may fail to cover all the accounting requirements present in some developing countries. This could also be an issue in
the UAE. Some Arab countries, such as the UAE, use Shariah as a guide in most aspects of life and find that this is not always compatible with IFRS, as certain issues must be considered. For example, Islamic law forbids interest, but no provision is made for this in the IFRS (Hussain et al. 2002). Religion is therefore one of the environmental factors that should be taken into account when considering the adoption of IFRS.

- The question here is: *What was the role of key players in the development of the Islamic Accounting Standards in the UAE?*

This question was answered from information gained through interviews conducted with a number of the key players involved in the development of the Islamic Accounting Standards in the UAE. Their viewpoints were acquired by questioning them about the factors or reasons that might lead the UAE Islamic banks to adopt AAOIFI standards, and the benefits of the potential adoption. As well, their opinions were sought about the actual problems and difficulties experienced during the adoption of IFRS.

**5.2.3 Identifying the differences between IFRSS and AAOIFI standards**

The third objective was to examine AAOIFI accounting standards in comparison to IFRS in order to identify the differences and determine which system may better satisfy user needs. The literature demonstrated that differences existed in the information needs of Islamic country’s users. Based on the literature and the discussion of the background of AAOIFI accounting standards and IFRS (see Chapters 2 & 3), this objective will be divided to two sub-objectives. To identify the differences and similarities between AAOIFI standards and IFRS, and to explore professionals’ perceptions of which system may better serve their needs and which they would prefer to be applied in the UAE.

- The principal question here is: *What are the main differences and similarities between the applications of AAOIFI Accounting Standards and the IFRS? And, which system can better satisfy users’ needs in the UAE?*

This question is divided into three subsidiary questions:

- *Who are the users of accounting information of Islamic Banks in the UAE?*
- *What are the user needs for accounting information in the UAE Islamic banks?*
- *Are these user needs different from those of Western countries?*
A comparison between AAOIFI standards and IFRS was made to help determine the main differences between them. This comparison was made by analysing the content and requirements of each set of standards in terms of the information that must be disclosed, and the different accounting treatments, if any, between them. Moreover, some of the comparisons were included in the questionnaires to gather respondents’ opinions on the extent to which the existing AAOIFI standards and IFRS meet the needs of accounting systems users in the Islamic banks of the UAE.

5.3 Research philosophy

This research acquired knowledge through exploring the perspectives of individuals included in the study sample. Both the culture and environment of researcher and participants also played a large part in determining the research approach taken (Snape & Spencer 2004). The research philosophy included a set of fundamental assumptions and beliefs as to how the world is perceived which then served as a framework for thinking about what guides the behaviour of the researcher (Jonker & Pennink 2010). The two main philosophical dimensions to distinguish existing research paradigms are ontology and epistemology. Ontology is the view of how one perceives a reality; epistemology is the structure of beliefs that generate, understand and use the knowledge that is deemed to be acceptable and valid (Saunders, Thornhill & Lewis 2009). The research philosophy in this research can be depicted as follows:

1. Philosophy of Positivism: This philosophy underpins the collection of necessary facts, data, figures and the like. The role played by the researcher is important as the data collected forms the basis on which the analysis and interpretation is undertaken. The researcher is then able to provide effective recommendations and conclusions and underline the limitations faced while conducting the study (Pring 2004).
2. Philosophy of Interpretation: This philosophy underpins the evaluation and analysis of the data and facts collected. It is ideal for social research because it allows the researcher to take into account issues such as social conditions and cultural matters raised in the organisations studied, which is not possible in a positivist paradigm. The interpretivist paradigm also helps with understanding and interpreting the qualitative component of the research, and can be used to describe the outcomes of the research (Teddlie & Tashakkori 2009). For analysing the data the researcher may need to adopt working assumptions. In this study the researcher collected qualitative information from the population sample through interviews and questionnaire survey. The researcher needed to take into consideration the cultural environment within which participants operated as well as their knowledge and their role, which played a significant part in shaping one’s thoughts.

3. Pragmatism as Research Philosophy: this philosophy implies the use of a research methodology that appeared best able to address the research problem. Therefore the researcher following this approach would have the freedom to use any of the techniques and processes associated with quantitative research or qualitative research. Pragmatism was described by Saunders, Thornhill and Lewis (2009) as:

A position that argues that the most important determinant of the research philosophy adopted is the research question, argued that it is possible to work within both positivist (quantitative) and interpretivist (qualitative) positions. It applied a practical approach, integrating different perspectives to help to collect and interpret data. (p. 598)

In employing “pragmatism” as a research philosophy the researcher uses different techniques as and when required. This study combined both quantitative and qualitative methods; the two methods complemented each other (Fielding & Fielding 1986), and the use of both methods was therefore deemed advantageous (Patton 1990). Pragmatism is particularly suitable for mixed methods research, and consequently this study is based on the pragmatic approach as the most suitable for the research.

Pragmatic philosophy is used to determine the overall utility of a given concept or construct in the research process (Creswell 2003). The main use of the pragmatic philosophy is to determine what issues need to be considered and which can be ignored; it can be used to determine the general function of a certain construct to the research process (Johnson & Onwuegbuzie 2004). Pragmatism as a research philosophy implied the use of a research methodology that appeared the best suitable to address the given research problem (Creswell
Thus the researcher followed the pragmatic approach to undertake this research, which gave the researcher the freedom to use any of the techniques and processes associated with quantitative or qualitative research. Mixed methods research are mainly based in the pragmatic philosophy, which states that the most important element of research is the practical difference it can make in the research environment (Creswell 2003).

5.4 Research method

The choice of research method and how a researcher conducts research depends on their own ontological and epistemological beliefs; in other words, their beliefs about the social world and what is known about it, and the nature of knowledge and how it can be acquired (Snape & Spencer 2004). The research or method adopted in this case can be depicted as follows:

a) Research setting: The research setting in this case is the Islamic Banks and financial institutions operating in the United Arab Emirates. The most significant aspect of Islamic banking is that it is banking without any interest rate.

b) Identifying the Problem: The problem is the analysis of the implementation of IFRS and Islamic Accounting Standards as prescribed by AAOIFI in the United Arab Emirates and comparing between these two standards. Explanatory Mixed Methods Design was used as described in Creswell (2005).

c) Documentary analysis: Documentary analysis was used to investigate the problem which in this case was the proposed implementation of IFRS and the features of Islamic Accounting Standards developed by AAOIFI. Conclusions, Recommendations and Limitations: A conclusion has provided at the end of the research, proposing an understanding of the basic issues faced by Islamic banks in the United Arab Emirates, when adopting and implementing IFRS and Islamic Accounting Standards as prescribed by AAOIFI. Also proposed was an understanding of the basic factors and issues that dealt with Islamic Accounting Standards developed by AAOIFI. Recommendations were provided as to what steps needed to be taken to solve the problem. Last, limitations were specified so that they could be taken into consideration while undertaking future research studies similar issues (Lategan 2012).
5.5 Research design

The researcher used the approach which best assisted in answering the research questions (Marshall & Rossman 1989). With regard to this study the mixed method research involved collecting the desired information through distribution of questionnaires to the sample population selected at random, followed by a semi-structured interview of a small section of the population sample so as to cross check the accuracy and reliability of the data collected. The researcher conducted interviews and formulated a questionnaire so as to identify the perceptions of the participants at large, and to check the validity of the statistical analysis. Both quantitative and qualitative methods were used which permitted a more thorough and comprehensive investigation of the subject than would be the case if using one method alone. Using the mixed method approach helped to achieve cross validation of data and avoided information bias which might have stemmed from the use of a single method of data gathering (Hussey & Hussey 1997; Silverman 2000).

In this study, the combination of the two approaches permitted the shortcomings of each to be neutralised or balanced. A large sample was surveyed through the use of formal questionnaires, as it was not possible to interview all participants due to considerations of time and funds. Where the questionnaires were limited in gathering detailed information and opinions, this was overcome through the use of interviews to gather more in-depth qualitative data. The quantitative approach used in the questionnaires helped to compare answers between sample groups and find significant differences between them. This is one of the advantages of the quantitative method (Saunders, Thornhill & Lewis 2009). The qualitative research design used the collection of textual or other forms of data and non-statistical analysis of that data to generate knowledge (Creswell 2009). Qualitative research offered the potential for acquiring deep knowledge which cannot be generated using statistical methods or generalisation offered by quantitative research (Creswell 2009).

5.6 Mixed methods research

A mixed method research was adopted to collect data for this study from which to draw the conclusions and make recommendations. Mixed method research studies are defined as those studies that tend to combine different research methodologies (Bergman 2008). It was particularly important in mixed methods research to demonstrate how specific insights arose and how research questions were answered (Creswell & Plano Clark 2007). As the aim of the research questions was to investigate and describe the motives for, and benefits, problems and
difficulties of, the potential adoption of AAOIFI standards, the mixed methods were considered to be in keeping with this aim. To collect the desired information, this study employed a quantitative method comprising closed-ended questions in a questionnaire survey, and a qualitative method comprising a check-list of specific questions in semi-structured interviews. Both methods have their strengths and weaknesses (Spitzlinger 2006). The other aspect of the mixed methods research in this study was the use of various tools and techniques to analyse the data in a quantitative manner, and to provide the necessary conclusions and recommendations (Creswell 2003). Mixed method research were also considered to help in better identifying the problem that shaped the future direction of the research by overcoming the limitations encountered by the researcher (Spitzlinger 2006).

Quantitative research is highly structured, objective, and generally uses quantitative measures, whereas qualitative research focuses on the details of a situation and the reality behind these details, and thus is more subjective (Collis & Hussey 2003). Using quantitative research methods, the researcher studied and examined specific research factors, such as religion, culture, local investors, regulators, foreign investment, and global financial institutions their impact on the adoption of AAOIFI standards and the environment within which they operated, and the most importantly, why and how the issues arose. Quantitative research seeks to determine the existence of a constant relationship between events, or between factors (Robson 2002).

Qualitative research, on the other hand, emphasises words rather than quantification in data collection and analysis (Bryman 2004). In this study, the researcher relied on the beliefs and views expressed by the participants in response to the researcher's specific questions directed through questionnaire survey and interviews, the data collected being expressed in words. Qualitative research is based on data in the form of words rather than numbers, and conclusions are based on data that was not quantified, such as attitudes and values (Rudestam & Newton 1992). The researcher then analysed the data and presented the outcomes in diagrammatic representations in the form of pie and bar chart graphs. Qualitative research, assisted in comprehending the phenomena being researched, assessing the essential keynotes that appeared during the research, and ultimately assisting in the construction of a theory (Easterby-Smith, Thorpe & Lowe 2002).
5.7 Data collection

The data collection process in this research study was based on the acquisition of required data and information from professionals, managers and key persons in Islamic banks and financial institutions in the UAE, using questionnaire survey methods. To achieve the objectives of the current study and to answer the research questions the researcher employed three data collection methods, namely, documentary data, unstructured interviews, and questionnaires. The document review and interviews were selected as data collection procedures to represent the qualitative component of this research and the questionnaires represented the quantitative component. These methods will be discussed in the following section.

5.7.1 Documentary data

Documentary data may be either qualitative or quantitative, and it may also be public or private (Punch 2005). Data may be collected from organisations and individuals, with the researcher determining what is important within the documents and how it may be understood (Tight, Hughes & Blaxter 2006). There were two types of documentary data used in this research, namely primary documents and secondary documents. Documentary data was considered to be secondary data as it had already been analysed, such as in the case of a biography, but in many cases it would be considered primary data if it hadn’t been analysed (Punch 2005). The documentary data used in this research included formal documents, IFRS, Islamic Accounting Standards issued by AAIOIFI, banks’ annual reports, legal standards, Shariah principles embodied in the Holy Quran and narrations of the prophet (peace be upon him), previously related studies, and surveys. Documents were selected to reflect different issues, including the key factors of IFRS and AAoIFI accounting standards. Secondary documents were documents produced by people who were not present at the scene but who received eye-witness accounts to compile the documents, or had read eye-witness accounts (Bailey 1995). A document, unlike a speech, could have an independent existence beyond the writer and beyond the context of its production (Jary & Jary 1991).

In this study, for secondary data, library searching was adopted to collect documentary data starting with documents about the literature of Islamic accounting standards and the background of AAoIFI. The collected documents focused on the structure, objectives and development of the AAoIFI as well as the willingness to provide information. The collected documentary data for the unstructured telephone interviews also involved identifying the key
parties involved in the preparation of AAOIFI in the UAE. On the other hand, primary documents referred to accounts produced by people who experienced the particular event or the issue that the researcher wanted to study (Bailey 1995). Primary data was collected by conducting both the questionnaire survey and unstructured interviews with participants who represented different Islamic Financial Institutions in the UAE.

5.7.2 Design of the questionnaire

In order to obtain more valid data and information in an effective and efficient manner; the questionnaire survey was selected for this study as a key instrument for data collection from the sample of participants. The reason behind this was that the questionnaire survey helps in the collection of pertinent data in a cost efficient manner (McNeill & Chapman 2005). The questionnaire survey is the method most commonly used by researchers to collect primary data (Aaker, Kumar & George 2000). The questionnaire comprised of a set of questions that were related to the defined research objectives, so that required data was collected from the selected participants to obtain information about the sample participants’ attitudes and opinions concerning the subject of the research (Bryman & Bell 2007). Some of the advantages of the questionnaire have been outlined such as they were economical; they permitted wide coverage; they were comparatively easy to arrange and analyse, and they avoided personal interaction with the researcher (Babbie 2001). The questionnaire survey was also helpful in gaining support for answering the main research question and related sub-questions so as to reach final conclusions (Crowther & Lancaster 2008).

Questionnaires could be administered through the post, face-to-face, by telephone or by e-mail (Oppenheim 2000). This study used internal postal questionnaires, as this method encouraged respondents to complete the questionnaires at the time and place of their preference. The questionnaire survey for this study was carried out within several Islamic banks in the UAE. Participants were identified through their banks; arrangements were made with the Public Relations department of each bank approached, to select volunteers from amongst managers and professionals to undertake the questionnaire survey. Letters of invitation, and information sheet and consent form were provided with a questionnaire for each participant who indicated their willingness to be contacted. Also, an enclosed stamped addressed envelope was attached for the return of the completed questionnaires. This method of administering the questionnaires was simple and inexpensive, generating a high response rate. There were various ways in which the response rate was improved. For instance, the
questions were clear, unambiguous, and non-controversial. Also a follow-up questionnaire was sent to individuals who had not responded to the first one; this certainly generated a few more responses, which then served to provide a means to check any bias.

The questionnaire survey has been considered by some previous studies which examined related issues of IFRS in different developing countries, such as Joshi and Ramadhan (2002), Kosonboov (2004), Tyrrall, Woodward and Rakhimbekova (2007) and Alkhtani (2010). A comparison between AAOIFI standards and IFRS was also considered when developing the questionnaire. The questionnaire was administered to current managers and professionals who had already applied Islamic Accounting Standards and methods. The questionnaire was designed to be completed within a 20 minute time frame so that banks did not find it a burden on their managers. The questionnaire framed for the research study utilised a mixed method approach for the collection of data. The questionnaire was carefully planned and designed in a manner which maximised its effectiveness, kept costs low, and simplified the analysis of the results.

The questionnaire was divided into four parts. The first section covered the respondents’ background and current job title, level of education, professional qualifications and experience in their current occupation. The second section covered questions about the respondent’s perceptions of the users, the users’ needs, and financial reporting related to IFRS, and addressed perceptions concerning difficulties and problems encountered in the adoption of IFRS in the UAE Islamic banks and the factors that had been taken into account when considering the IFRS adoption. The third section compared AAOIFI standards and IFRS. The fourth section addressed perceptions of different influences that could play a major role in the development of AAOIFI standards, and the advantages and benefits of adopting AAOIFI standards by Islamic banks in the UAE. The questionnaire included both closed-ended and open-ended questions in order to create a flexible platform so that relevant data in regard to the research study could be collected and analysed using both quantitative and qualitative methods (Crowther & Lancaster 2008). The set of closed- and open-ended questions were helpful in seeking a detailed perspective of the participants about the research issue. They were also helpful in gaining support for answering the main research question and related sub-questions so as to reach the final conclusions (Crowther & Lancaster 2008).

The closed-ended questions provided a fixed number of alternative answers and were quick and easy for respondents to answer. Closed-ended questions were framed for making survey
respondents comfortable with questions. Also, the specific options of closed-ended questions created bounded responses that provided a simplified base to participants. There were different types of close-ended questions, such as lists, categories, rankings, ratings, quantities and matrices.

In this study the responses to the closed-ended questions were recorded using a Likert scale. This form is most frequently used by researchers where the participants are asked to scale their response to statements related to the questionnaire subject (Saunders, Thornhill & Lewis 2009). The Likert scale used for closed-ended questions measured the extent to which a person agrees or disagrees with a particular statement. According to Sekaran (2000), respondents typically indicate a degree of agreement or disagreement with a variety of statements about some attitudes, usually using odd-numbered scales containing five or seven points. The Likert scale used in this study was designed with a five point scale ranging from ‘Strongly Agree’ to ‘Strongly Disagree’ (Connolly 2006). Sekaran (2000), identifies an inherent problem that arises when using an odd-numbered Likert scale as it permits respondents to choose to ‘sit on the fence’, marking the mid-point neutral answer.

That is, when using a 1 to 5 rating, respondents could be tempted to mostly use 3. Such a choice could tend to artificially indicate a central tendency and kurtosis in the data that might otherwise not be present. Alternatively, an even-numbered scale could be used, but it would force respondents to make a choice on either side of an imaginary mid-point, thus introducing another form of artificial bias through skewing data either side of the mid-point. Therefore in this study, the choice was made in favour of the least-problematic option, selecting an odd-numbered Likert scale ranging from 1 to 5.

On the other hand, including open-ended questions as part of the mixed approach in the questionnaire survey desired to acquire specific information from the participants in a detailed manner. Open-ended questions were helpful in collecting the responses and perspectives of participants regarding the impacts, effects and challenges involved in adopting Islamic banking standards in the participants’ banks. The responses to the open-ended questions permitted the qualification of specific data sourced from responses to the closed-ended questions. Open-ended questions provided respondents with the freedom to write their own answers in their own words (Fink 2003). Although open-ended questions required more effort from the respondents, they allowed more spontaneity, probing and detail in the answers (Oppenheim 2000).
5.7.2.1 Pre-testing of the questionnaire

The pre-testing of the questionnaire provided an effective way to refine the research instruments and make changes to the research plans before the field study commenced (Creswell 1998). The pre-testing of the questionnaire comprised three survey respondents and focused on testing the feasibility of the questionnaire. The pre-testing of the questionnaire was oriented towards elimination of errors and vagueness from the questions included in the questionnaire instrument. It provided assistance in making the questionnaire more comprehensible to the respondents, thus improving the likelihood that the collected data was reliable.

The researcher conducted a pre-testing of the questionnaire by meeting three managers from different banks, discussing with them the questionnaire survey to check its reliability and suitability in achieving the research objectives. The feedback were collected and evaluated; there were comments about some questions needing to be clearer, some needing to be combined into a single question and some less important questions being deleted in order to keep the questionnaire to a reasonable length. All the required modifications based on the pre-testing of the questionnaire were made by the researcher.

5.7.3 Unstructured telephone interviews

The posted questionnaires alone were not enough to achieve all the research objectives, particularly as some of the questions required exploring in more detail and going into greater depth about key players’ experiences related to the potential adoption of AAOIFI by the Islamic banks in the UAE. For this reason primarily, telephone interviews were selected as a data collection approach for the qualitative portion of this research providing a greater volume and depth of data to enhance the research. The qualitative data required a more detailed data collection approach that allowed the participants to provide full details about the subject discussed. The interviews were conversational in tone during which the researcher and participants exchanged information about the topic of research and their views on the matter. According to (King & Horrocks 2010) conversational interviews give opportunity to derive unexpected information.

Interviews in general may be structured, semi-structured and unstructured. Unstructured interviews were deemed the most appropriate for this study. In the unstructured interviews, the questions concentrated on a number of particular points, but offered certain flexibility and
scope for the interviewer to elicit further information from the interviewee (Bryman 2004). Unstructured interviews also allowed the interview questions to vary according to the role of the interviewee and their particular experiences. This method provided opportunities to discover issues not considered previously and then helped to answer the research questions (Kosonboov 2004).

The interviews which were used in this research phase were conducted via telephone with five of the key people engaged in Islamic Accounting Standards in the UAE. The researcher maintained careful control over the interviews. The interviewer noted down responses to the questions on the interview guide, and any diversions from the telephone interview guide were noted, along with the answers given.

**5.7.3.1 Design of interviews**

Before the interviews the researcher summarised the topics that should be covered during the interviews. This served to increase the validity of the information provided (Saunders, Thornhill & Lewis 2009). The interview questions or themes were derived from the literature and the comparison of AAOIFI standards and IFRS and the information and results from the questionnaire analysis.

Interview appointments were arranged and conducted by telephone. At the beginning of each interview session the researcher explained the purpose of the study and the contributions that interviewees could make to the study. Each interview lasted between 15 to 30 minutes. During the interviews attempts were made to answer all the interview questions; issues that were expected to be sensitive were left until the end of the interviews, as according to (Healey & Rawlinson 1993) the longer that interviewees are in discussion with the researcher the more likely it is that their trust and confidence will increase. Although the researcher tried to adhere to the sequence of the interview themes, the content of the interviews was largely governed by the flow of the interviewees’ thoughts. Occasionally the researcher would probe for more explanation, or interrupt to ensure the interview session remained on track. Throughout all the interviews, the researcher made notes, with the permission of the interviewees.

Following were the main questions used in the interviews:

- What were the reasons behind the introduction of Islamic Accounting Standards in the UAE?
• When and where were the first efforts made towards coming up with Islamic accounting standards in the UAE?
• What were the problems faced?
• How will the problems be solved?
• Which key parties were involved in the implementation of Islamic Accounting Standards in the UAE?

5.8 Population, sampling and respondents

The target population, the size of the sample, and the sampling strategy for the qualitative and quantitative segments of this research were different for the questionnaire survey and the unstructured telephone interviews. As such, these procedures are described separately.

5.8.1 Target population

The population of a research study is generally defined as the group of people, organisations, or objects to which the results would apply, and from which a representative sample could be drawn (Gill & Johnson 1991). For this research, the target population of the quantitative and qualitative research segments were different. The target population for the quantitative segment of the study was represented by the questionnaire survey, comprised managers and professionals from four Islamic banks in the UAE. These banks were the Abu Dhabi Islamic bank, the Dubai Islamic bank, the Al Hilal Islamic bank, and the Emirates Islamic bank. The target population of participants was selected on the basis of the information requirements of the research questions. The respondents presented the actual and practical aspects of the benefits, impacts and challenges of the potential adoption of AAOIFI accounting standards, and the differences between AAOIFI accounting standards and IFRSs.

The target population for the qualitative segment of the study represented by unstructured telephone interviews was substantially more limited. It consisted of some of the key persons involved in Islamic accounting standards in the UAE, comprised of managers and members of Fatwa and Shariah Supervisory Board of four different Islamic banks in the UAE namely; Abu Dhabi Islamic bank, Dubai Islamic bank, Al Hilal Islamic bank, and Emirates Islamic bank.
5.8.2 Sample size

The questionnaire survey covered a wider sample of potential respondents than did the interviews. The final sample size for the questionnaire survey was 52. A total of 80 questionnaires were distributed to managers and professionals in four Islamic banks in the UAE, from which 63 questionnaires were returned, and eleven were discarded as unusable. These managerial and professional respondents were selected because they were involved with Islamic bank transactions on a daily basis and it was expected that they had an understanding of the accounting standards in the Islamic banks. It was important to gain their viewpoints, to provide a basis for contrast with the viewpoints held by the central bank. The population sample size of 80 managers and professionals were not high, relative to the regular employees, however the population size was deemed appropriate for the questionnaire survey purposes. Moreover, given the numbers of managers and professionals were not high, relative to the regular employees, the population size was deemed appropriate for the questionnaire survey purposes. Initially, there were 80 managers and professionals selected from four Islamic banks (Abu Dhabi Islamic bank – 23; Al Hilal bank – 19; Dubai Islamic bank – 22; Emirates Islamic bank – 16). The resources at the researcher’s disposal and the anticipated rate of useable questionnaires returned determined the size of the sample (Finn, Elliott-White & Walton 2000). Out of the 63 completed questionnaires, only 52 were completed correctly and in all respects and were included in the analysis. The response rate for the questionnaire survey was 78.75%, and the usable response rate was 65%, which was acceptable for this study. The branches of the Islamic banks surveyed were selected on a random basis.

The size of the sample is a less important characteristic for qualitative research, because of the purposeful selection of the research process (Creswell & Plano Clark 2007). The sample size for the unstructured interviews was fixed at a size that was likely to achieve saturation, or the point at which the researcher discovered no further information emerging about the topic. David and Sutton (2004) suggested that it is possible for the sample size to be estimated according to the experience of the researcher and the resources available in terms of expenditure and time. The targeted sample was eight respondents; three of them refused to participate in an interview as they were very busy and did not have the time. Accordingly, the final sample size selected for the unstructured telephone interviews was five participants.
5.8.3 Sampling procedure

It was essential that the sampling process for the questionnaire survey was random and unbiased to ensure the reliability of the collected data for achieving the final results (Bryman & Bell 2007). A random selection process in this research was used to identify the impact of the potential adoption of the Islamic Accounting Standards on the Islamic banks and to identify the challenges associated with their adoption. The random sampling approach was based on the equal probability that individuals in the target population were included by chance in the sample. The idea was also to ensure that the overall process of sample selection was based on the unbiased behaviour of the researcher (Connolly 2006).

To obtain participants for the research across a range of Islamic banks in the UAE, this research involved three stages in the sampling process whilst maintaining the randomness of the selection. The first stage required the identification of all the UAE Islamic banks that could be in the sampling pool; that is, all Islamic banks in the UAE that could adopt the IFRS. When this stage of the sampling was completed it was found that there are nine such Islamic banks (Global Banking & Finance Review 2013). The second stage involved selecting the four largest Islamic banks in the UAE and their branches. These Islamic banks were identified in terms of their location, the number of branches, and the number of professionals and managers employed. The third stage of the sampling process involved selection of the individual participants. Eighty (80) professionals and managers were selected using a multi-stage random sampling process. Arrangements were organised with the media centre of each of the four Islamic banks, and approvals were requested to allow the researcher to contact the selected managers and professionals who were willing to participate in the questionnaire survey, and liaise with them. These participants were contacted via email and telephone. Letters of invitation (by email and post) were also sent to them. After receiving responses from the potential participants indicating their willingness to be contacted directly, information sheets and consents forms were sent to them, in preparation for the questionnaire.

In the first section of the questionnaire, some preliminary questions were asked of all participants to ensure they were appropriate for the research. This involved the completion of the participants’ consent to participate in the questionnaire survey, indicating their understanding of all of the aspects of such participation. The researcher monitored the participants’ willingness to continue participation in the research by maintaining contacts via email or phone, and addressing all questions or concerns that they raised.
For the unstructured interviews, the selection of participants was based on purposeful sampling. Purposeful sampling is an approach in which participants are selected based on their specific characteristics of interest to the researcher and their knowledge about the research project (Creswell & Plano Clark 2007). Therefore, interview respondents were selected for this study based on their role, experience, and ability to make an important contribution to the study as well as their involvement in setting AAOIFI or using financial information in their places of employment.

This was a non-random sampling method that was not appropriate for quantitative research, but which is ideal for qualitative research due to the smaller sample size and the need to target the specific characteristics of the participants involved in the research (Creswell & Plano Clark 2007). The key persons of interest with regard to Islamic accounting standards in the UAE were selected based on their known roles within the Islamic institutions. This can be classified as a form of expert sampling, whose opinions offered particular insights into the research area (Creswell & Plano Clark 2007). In this case, eight respondents from four different Islamic institutions in the UAE were selected. These Islamic institutions were: Dubai Islamic Bank, Al Hilal Islamic Bank, Abu Dhabi Islamic bank and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).

5.8.4 Respondents

The overall questionnaire survey usable response rate was 65%. Following, Table 5.1 shows that this rate represented 57% of professionals and managers approached in the Abu Dhabi Islamic bank, 63% in the Al Hilal bank, 68% in the Dubai Islamic bank and 75% in the Emirates Islamic bank.

<table>
<thead>
<tr>
<th>Group</th>
<th>Population (No.)</th>
<th>Sample (No.)</th>
<th>Distributed (No.)</th>
<th>Usable Responses (No.)</th>
<th>Usable Response Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Abu Dhabi Islamic bank</td>
<td>23</td>
<td>23</td>
<td>23</td>
<td>13</td>
<td>57</td>
</tr>
<tr>
<td>Al Hilal bank</td>
<td>19</td>
<td>19</td>
<td>19</td>
<td>12</td>
<td>63</td>
</tr>
<tr>
<td>Dubai Islamic bank</td>
<td>22</td>
<td>22</td>
<td>22</td>
<td>15</td>
<td>68</td>
</tr>
<tr>
<td>Emirates Islamic bank</td>
<td>16</td>
<td>16</td>
<td>16</td>
<td>12</td>
<td>75</td>
</tr>
<tr>
<td>Total</td>
<td>80</td>
<td>80</td>
<td>80</td>
<td>52</td>
<td>65</td>
</tr>
</tbody>
</table>

On the other hand, five interviews were conducted for the qualitative segment of this study. The interviewees were two managers and three members of Fatwa and Shariah Supervisory
Board selected from four different Islamic banks in the UAE, and these Islamic banks were coded 1 to 4. Table 5.2 shows the number of interviewees.

<table>
<thead>
<tr>
<th>Group</th>
<th>Respondents (No.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Islamic Bank 1</td>
<td>2</td>
</tr>
<tr>
<td>Islamic Bank 2</td>
<td>1</td>
</tr>
<tr>
<td>Islamic Bank 3</td>
<td>1</td>
</tr>
<tr>
<td>Islamic Bank 4</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>5</strong></td>
</tr>
</tbody>
</table>

5.9 Methods of analysis

The analyses of data collected from the questionnaire survey and unstructured interviews were varied in this study. Quantitative data collected from the questionnaires was analysed using descriptive statistics generated by SPSS software, while, the qualitative data collected from the questionnaires and the unstructured interviews was analysed using qualitative content. This section describes each of the methods of quantitative and qualitative analysis.

5.9.1 Quantitative analysis

The quantitative analysis was performed using descriptive statistical analysis. Descriptive statistics were univariate analyses describing the shape, distribution, and variations in the data that was collected from the sample, and provided an understanding of the sample’s basic characteristics (Healey 2011). Some characteristic of descriptive statistics included measures of central tendency; such as the arithmetic mean, median, and mode. Other characteristics included descriptions of and the data spread, such as quartiles and standard deviations, as well as percentages and frequencies. Quantitative data collected from the questionnaires was analysed using computer software, the data being coded and analysed using SPSS for Windows. Such software provides significant assistance in the evaluation of descriptive statistics of different aspects of the sample as revealed by the questionnaire responses (Hanson et al. 2005). Moreover, with the assistance of the SPSS software, the analysis and description of the data became easier, which assisted the researcher in deriving inferences from the questionnaire survey data.

The sample for this study was considered small (52 respondents). The respondents were from different Banks. To explore the differences in answers, Cronbach’s alpha testing was used to
determine the internal reliability or internal consistency of the scales. For this analysis, a threshold of $\alpha \geq 0.5$ was set for determining whether a scale would be adjusted or accepted as it was, based on previous research suggesting this was the lowest acceptable rating. Exploratory factor analysis (EFA) was used in order to determine the validity. These two tests were used because the variables in the questionnaires were of the ordinal and nominal scales, and were performed using frequency tables that showed the frequency of the various categories as well as the proportion of responses within the category. Comparing the differences and similarities in the responses of participants for the two financial accounting standards i.e. AAOIFI standards and IFRS was made easy through creating cross tabulations. Correlation analysis was used for examining the relationship between the predictors and the identified variables. Such analysis was helpful in evaluating the correlation between adoption of AAOIFI standards and the positive effect in the form of increased transparency.

5.9.2 Qualitative analysis

Qualitative analysis was used to the open-ended questions that were included in the questionnaire. Patterns in the source text or coding were explored. The answers were explored qualitatively so as to identify the themes revealed by survey responses. The analysis was used to understand detailed perspectives of the Islamic bank managers and professionals by accessing more information than a Likert scale allows.

Qualitative content analysis was then used on the outcomes of the unstructured interviews. Qualitative content analysis has been defined as an approach of experimental, methodological controlled analysis of texts within their context of communication, following content analytic rules and models, without rash quantification (Mayring 2000). Qualitative content analysis goes beyond extracting objective content from conversations to examine meanings, themes and patterns that may in particular conversations. Such analysis allows an understanding of social reality in a subjective way, and provides insight into complex models of human thought and language used, as well as providing analysis of the content and meaning of messages passed through a text, media or communications (Krippendorff 2004).

Qualitative content analysis was selected for this study because it was ideal for determining meanings and interpretations of the unstructured interviews, rather than focusing strictly on the word choices used by interviewers. Each interview was examined to determine the content with regard to the research questions. Responses were combined and organised to determine a
general theme within the responses. Qualitative content analysis emphasised an integrated view of speech and its specific contexts. It was then constructed to provide a general insight into each of the topics as discussed within the research questions which was organised thematically. A summary of the interviewees’ insights for each area was then provided, which included specific responses as well as any disagreement that was found.

5.10 Reliability and validity

Key issues in this study included reliability and validity. The research instruments, both the questionnaires and the unstructured interview questions, were initially tested using peer review; that is, these questions were assessed and evaluated by supervisors to determine the overall performance and provided more accurate information compared to the assessment of the individual. Reliability and validity were different in the qualitative and quantitative research methods. This section discusses these concerns separately in each case to demonstrate how they were approached.

5.10.1 Quantitative research reliability and validity

Reliability and validity are both required for the quantitative research method (Salkind 2004). Reliability referred to the ability of the questionnaire as a research instrument, to consistently measure the same thing, while validity referred to the consistency with which the questionnaire provided the basis for measurement of the underlying construct it was intended to measure (Salkind 2004). To determine the reliability of the instrument, the researcher used two approaches. First, robust questionnaire construction techniques were used to create the questionnaire, including techniques for constructing questions and avoiding researcher bias (Bradburn, Sudman & Wansink 2004). Second, the researcher used a Pre-testing approach for oversight and critique before adjusting the questionnaire (Bradburn, Sudman & Wansink 2004). To determine the reliability of the questionnaire, the researcher examined its internal validity using Cronbach alpha, which determined the internal consistency of the questionnaire and its findings. The Cronbach alpha was a coefficient that determined how well the questionnaire findings were correlated with each other (Hill & Lewicki 2006).

However, to eliminate unreliable items from the scales and improve the reliability of the statistical analysis, the researcher used the factor analysis technique as the key statistical approach. Factor analysis is designed to identify factors, or latent variables that underlie observed variables (Harrington 2009). It uses a regression technique to determine the strength
of relationships between variables along specific relationship lines. This technique was performed in SPSS, resulting in factor loadings that identified the strength of the relationship between factors (Harrington 2009). These factor loadings were then used to identify the strength of the factor and its contribution to the overall observed outcomes of the dependent variables (Harrington 2009). This allowed the identification of the strength of relationship between variables and factors, identified causal factors underlying one or more variables, and eliminated items that were not associated with certain variables (Harrington 2009). The use of the factor analysis technique was chosen as a useful method because it was easy to understand and because it provided a more detailed analysis than simple causal variable relationships. It also provided satisfactory results in terms of improving scale reliability, through elimination of any low-level factors.

The approach followed for conducting questionnaire survey of closed-ended questions was intended to add credibility and validity to the research. Respondents were provided with multiple options to answer the questions. Simple and unambiguous questions were included in the questionnaire survey, so as to make sure that all respondents could interpret the questions in a similar manner. Random selection of respondents for collecting the responses made the questionnaire survey process more valid and reliable (Greig, Taylor & Mackay 2007). The use of the SPSS tool for quantitative analysis of the collected data helped to prevent personal bias arising from the involvement of the researcher, thus ensuring the reliability of the data. The analysis of quantitative data for reliability and validity was carried out through correlation analyses and cross-tabulations. Both statistical tools gave an authentic base to the data analysis approach which was necessary for reaching validated outcomes, thus making the research reliable as well (Jackson 2008).

5.10.2 Qualitative research reliability and validity

It was difficult to analyse and interpret the qualitative data as it was unstructured in nature. Golafshani (2003) holds that qualitative reliability and validity cannot be determined by statistical approaches or the control of research design. He argued that reliability and validity have less application for qualitative research than for quantitative research. Indeed, dependability and credibility, rather than reliability, was considered to be a more appropriate determination for qualitative research; that is, under this criterion, the ability of the researcher to conduct the research credibly, and the credibility of the outcomes, served as a determining factor in reliability. As well, validity, a concept that was embedded in quantitative research,
was seen more as a matter of trustworthiness and openness of the analysis in qualitative research (Golafshani 2003). Tracy (2010) proposed a framework of criteria for determining the reliability and validity of qualitative research. These criteria have been applied in this study, and these include “(a) worthy topic, (b) rich rigor of the study, (c) sincerity the researcher, (d) credibility of the researcher, (e) resonance of research, (f) significant contribution, (g) ethics, and (h) meaningful coherence” (Tracy 2010, p. 837).

Therefore, the meaningfulness and the significance of the research was discussed in Chapter 1 and demonstrated to be a meaningful topic. The rigor of the study was described in Chapters 2, 3 and 4, which allowed understanding how the knowledge was derived. The credibility of the researcher was communicated through the discussions in preparation for the research as described in Chapters 5 and 6. Also, resonance and coherence qualities were demonstrated in the discussion of the research findings in Chapter 7. According to Hennink, Hutter and Bailey (2011), reliability came when there was a fit between what the researcher recorded as data and what occurred in an actual way in the natural setting where the research was conducted. So, open-ended questions that were asked of participants in their natural setting of work i.e. Islamic banks were measured in accordance with the aims of this research study.

According to Gravetter and Forzano (2011), validity is achieved in qualitative research when the data is collected in depth. The data in this study was analysed to identify and explore the various themes arising from the interviews of professionals and managers in selected Islamic banks in the UAE. This shows that all the findings generalised from the qualitative data were authentic and thus formed a basis from which to derive valid conclusions and obtain answers to the research questions. Overall, the content of the selected sources and citations along with the degree of the qualitative questionnaire’s relevance to the given topic contributed to the both validity and reliability of the data (Taylor, Sinha & Ghoshal 2006).

5.11 Ethical issues

Survey respondents should be assured about the confidentiality of their responses along-with maintaining their anonymity with respect to the research study prior to the discussion and analysis of their crucial perspective about the research issue (Hanson et al. 2005). The surveys conducted in this research study involved ethical considerations since it required information regarding individuals’ beliefs, opinions and practices. These considerations included the protection of individual participants’ identity. Before carrying out the data collection and
analysis sections of this research process, effort was made to establish and convey the fact that the surveys were conducted with high ethical standards and morality and that the researcher maintained a high degree of responsibility, accountability and transparency in the administration of the survey. Additionally, care was taken to prevent the identification of participants. Therefore, privacy, anonymity of the participant and confidentiality of the information were paid close attention to at all stages of this research. In order to minimise respondents’ risks and discomfort, the respondents were informed of the survey’s ethical safeguards.

It is crucial to take ethical aspects of the research study into consideration in developing an authentic and valid base for evidence gathered during the study. A breakdown in the ethical safeguards would have negative implications for the entire research work. In this study, high importance was given to ethical considerations to ensure the study was authentic and reliable. Participants in social research frequently place themselves in a position of significant vulnerability during participation in a survey (Punch 2005). Voluntary consent was required of the respondents before participation in the research. In addition, the participants were not bound by any obligation towards the research, and they were reminded that they may withdraw from participation at any time without penalty. They could also withdraw any information that they had provided while the research progresses without giving any reason (Rugg & Petre 2007). Participants were asked to sign the research consent form to indicate that they had read and understood the information sheet describing the research. They also had to indicate that they had agreed to participate in the research, and consent to publication of the results of the research on the understanding that they were not individually identified in any report of the project. Participants were also provided with the researcher’s university contact details, and were made aware that they may contact the researcher with questions or concerns about the research. They were also reminded that the questionnaire responses were anonymous.

The collected responses were kept confidential as per the university’s policy on academic integrity. For ensuring the secure storage of data, it was essential for the researcher not to make personal use of the collected data and keep the information in the secured database. The personal data of individual participants was not identified in the research and participants were assured that the data collected from them would be used solely for the purposes of the research. The information would not be provided to third party for any reason. With the aim
of addressing these ethical issues, the survey respondents were informed about the main concerns of the research study and the key rationale behind organising the survey process prior to conducting the actual survey.

Approval to conduct research with human subjects was granted for this study by the Human Research Ethics Committee of the University of Canberra. This study was subject to process which involved reviewing primary ethical issues for humans in accordance with the national statement on ethical conduct in research involving humans and the policies of the University of Canberra. Confidentiality procedures complied with the University of Canberra’s policy for responsible research practice.

The questionnaires were anonymous and the participants’ privacy was protected as far as possible. The information sheets and consent forms explained to participants that any information that they provided would be kept confidential. Measures were adopted to protect confidentiality during the data collection, storage analysis and publication stages. The data collected from participants was used in the aggregate. The responses of individual participants could not be identified, and any reports or publications from this research would provide only broad descriptions of the sample, for example, noting the average age and the proportion of participants in different banks. The methodology also required consent to have access to all data sources and to consider any related ethical implications of the research. This research also provided references to prevent plagiarism, and avoid any misleading or false reporting of research findings.

5.12 Conclusion

This chapter has presented the research objectives and the research questions that were informed by the extant literature. There was an exploration of the most appropriate approaches that may be used to answer the research questions. It was decided to choose a mixed method by employing both qualitative and quantitative approaches. There were several reasons for this choice and these reasons were discussed. This study used questionnaire survey and unstructured interviews. The sample for each method, as well as their administration and data analyses have been presented and discussed.
Chapter 6 – Description of Results

6.1 Introduction

This chapter investigates the different perceptions of professionals, managers and key players in the UAE concerning the suitability of the IFRS and AAOIFI accounting standards to Islamic banks. The chapter will therefore present the respondents’ opinions on this issue as well as other related issues such as, comparing the IFRS and AAOIFI accounting standards. The aim of this chapter is to provide a general picture of the findings of both the questionnaire survey and interviews, while the next chapter will explore the combined results of the questionnaires and interviews, including discussions underpinned by the theoretical framework and prior literature. This chapter is based on an analysis of the questionnaires returned by professionals and managers in the Islamic banking sector. A detailed analysis of the findings of the unstructured interviews is conducted with the aim of gaining deeper insights into important issues relating to the suitability of the IFRS and AAOIFI accounting standards, to the UAE. Interviews were conducted with managers and members of the Fatwa and Shariah Supervisory Board in the Islamic banking sectors, and members of the board of trustees of AAOIFI.

The chapter is organised as follows. First is the analysis of the completed questionnaires results, starting with a demographic and professional profile of the respondents, then the perceptions of respondents concerning Islamic banking in the UAE. Among these perceptions those are relating to the adoption of IFRS, a comparison between the IFRS and AAOIFI, and the potential adoption of AAOIFI accounting standards. This is followed by considerations of questionnaire reliability and validity testing. Second is the analysis of the unstructured interviews including background on the interviewees, followed by the interviewees’ perceptions concerning the reasons for the introduction of Islamic accounting standards in the UAE. This will be written together with interviewees’ perceptions of the initial efforts made to introduce Islamic accounting standards in the UAE, the problems and difficulties encountered with IFRS. The study will also comment about the suggestions for solving these problems, and the identification of key parties involved in the implementation of Islamic accounting standards in the UAE.

The findings in this chapter will inform later analysis and discussion in greater depth in order to answer the research questions.
6.2 Analysis of questionnaires

A comprehensive questionnaire survey was distributed to professionals and managers across the surveyed Islamic banks. This section reports on the quantitative findings of those questionnaire surveys. These findings will be further deconstructed in the qualitative analysis. The questions in the questionnaire were constructed and scored differently. Thus, the analysis for each question has been treated separately, and the next chapter will present the overall discussion of results and conclusions. Respondents answered some of the closed questions answered by choosing the most appropriate response or by expressing a view as to whether someone agreed or not with the proposition expressed. Other closed questions in the questionnaire were answered by scoring on a Likert scale (1 = strongly agree to 5 = strongly disagree) or other relevant descriptors also using a five-point scale. The results of these questions were reported in terms of the degree of agreement or disagreement, the mean responses and the standard deviations. The open-ended questions in the questionnaires were analysed by consolidating and categorising the various opinions expressed.

6.2.1 Demographic and professional profiles

The demographic profile of respondents to the questionnaire survey was structured on considerations of respondents’ education and work experience, as well as gender and age. Employment information collected included the number of years involved in their current employment and the job title. Each of these areas is briefly discussed below.

6.2.1.1 Demographic profile of respondents

There were 52 respondents included in this questionnaire survey. Figure 6.1 shows the distribution of the respondents by the four Islamic banks included in the questionnaire survey: the Dubai Islamic bank (DIB) accounted for 15 respondents, representing 29% of total respondents; the Abu Dhabi Islamic bank (ADIB) accounted for 13 respondents, representing 25% of total respondents; the Al Hilal bank (AHB) and the Emirates Islamic bank (EIB) each accounted for 12 respondents representing 23% of total respondents attributable to each bank.
6.2.1.2 Age group of respondents

Figure 6.2 shows the age distribution of the 52 respondents to the questionnaire survey. The greatest number, 19 respondents, were in the age group 30 to 39 years, with another 16 respondents in the age group 40 to 49 years; a further 10 respondents were below 29 years of age and 7 respondents were above 50 years.
6.2.1.3 Gender of respondents

Figure 6.3 shows the distribution of survey respondents by gender. Of 52 respondents, 44 were males, representing 85% of the sample, and 8 were females representing 15% of the sample.

![Figure 6.3: Distribution of survey respondents by gender](image)

**Q.2 What is your gender?**

6.2.1.4 Education background of respondents

Figure 6.4 shows the distribution of survey respondents by level of education attained. The greatest number of respondents held a master’s degree (58%) followed by those holding a bachelor’s degree (21%); 8% of respondents held a PhD degree. The remaining 13% of respondents were in possession of a professional qualification and of these, 71% hold either a CPA or equivalent professional certificate from another country, and 29% hold a Certification of Islamic Professional Accountant (CIPA) issued by the AAOIFI.
6.2.1.5 Employment experience of respondents

Figure (6.6) portrays the length of employment experience in financial institutions by survey respondents. A majority of respondents (87%) had more than five years’ experience in relevant employment, whilst 10% of these had more than 15 years’ experience.
6.2.1.6 Job categories of respondents

The generalised employment categorisation of the survey respondents is portrayed in Figure 6.7. This graph shows that finance professionals accounted for 56% of the survey respondents. The professional category includes such roles as the foreclosure specialists, financial planners, auditors, loan officers, trust investment officers, security traders, loss mitigation officers, fraud prevention specialists, portfolio and equity officers, and senior consultants. The second group of respondents (46%) includes management ranks such as branch managers, regional managers, portfolio managers and lending managers as well as the heads of treasury & investment operations.
6.2.2 Islamic banking in the UAE, in the context of IFRS adoption

The purpose of this section is to find the answers to two research questions:

- What are the user needs for accounting information in the UAE Islamic banks?
- Do Islamic banks in the UAE need a corresponding alternative set of accounting standards rather than the currently adopted IFRS?

For both these questions, the perspectives of both professionals and managers in each of the four selected Islamic banks were provided by survey respondents. The following sections describe the findings.

6.2.2.1 Perceptions of Islamic banking services

Figure 6.8 shows the perceptions of respondents related to how Islamic banking services could be differentiated from those of conventional banking. The respondents agreed overall that interest rate/profit represented the main differentiating factor between Islamic and non-Islamic Banking Services, accounting for 42 respondents (81%). Only four respondents favoured convenience as a key point of differentiation, whereas, three respondents opted for cost of banking. Interestingly, three respondents indicated there was no differentiating factor for Islamic Services.
Survey respondents were asked to nominate their perceptions concerning the reason why customers chose to do business with Islamic banks. The principal reason proposed was religion (42% of respondents), followed by culture (35%). Ethical reasons accounted for 15% of respondents and the availability of cheap products accounted for the remaining respondents (8%).

Figure 6.9: Survey respondents’ perceptions: Why customers chose Islamic banks
6.2.2.3 Adoption of International Financial Reporting Standards (IFRS)

When asked about currently adopted accounting standards, all the survey respondents stated that their Islamic banks have adopted IFRS. Figure 6.10 reflects that outcome. It shows that 100% of respondents confirmed that Islamic banks in the UAE have adopted IFRS.

6.2.2.4 Practicality of IFRS for developing countries

Whilst the IFRS were created to meet the needs of developed countries, they were also generally considered applicable in developing countries (Hameed 2000). Figure 6.11 shows that 67% of the survey respondents disagreed with the proposition that the IFRS were impractical for developing nations. Conversely, the remaining 33% of survey respondents agreed with the proposition that the IFRS were impractical for developing nations.

Figure 6.10: Adoption of IFRS

Q.8 Why in your opinion have customers chosen Islamic Banks?

Q.9 Does your Islamic bank adopt IFRSs?

Current Adoption

<table>
<thead>
<tr>
<th>Frequency</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>52</td>
<td></td>
<td></td>
</tr>
<tr>
<td>0</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Reasons for choosing Islamic Banks

<table>
<thead>
<tr>
<th>Frequency</th>
<th>Religion (42.30%)</th>
<th>Culture (34.62%)</th>
<th>products (15.38%)</th>
<th>Ethical (7.70%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>22</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>18</td>
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</table>
6.2.2.5 Perceptions of characteristics of the IFRS

6.2.2.5.1 IFRS and characteristics of understandability and comparability

Figure 6.12 shows that 79% of respondents perceived the IFRS to have characteristics of understandability and comparability in the context of their Islamic banks, while 21% disagreed with this proposition.

6.2.2.5.2 Perceptions of the characteristics of IFRS

This section reports on the survey responses to statements made about the characteristics of IFRS, in particular those of comprehensiveness, understandability, its implementation at...
reasonable cost and whether IFRS allows for the exercise of appropriate professional judgment. Respondents recorded their responses in terms of a Likert scale ranging from 1 = ‘Strongly Agree’ to 5 = ‘Strongly Disagree’. Table 6.1 shows descriptive statistics relating to survey responses to Questions 12A to 12D.

Question 12A asked whether the standards provided by the IFRS are comprehensive. Table 6.1 presents the accumulated responses yielded a mean of 2.71 with standard deviation 0.915 and median 2.50. Almost half of the respondents fall within the category of ‘somewhat agree’, and two-thirds (68.7%) of all respondents were distributed about the mean in the range from 1.8 to 3.6, indicating a tendency to agree with the proposition that the IFRS standards provided comprehensiveness. The measures of skewness and kurtosis were 0.458 and -0.628, respectively. The histogram showed an approximate normal distribution. The box plot excluded case number 24 as an outlier.

Question 12B asked whether the standards provided by the IFRS are understandable. Table 6.1 presents the accumulated responses yielded a mean of 2.56 with standard deviation 0.938 and median 2.0. The response distribution was very similar to that for Question 12A, with a slightly stronger inclination to agreement with the Question 12B proposition. The measures of skewness and kurtosis were 0.717 and 0.346, respectively. The histogram showed an approximate normal distribution. The box plot excluded case numbers 3 and 24 as outliers.

Question 12C asked whether the standards provided by the IFRS can be implemented at a reasonable cost. Table 6.1 presents the accumulated responses yielded a mean of 2.73 with standard deviation 0.843 and median 3. Half the survey responses could be categorised as ‘neutral’ and two-thirds (68.7%) (Mean ± SD) of all responses were distributed around the mean in the range from 1.9 to 3.6. This indicates a general uncertainty (neutrality) with the Question 12C proposition. The measures of skewness and kurtosis were 0.350 and 0.969 respectively. The histogram showed an approximate normal distribution. The box plot excluded case numbers 12 and 24 as outliers.

Question 12D asked whether the standards provided by the IFRS allowed for appropriate level professional judgement to be exercised. Table 6.1 presents the accumulated responses yielded a mean of 2.56 with standard deviation 0.826 and median 3. Two-thirds of the responses (Mean ± SD) were distributed in the range of 1.7 to 3.4. This indicates a slightly greater tendency to agreement with the Question 12D’s proposition than has been evident
amongst the other Question 12 sub-questions. The measures of skewness and kurtosis were 0.351 and 0.567, respectively with a leptokurtic distribution not evident heretofore in Question 12. The histogram showed an approximate normal distribution, though leptokurtic compared to other Question 12 sub-questions. The box plot excluded case number 24 as an outlier.

Table 6.1: Descriptive statistics for aggregated survey responses to questions 12a to 12d

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 12A Statistic</th>
<th>Q 12B Statistic</th>
<th>Q 12C Statistic</th>
<th>Q 12D Statistic</th>
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<td></td>
<td>Std. Error</td>
<td>Std. Error</td>
<td>Std. Error</td>
<td>Std. Error</td>
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<tr>
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<td>2.56</td>
<td>2.73</td>
<td>2.56</td>
</tr>
<tr>
<td>Median</td>
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<td>2.00</td>
<td>3.00</td>
<td>3.00</td>
</tr>
<tr>
<td>Std. Dev.</td>
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<td>.938</td>
<td>.843</td>
<td>.826</td>
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<td>Range</td>
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<td>.351</td>
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<td>Kurtosis</td>
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<td>.346</td>
<td>.969</td>
<td>.567</td>
</tr>
</tbody>
</table>

6.2.2.6 Perceptions of factors that influenced the adoption of IFRS by Islamic banks

This section reports on the answers to the closed questions asked of respondents about their perceptions of factors that influenced the adoption of IFRS by their Islamic bank employer. Respondents recorded their responses in terms of a Likert scale which ranged from 1 = ‘Strongly Agree’ to 5 = ‘Strongly Disagree’. Table 6.2 shows the descriptive statistics of responses to Questions 13A to 13D.

Question 13A asked about the extent to which the Bank’s growth greatly influenced the adoption of IFRS. Table 6.2 presents the accumulated responses yielded a mean of 3.19 with standard deviation 1.067 and median 3.0. The responses yielded a bi-modal distribution with approximately two-thirds of all responses (Mean ± SD) widely distributed about the mean in the range from 2.1 to 4.3. This indicates a tendency towards mild disagreement among the respondents with the Question 13A proposition. The measures of skewness and kurtosis were -0.199 and -1.005, respectively. The histogram exhibits a bi-polar distribution and the box plot shows a near normal distribution of wide spread, but with no outliers.
Question 13B asked about the extent to which the legal system influenced the Bank’s adoption of IFRS. Table 6.2 presents the accumulated responses yielded a mean of 2.12 with standard deviation 1.114 and median 2.0. About one-third of the survey responses were scored as ‘strongly agree’ and another 30% were scored as ‘moderately agree’. Two-thirds of all responses (Mean ± SD) were concentrated in the range from 1.0 to 3.2. This indicates reasonably strong agreement with the Question 13B’s proposition. The measures of skewness and kurtosis were 0.826 and 0.037, respectively. The histogram exhibits an asymmetric distribution and the box plot shows a strongly skewed distribution with no outliers.

Question 13C asked about the extent to which the external environment (e.g. World Bank and IMF) greatly influenced the Bank’s adoption of IFRS. Table 6.2 presents the accumulated responses yielded a mean of 2.50 with standard deviation 1.094 and median 2.0. Two-thirds of all responses (Mean ± SD) were distributed about the mean in the range 1.4 to 3.6, indicating a tendency among respondents to mildly agree with the Question 13C’s proposition. The measures of skewness and kurtosis were 0.655 and -0.175 respectively. The histogram shows a near normal distribution as did the box plot, after excluding cases 3, 41 and 49 as outliers.

Question 13D asked about the extent to which the existence of the capital market greatly influenced the Bank’s adoption of IFRS. Table 6.2 presents the accumulated responses which yielded a mean of 3.52 with standard deviation 0.980 and median 4. Forty-six per cent of the responses scored 4 (‘somewhat disagree’) and two-thirds of all responses (Mean ± SD) were distributed about the mean in the range 2.5 to 4.5. This indicates a strong tendency to a moderate disagreement with the Question 13D proposition. The measures of skewness and kurtosis were -0.316 and -0.931 respectively. The histogram and box plot shows a near normal distribution with no outliers.

Table 6.2: Descriptive statistics for aggregated survey responses to questions 13a to 13d

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 13A Statistic</th>
<th>Std. Error</th>
<th>Q 13B Statistic</th>
<th>Std. Error</th>
<th>Q 13C Statistic</th>
<th>Std. Error</th>
<th>Q 13D Statistic</th>
<th>Std. Error</th>
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<tbody>
<tr>
<td>Mean</td>
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<td>.148</td>
<td>2.12</td>
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<td>2.50</td>
<td>.152</td>
<td>3.52</td>
<td>.136</td>
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<td>Median</td>
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<td>2.00</td>
<td></td>
<td>4.00</td>
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<td>Std. Dev.</td>
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<td>1.114</td>
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<td>1.094</td>
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<td>.980</td>
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<td>4</td>
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<td>4</td>
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<td>3</td>
<td></td>
</tr>
</tbody>
</table>
6.2.2.7 Perceptions of merits and demerits of adopting IFRS by Islamic banks

Survey respondents were asked open-ended questions about their perceptions of the advantages (merits) and disadvantages (demerits) of adopting IFRS into their Islamic banks. These open-ended questions gave respondents the opportunity to express their opinions in depth, as desired. Overall advantages and disadvantages are grouped into themes and presented separately in Tables 6.3 and 6.4. Table 6.3 shows that the majority of survey respondents believed that the greatest benefits in adopting IFRS would be the ease of comparability of financial statements with other financial institutions, uniformity and consistency with the reporting requirements of other conventional financial institutions, and compliance with regulatory requirements.

Furthermore, as can be seen from Table 6.3, respondents also believed that the adoption of IFRS facilitated the growth of foreign direct investment in the UAE. Respondents found this to be the second greatest benefit resulting from the adoption of IFRS in their Islamic banks. The survey respondents also assumed that one of the greatest benefits would be that Islamic banks in the UAE would have access to better and enlarged sources of finance from international organizations such as World Bank and IMF which rely on the use of IFRS as a condition for granting loans. Some respondents believed that IFRS allowed users of financial statements to increase the ability of the entity to generate cash and cash equivalents in the future.

Moreover, other respondents also suggested that the benefits are likely to include ease of establishment for foreign banks in the UAE as they do not have to bear the additional cost of preparing accounts according to different accounting practices. Further discussion of these merits will be also presented in the next chapter.
Table 6.3: Descriptive statistics relating to merits of adopting IFRS by Islamic banks

<table>
<thead>
<tr>
<th>Overall advantages</th>
<th>Frequency</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Comparability of financial statements.</td>
<td>26</td>
<td>1</td>
</tr>
<tr>
<td>Facilitate foreign investments.</td>
<td>21</td>
<td>2</td>
</tr>
<tr>
<td>International organizations rely on IFRS.</td>
<td>18</td>
<td>3</td>
</tr>
<tr>
<td>Enhance the reporting of Islamic banks.</td>
<td>15</td>
<td>4</td>
</tr>
<tr>
<td>Help the users of financial statements.</td>
<td>15</td>
<td>5</td>
</tr>
<tr>
<td>Reduce information asymmetry and relevance.</td>
<td>12</td>
<td>6</td>
</tr>
<tr>
<td>Establishment of foreign Islamic banks.</td>
<td>9</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>116</strong></td>
<td></td>
</tr>
</tbody>
</table>

**Q.14 What would you say are the merits of adopting IFRS by your Islamic bank?**

On the other hand, Table 6.4 showed that the majority of survey respondents indicated that the greatest disadvantage of IFRS adoption would be the conflict with Islamic principles for some Islamic products. Some respondents believed that IFRS violated the essence of Shariah principles by emphasising the concept of time value of money and interest.

The respondents also suggested that the complete adoption of IFRS is nearly impossible as it cannot cater for Shariah-compliant transactions. Respondents illustrated that Islamic banks have transactions that could not sustain the application of the accounting concepts of IFRS as it was skewed towards conventional banking practices and does not reflect the Islamic financial principles of Islamic financial institutions. IFRS have been drafted to account for conventional products and can be adopted only in part by Islamic banks in the UAE. Moreover, other respondents also said that the IFRS are more likely to challenge the cultural practices and beliefs of the UAE. Further discussion of these demerits will be also presented in the next chapter.

Table 6.4: Descriptive statistics relating to demerits of adopting IFRS by Islamic banks

<table>
<thead>
<tr>
<th>Overall disadvantages</th>
<th>Frequency</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Challenge cultural practices.</td>
<td>41</td>
<td>1</td>
</tr>
<tr>
<td>Existence of interest rate.</td>
<td>34</td>
<td>2</td>
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<tr>
<td>Conflicts with Islamic principles.</td>
<td>23</td>
<td>3</td>
</tr>
<tr>
<td>Utilizing Shariah terminologies in the standards of accounting.</td>
<td>19</td>
<td>4</td>
</tr>
<tr>
<td>Islamic banks have transactions that could not apply IFRS.</td>
<td>16</td>
<td>5</td>
</tr>
<tr>
<td>The official language of Shariah principles is Arabic.</td>
<td>4</td>
<td>6</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>137</strong></td>
<td></td>
</tr>
</tbody>
</table>

**Q.15 What in your opinion are the demerits of adopting IFRS by your Islamic bank?**
6.2.2.8 Perceptions of Islamic banking facilities

This section indicates the perceptions of respondents relating to how their Islamic banking facilities could be ranked in terms of eight different facilities provided by Islamic banks. Respondents recorded their responses in terms of a Likert scale ranging from 1 = ‘Highly Satisfied’ to 5 = ‘Highly Dissatisfied’. Table 6.5 shows descriptive statistics relating to Questions 16A to 16D, and Table 6.6 shows descriptive statistics relating to responses of Questions 16E to 16H.

Question 16A asked the respondent to rank their Islamic bank facilities in terms of the provision of interest-free loans. Table 6.5 presents the accumulated responses yielded a mean of 3.39 with standard deviation 1.069 and median 3.0. About two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.3 to 4.5, indicating some dissatisfaction with the Bank’s provision of interest-free loans. The measures of skewness and kurtosis were -0.237 and -0.569, respectively. The histogram shows a near normal distribution and the box plot, after excluding case numbers 24 and 49, reflected the tendency to general dissatisfaction reflected in the survey responses.

Question 16B asked the respondent to rank their Islamic Bank facilities in terms of the provision of Islamic products and services. Table 6.5 presents the accumulated responses yielded a mean of 2.67 with standard deviation 0.923 and median 3.0. About two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.75 to 3.6, indicating a degree of satisfaction with the Bank’s provision of Islamic products and services. The measures of skewness and kurtosis were -0.237 and -0.569 respectively. The histogram shows a near normal distribution and the box plot, after excluding case number 51 as an outlier reflected the general tendency to satisfaction reflected in the survey responses.

Question 16C asked the respondents to rank the operation of their Islamic Bank in terms of Islamic law and principles. Table 6.5 presents the accumulated responses yielded a mean of 3.42 with standard deviation 0.801 and median 3.50. About two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.6 to 4.2, indicating a mild dissatisfaction with the Bank’s operations in terms of Islamic law and principles. The measures of skewness and kurtosis were -0.216 and -0.479 respectively. The histogram and box plot shows a near normal distribution with no outliers.
Question 16D asked the respondents to rank their Islamic Bank in terms of the strength of their Global Network. Table 6.5 presents the accumulated responses yielded a mean of 2.65 with standard deviation 0.789 and median 3.0. About two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.86 to 3.44, indicating a mild satisfaction with the Bank’s operations in terms of the strength of their Global Network. The measures of skewness and kurtosis were -0.035 and -0.386, respectively. The histogram showed a near normal distribution and the box plot contained no outliers.

Table 6.5: Descriptive statistics for aggregated survey responses to questions 16a to 16d

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 16A Statistic</th>
<th>Std. Error</th>
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<th>Std. Error</th>
<th>Q 16C Statistic</th>
<th>Std. Error</th>
<th>Q 16D Statistic</th>
<th>Std. Error</th>
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<tr>
<td>Mean</td>
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<td>3.42</td>
<td>.111</td>
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<td>.109</td>
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<tr>
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<td>.650</td>
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<td>.650</td>
<td>-.386</td>
<td>.650</td>
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</table>

Q.16 Please rank your Islamic bank facilities for following items...

Question 16E asked the respondents to rank their Islamic bank facilities in terms of the sufficiency of time for transactions. Table 6.6 presents the accumulated responses yielded a mean of 2.40 with standard deviation 0.934 and median 2. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.5 to 3.3, indicating general satisfaction with the bank’s performance with regard to transaction time. The measures of skewness and kurtosis were 0.291 and -0.022, respectively. The histogram showed a near normal distribution as did the box plot after eliminating case number 51 as an outlier.

Question 16F asked the respondents to rank their Islamic bank facilities in terms of competitive product offerings. Table 6.6 presents the accumulated responses yielded a mean of 2.56 with standard deviation 0.998 and median 2.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.6 to 3.6, indicating satisfaction with the bank’s performance with regard to competitive product offerings. The measures of skewness and kurtosis were 0.511 and -0.087, respectively. The histogram showed a near normal distribution as did the box plot after eliminating case numbers 51 and 29 as outliers.
Question 16G asked the respondents to rank their Islamic bank facilities in terms of overdraft privileges on current account. Table 6.6 presents the accumulated responses yielded a mean of 2.54 with standard deviation 0.874 and median 2.50. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.7 to 3.4, indicating a mild degree of satisfaction with the bank’s provision of overdraft privileges on current account. The measures of skewness and kurtosis were 0.337 and 0.231, respectively. The histogram showed a near normal distribution as did the box plot after eliminating case number 51 as an outlier.

Question 16H asked the respondents to rank their Islamic bank facilities in terms of lower service charges. Table 6.6 presents the accumulated responses yielded a mean of 2.77 with standard deviation 0.877 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.9 to 3.6, indicating a tendency to satisfaction with the bank’s provision of lower service charges. The measures of skewness and kurtosis were 0.296 and -0.413, respectively. The histogram showed a near normal distribution, as did the box plot after eliminating case number 29 as an outlier.

Table 6.6: Descriptive statistics for aggregated survey responses to questions 16e to 16h

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<th>Q 16F</th>
<th>Std. Error</th>
<th>Q 16G</th>
<th>Std. Error</th>
<th>Q 16H</th>
<th>Std. Error</th>
</tr>
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<tr>
<td>Mean</td>
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<td>2.56</td>
<td>.138</td>
<td>2.54</td>
<td>.121</td>
<td>2.77</td>
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<tr>
<td>Median</td>
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<td>.133</td>
<td>2.00</td>
<td>.138</td>
<td>2.50</td>
<td>.121</td>
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<td>.122</td>
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<td>.877</td>
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<td>-.413</td>
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6.2.2.9 Perceptions of the content of financial reports by Islamic banks

This section indicates the perceptions of survey respondents about the inclusion of four specific elements in the financial reports of Islamic banks. Respondents recorded their responses in terms of a Likert scale ranging from 1 = ‘Fully Included’ to 5 = ‘Not Included’. Table 6.7 shows descriptive statistics of responses to Questions 17A to 17D.
Question 17A asked respondents to what extent the financial reports of the Islamic bank included full disclosure of any and all relevant information which facilitates the users’ economic and religious decision making. Table 6.7 presents the accumulated responses yielded a mean of 3.54 with standard deviation 0.874 and median 4.0. Three-quarters of all respondents were concentrated and fairly evenly distributed amongst scores 3 (‘Neutral’) and 4 (‘Somewhat not included’), indicating a mild tendency to believe that the relevant information was not fully disclosed. The measures of skewness and kurtosis were -0.030 and -0.608, respectively. The histogram revealed an approximate normal distribution and the box plot was without outliers.

Question 17B asked respondents to what extent the financial reports of the respondent’s Islamic bank included financial instruments not related to interest. Table 6.7 presents the accumulated responses yielded a mean of 2.81 with standard deviation 0.793 and median 3.0. Eighty per cent of all respondents were concentrated and evenly distributed amongst scores 2 (‘Somewhat Included’) and 3 (‘Neutral’), indicating a mild tendency to believe that financial instruments unrelated to interest were at least partially included. The measures of skewness and kurtosis were 0.608 and -0.383, respectively. The histogram revealed an approximate normal distribution, as did the box plot after eliminating case number 33 as an outlier.

Question 17C asked respondents to what extent the financial reports of the respondent’s Islamic bank included information that enables Muslims to determine the amount of Zakat. Table 6.7 presents the accumulated responses yielded a mean of 4.08 with standard deviation 0.813 and median 4.0. Almost half the survey responses were scored 4 (‘Somewhat not Included’), and two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 3.3 to 4.9. This indicates strong support for the notion that relevant and sufficient information related to Zakat is not included in financial reports. The measures of skewness and kurtosis were -0.600 and -0.069, respectively. The histogram revealed an approximate normal distribution as did the box plot after eliminating case numbers 3 and 5 as outliers.

Question 17D asked respondents to what extent the financial reports of their Islamic bank included the disclosure of paid interest, the reasons for this payment and the steps which should be taken to avoid such interest in the future. Table 6.7 presents the accumulated responses yielded a mean of 3.65 with standard deviation 0.653 and median 4.0. Ninety per cent of all responses were distributed unequally across scores 3 (‘Neutral’) and 4 (‘Somewhat
not Included’), and two-thirds (Mean ± SD) were distributed about the mean in the range 3.0 to 4.3, indicating strong support for the notion that the disclosure of interest, the reasons, and future actions were not necessarily included. The measures of skewness and kurtosis were 0.056 and -0.200, respectively. The histogram showed an approximate normal distribution and the box plot revealed no outliers.

Table 6.7: Descriptive statistics for aggregated survey responses to questions 17a to 17d

<table>
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<th>Variables</th>
<th>Q 17A</th>
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<td>Std. Error</td>
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<td>.608</td>
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<td>Kurtosis</td>
<td>-.608</td>
<td>.650</td>
<td>-.383</td>
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</table>

Q.17 To what extent do you think that the financial reports of your Islamic bank includes the following elements...

6.2.2.10 Comparison of financial reporting by Islamic banks and commercial banks

Survey respondents were asked about their perceptions of Islamic banks financial reporting practices comparing with those of commercial banks. Respondents recorded their responses in terms of a Likert scale graduated from 1 = ‘Strongly Agree’ to 5 = ‘Strongly Disagree’. Table 6.8 shows the descriptive statistics of responses to Questions 18A and 18B.

Question 18A asked respondents to what extent they agreed that Islamic bank financial reports should differ from those of commercial banks, because the readers of Islamic bank reports have different needs. Table 6.18 presents the accumulated responses yielded a mean of 2.75 with standard deviation 0.926 and median 3.0. Two-thirds of all responses (Mean ± SD) were distributed about the mean in the range from 1.8 to 3.7, thus displaying a tendency to agreement with the proposition of Question 18A. The measures of skewness and kurtosis were 0.221 and -0.577, respectively. The histogram shows an approximate normal distribution, as reflected in the box plot after eliminating case 19 as an outlier.
Question 18B asked respondents to what extent they agreed that Islamic bank financial reports should differ from those of commercial banks, because Islamic Banks exist to produce Islamic financial services. Table 6.18 presents the accumulated responses yielded a mean of 2.50 with standard deviation 0.874 and median 2.0. Two-thirds of all responses (Mean ± SD) were distributed about the mean in the range from 1.6 to 3.4, thus displaying a mild agreement with the proposition of Question 18B. The measures of skewness and kurtosis were 0.091 and -0.611, respectively. The histogram shows an approximate normal distribution, reinforced in the box plot with no outliers.

Table 6.8: Descriptive statistics of aggregated survey responses to questions 18a and 18b

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 18A</th>
<th>Std. Error</th>
<th>Q 18B</th>
<th>Std. Error</th>
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<tr>
<td>Mean</td>
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<td>2.50</td>
<td>.121</td>
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<td>2.00</td>
<td></td>
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<tr>
<td>Std. Deviation</td>
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<td>.874</td>
<td></td>
<td></td>
</tr>
<tr>
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<tr>
<td>Range</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Skewness</td>
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<td>.330</td>
<td>.091</td>
<td>.330</td>
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<tr>
<td>Kurtosis</td>
<td>-.577</td>
<td>.650</td>
<td>-.611</td>
<td>.650</td>
</tr>
</tbody>
</table>

Q.18 Please indicate the extent to which you agree or disagree with the following statements. Islamic banks financial reporting should be different from commercial banks reporting because...

6.2.3 Comparison between IFRS and AAOIFI

The purpose of this section is to contribute to answering the research questions: ‘What are the main differences and similarities between the applications of AAOIFI Accounting Standards and the IFRS?’ and ‘Which system can better satisfy users’ needs?’ by evaluating the perspectives of survey respondents.

6.2.3.1 Comparing the measurement of investment property under IFRS and AAOIFI

The IFRS allows the use of fair value measurement of investment property, but under AAOIFI standards it must be measured at historical cost. Questionnaire survey Question 19 asks respondents to select one of four alternative statements that best reflects their viewpoint, namely, (A) that the historical cost measurement provides accurate information for Zakat, (B) that the fair value measurement provides accurate information for Zakat, (C) that either the historical cost measurement or the fair value measurement provides accurate information for
Zakat and (C) that neither the historical cost measurement nor the fair value measurement provides accurate information for Zakat.

**Figure 6.13: Measurement of investment property under IFRS and AAOIFI**

Figure 6.13 shows the frequency of response to each statement by means of a Column Chart. Thirty-one respondents (59.6%) considered the use of the historical cost measurement in investment property provides useful accurate information for Zakat purposes (coded A on the chart). Five respondents (9.6%) considered the use of the fair value measurement in investment property provides useful accurate information for Zakat purposes (coded B). Fourteen respondents (26.9%) considered that either the use of historical cost measurement or the use of fair value measurement in investment property provides useful accurate information for Zakat purposes (coded C), whilst only two respondents (3.9%) considered that neither the use of historical cost measurement nor the use of fair value measurement in investment property provides useful accurate information for Zakat purposes (coded D).

**6.2.3.2 Perceptions of IFRS and AAOIFI standards: time consuming implementation**

Figure 6.14 shows the column chart of the respondents’ perceptions of relative time consumption between the implementation of IFRS and AAOIFI standards. Thirty-eight respondents (73.1% of the sample) felt that AAOIFI standards would be more time consuming of implementation as compared to the IFRS (coded A on the chart), whilst five respondents (9.6%) felt that IFRS would be more time consuming of implementation than AAOIFI standards (coded B). Six respondents (11.5%) expressed the view that neither IFRS nor AAOIFI would be time consuming of implementation (coded D), whereas, three
respondents (5.8%) thought that both IFRS and AAOIFI would be time consuming of implementation (coded C).

![Figure 6.14: Time consuming implementation of IFRS and AAOIFI standards](image)

**Q.20 If you compare IAS to the AAOIFI standards, which one would be more time consuming of implementation?**

Figure 6.14: Time consuming implementation of IFRS and AAOIFI standards

### 6.2.3.3 Perceptions of preferences concerning implementation of IFRS vs. AAOIFI accounting standards

Figure 6.15 shows the column chart of the respondents’ preferences regarding the choice of implementing IFRS or AAOIFI standards. Thirty-two respondents (61.5% of the sample) preferred the implementation of IFRS (coded A on the chart); whilst six respondents (11.6%) preferred the implementation of AAOIFI (coded B). Thirteen respondents (25.0%) thought that both IFRS and AAOIFI standards are preferable to be implemented (coded C), whilst one respondent (1.9%) believed that neither IFRS nor AAOIFI are preferable to be implemented (coded C).
6.2.3.4 Reasons for respondents’ preferences: implementation of IFRS and AAOIFI standards

Survey respondents were invited to respond to an open-ended question (Q.22 I): ‘What are the main reasons for your preferences?’ (as articulated in Questions 19 to 21) and to express in greater depth (Q.22 II) the reasons for their preferences regarding the implementation of IFRS, AAOIFI standards, or other preferences. Overall reasons are grouped into themes and presented in Table 6.9. Further discussion of these reasons will be presented in the next chapter.
Table 6.9: Descriptive statistics of the reasons for respondents’ preferences regarding the implementation of IFRS and AAOIFI standards

<table>
<thead>
<tr>
<th>Reasons – IFRS preferences</th>
<th>Frequency</th>
<th>Rank</th>
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</thead>
<tbody>
<tr>
<td>Providing credibility all over the world.</td>
<td>29</td>
<td>1</td>
</tr>
<tr>
<td>International organizations rely on IFRS.</td>
<td>26</td>
<td>2</td>
</tr>
<tr>
<td>Comparability of financial statements.</td>
<td>23</td>
<td>3</td>
</tr>
<tr>
<td>Facilitates Islamic banking investments.</td>
<td>13</td>
<td>4</td>
</tr>
<tr>
<td>Consistent with regulatory requirements.</td>
<td>11</td>
<td>5</td>
</tr>
<tr>
<td>Establishment of foreign Islamic banks.</td>
<td>8</td>
<td>6</td>
</tr>
<tr>
<td>Its financial concepts based on calculations that prevent human bias.</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td><strong>112</strong></td>
<td></td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Reasons – AAOIFI preferences</th>
<th>Frequency</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Representing the correct picture of Islamic products.</td>
<td>22</td>
<td>1</td>
</tr>
<tr>
<td>Compatible with beliefs and culture of Islamic countries.</td>
<td>21</td>
<td>2</td>
</tr>
<tr>
<td>Capture the Islamic financial transactions.</td>
<td>18</td>
<td>3</td>
</tr>
<tr>
<td>Abide by the principals of <em>Shariah</em>.</td>
<td>15</td>
<td>4</td>
</tr>
<tr>
<td>More acceptable to Islamic countries.</td>
<td>13</td>
<td>5</td>
</tr>
<tr>
<td>Created for Islamic financial institutions.</td>
<td>5</td>
<td>6</td>
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<tr>
<td><strong>Subtotal</strong></td>
<td><strong>94</strong></td>
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<table>
<thead>
<tr>
<th>Reasons – Other preferences</th>
<th>Frequency</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>The adoption of both IFRS and AAOIFI will tap global alliances.</td>
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<td>1</td>
</tr>
<tr>
<td>Local accounting standards are the most suitable for satisfying users’ needs.</td>
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<td>2</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
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<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>209</strong></td>
<td></td>
</tr>
</tbody>
</table>

Q.22 What are the main reasons for your preferences?

6.2.4 Potential adoption of AAOIFI standards

The purpose of this section of Chapter 6 is to find survey responses which may answer the main research question: ‘What would be the impact of applying the AAOIFI Accounting Standards in the UAE Islamic banks?’. Also, to better clarify the key factors associated with the primary research question, this section tries to answer the subsidiary questions: ‘What are the underlying factors that may influence the adoption of AAOIFI Accounting Standards in the UAE Islamic banks, and which issues might act as barriers to their adoption?’ The responses from Section 4 of the questionnaire survey provide the perspectives of both professionals and managers in the selected Islamic banks regarding these research questions.
6.2.4.1 Perceptions of Islamic banks’ policy to converge with or adopt AAOIFI standards

When asked about their banks’ policy regarding convergence with, or adoption of, AAOIFI standards, the majority of survey respondents stated that their Islamic banks currently do not have plans for such convergence or adoption. Figure (6.16) shows that 38 respondents (73.1%) believed that their Islamic banks do not have plans to converge with, or adopt, AAOIFI standards (coded A). Just four respondents (7.7%) indicated that their Islamic bank will be converging with, or adopting, AAOIFI standards (coded B), and no respondents stated that their Islamic banks had already converged with, or adopted, AAOIFI standards (coded C). Ten respondents (19.2%) indicated that they don’t know whether their Islamic bank has a policy to converge with, or adopt, AAOIFI standards (coded D).

![Respondents' Perceptions](chart.png)

Q.23 Does your Islamic bank have a policy of convergence with or adopting AAOIFI Standards?

Figure 6.16: Respondents’ perceptions of Islamic banks’ policy to converge with or adopt AAOIFI standards

6.2.4.2 Perceptions of cost in time and resources for first-time adoption of AAOIFI standards by Islamic banks

Figure 6.17 shows the bar chart of the survey respondents’ perceptions of the cost of time and resources for the first-time adoption of AAOIFI standards by their Islamic banks. Seven respondents (13.46%) thought that the cost would be just time (coded A), while, 9 respondents (17.30%) expressed the view that the cost would be just resources (coded B). Thirty-one respondents (59.62%) thought that the cost would comprise both time and
resources (coded C). However, 5 respondents (9.62%) thought that neither time nor resources would be a cost incurred by their Islamic banks if adopted it AAOIFI Standards (coded D).

![Respondent's Perceptions](image)

**Q. 24** Do you think that the first time adoption of AAOIFI standards for your Islamic bank will cost the bank both with the time and resources?

**Figure 6.17:** Respondents’ perceptions of cost in time and resources for first-time adoption of AAOIFI standards by Islamic banks

### 6.2.4.3 Perceptions of benefits of AAOIFI standards for Islamic banks

The survey respondents were asked whether the benefits of AAOIFI standards for their Islamic banks in the later stages of implementation would outweigh the initial costs incurred. Figure 6.18 showed that 39 respondents (75%) reported that the later benefits of AAOIFI standards would not outweigh the initial costs incurred, whereas 13 respondents (25%) reported that the later benefits of AAOIFI standards would outweigh the initial costs incurred.
6.2.4.4 Possible outsourcing of implementation of AAOIFI

The survey respondents were asked whether their Islamic banks would implement AAOIFI standards unilaterally or outsource part of the task to auditors and analysts to complete the transition process. Figure 6.19 shows that 35 respondents (67.31%) said yes, that their banks would act independently in transitioning their Islamic Bank through the implementation of AAOIFI standards, whereas 17 respondents (32.69%) said no, indicating that they would outsource at least part of the transition tasks to auditors and analysts for completion.
6.1.4.5 Knowledge of Islamic ethical and legal aspects

The survey respondents were asked whether the application of AAOIFI standards for Islamic banks required an accountant to have knowledge of Islamic ethical and legal aspects. Figure 6.20 shows that 41 respondents 78.85% considered that accountants of Islamic banks should be required to have knowledge of Islamic ethical and legal aspects, whereas 11 respondents (21.15%) thought that it is not necessary that accountants of Islamic banks have knowledge of Islamic ethical and legal aspects.

![Respondents' Opinions](Figure 6.20: Is knowledge of Islamic ethical and legal aspects required?)

6.2.4.6 Quality of AAOIFI standards

Survey respondents were asked to rate the quality of four aspects of the AAOIFI. Respondents recorded their responses in terms of a Likert scale ranging from 1 = ‘Excellent’ to 5 = ‘Poor’. Table 6.10 shows the descriptive statistics for the responses to Questions 28A to 28D.

Question 28A asked respondents to rate the credibility of the AAOIFI standards. Table 6.10 presents the accumulated responses yielded a mean of 3.02 with standard deviation 0.960 and median 3.0. Ninety per cent of all the responses were fairly evenly distributed over scores 2, 3 and 4. Two-thirds (68.7%) (Mean ± SD) of all responses were distributed about the mean in the range from 2.1 to 4. This indicates a general neutrality, or perhaps ambivalence about the
issue of credibility. The measures of skewness and kurtosis were -0.039 and -0.715, respectively. The histogram has an approximate normal distribution with broad spread and the box plot had no outliers.

Question 28B asked respondents to rate the overall quality of the AAOIFI standards. Table 6.10 presents the accumulated responses yielded a mean of 3.29 with standard deviation 0.825 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in a range from 2.5 to 4.1. This suggests a mild tendency to a fair rating. The measures of skewness and kurtosis were -0.155 and 0.358 respectively. The histogram has an approximate normal distribution and the box plot, after excluding case number 38 as an outlier, exhibited a narrower spread than for Question 28A.

Question 28C asked respondents to rate the quality of AAOIFI's outreach to its constituents. Table 6.10 presents the accumulated responses yielded a mean of 2.77 with standard deviation 0.831 and median 3.0. Eighty-two per cent of all the responses were nearly evenly distributed across scores 2 and 3. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.9 to 3.6. This reflects a fairly strong tendency to a good rating. The measures of skewness and kurtosis were 0.676 and 0.520, respectively. The histogram has an approximate normal distribution, tending leptokurtic, and the box plot, after excluding case numbers 29 and 43 as outliers, exhibited a fairly narrow spread.

Question 28D asked respondents to rate the quality of the AAOIFI organisation in general. Table 6.10 presents the accumulated responses yielded a mean of 2.87 with standard deviation 0.742 and median 3.0. Eighty-six per cent of all the responses were distributed over scores 2, 3, but concentrated in score 3. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.1 to 3.6. This reflects a strong (61%) neutral, or undecided, score, with a tendency to a ‘good’ rating. The measures of skewness and kurtosis were 0.523 and 1.739, respectively. The histogram has an approximate normal distribution, and the box plot, after excluding case numbers 29 and 43 as outliers, exhibited a fairly narrow spread.
### Table 6.10: Descriptive statistics of survey responses to questions 28A to 28D

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<th>Q 28C</th>
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<td>Std. Error</td>
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<td>Std. Error</td>
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<td>Kurtosis</td>
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<td>.650</td>
<td>.520</td>
<td>.650</td>
<td>1.739</td>
<td>.650</td>
</tr>
</tbody>
</table>

**Q.28 Please rate the quality of each of the following aspects of the AAOIFI:**

#### 6.2.4.7 AAOIFI to improve the quality of financial reporting

Survey respondents were asked to what extent they agreed that the adoption of AAOIFI in the UAE would improve the quality of financial reporting in terms of four specific factors. Respondents recorded their responses in terms of a Likert scale graduated from 1 = ‘Strongly Agree’ to 5 = ‘Strongly Disagree’. Table 6.11 shows the descriptive statistics for the responses for Questions 29A to 29D.

Question 29A asked about the extent to which the adoption of AAOIFI standards would improve the quality of financial reporting in terms of ‘relevance’. Table 6.11 presents the accumulated responses yielded a mean of 3.42 with standard deviation 0.893 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.5 to 4.3. This shows that respondents were in moderate disagreement with regard to the aspect of ‘relevance’. The measures of skewness and kurtosis were 0.241 and -0.607, respectively. An approximate normal distribution was revealed through the histogram and no outliers were identified in the box plot.

Question 29B asked about the extent to which adoption of AAOIFI standards would improve the quality of financial reporting in terms of ‘reliability’. Table 6.11 presents the accumulated responses yielded a mean of 3.44 with standard deviation 0.826 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.6 to 4.3, very similar to Question 29A. This shows that respondents were in moderate disagreement with regard to the aspect of ‘reliability’. The measures of skewness and kurtosis
were 0.299 and -0.372, respectively. An approximate normal distribution was revealed through the histogram and no outliers were identified in the box plot.

Question 29C asked about the extent to which adoption of the AAOIFI standards would improve the quality of financial reporting in terms of ‘comparability’. Table 6.11 presents the accumulated responses yielded a mean of 2.79 with standard deviation 0.825 and median 3.0. Seventy-nine per cent of all responses were fairly evenly spread across scores 2 and 3. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.0 to 3.6. This suggests that respondents were in moderate agreement with regard to this aspect of ‘comparability’. The measures of skewness and kurtosis were 0.418 and -0.259, respectively. An approximate normal distribution was revealed through the histogram and reflected in the box plot, after excluding case number 23 as an outlier.

Question 29D asked about the extent to which adoption of the AAOIFI standards would improve the quality of financial reporting in terms of ‘understandability’. Table 6.11 presents the accumulated responses yielded a mean of 3.52 with standard deviation 0.939 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.6 to 4.5, indicating that respondents were in moderate disagreement with this aspect of ‘understandability’. The measures of skewness and kurtosis were -0.353 and -0.115, respectively. An approximate normal distribution was revealed through the histogram, and reflected in the box plot, after eliminating case number 46 as an outlier.

Table 6.11: Descriptive statistics of responses to questions 29a to 29d

<table>
<thead>
<tr>
<th></th>
<th>Q 29A</th>
<th>Q 29B</th>
<th>Q 29C</th>
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<td>Range</td>
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<tr>
<td>Skewness</td>
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<td>.299</td>
<td>.418</td>
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<td>Kurtosis</td>
<td>-.607</td>
<td>-.372</td>
<td>-.259</td>
<td>-.115</td>
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</tbody>
</table>

Q. 29 To what extent do you agree that the adoption of Islamic accounting standards (AAOIFI) in the UAE would improve the quality of financial reporting?
6.2.4.8 Factors influencing the potential adoption of AAOIFI standards in the UAE

Survey respondents were asked to what extent each of four factors, of a selection of ten, would influence the potential adoption of AAOIFI standards in the UAE. Respondents recorded their responses in terms of a Likert scale ranging from 1 = ‘High Impact’ to 5 = ‘Low Impact’. Table 6.12 shows the descriptive statistics for responses to the first four factors, represented in Questions 30A to 30D.

Question 30A asked about the extent to which International auditing firms may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.12 presents the accumulated responses yielded a mean of 2.94 with standard deviation 0.958 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.0 to 3.9, indicating a mild tendency to moderately high impact. The measures of skewness and kurtosis were 0.258 and -0.343, respectively. The histogram shows an approximate normal distribution and the box plot revealed a wide data spread with no outliers.

Question 30B asked about the extent to which international lending organisations (i.e. the World Bank) may influence the potential adoption of AAOIFI standards in the Islamic banks. Table 6.12 presents the accumulated responses yielded a mean of 3.08 with standard deviation 0.882 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.2 to 4.0, indicating a mild tendency to low impact. The measures of skewness and kurtosis were 0.024 and 0.396, respectively. The histogram showed an approximate normal distribution, and the box plot showed a narrow data spread, after eliminating case numbers 14 and 18 as outliers.

Question 30C asked about the extent to which multinational companies may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.12 presents the accumulated responses yielded a mean of 2.88 with standard deviation 0.983 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.9 to 3.9, indicating a mild tendency to moderately high impact. The measures of skewness and kurtosis were 0.239 and -0.844, respectively. The histogram shows an approximate normal distribution and the box plot showed a wide data spread with no outliers.

Question 30D asked about the extent to which global capital market may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.12 presents the accumulated responses yielded a mean of 3.10 with standard deviation 0.913 and median 3.0.
Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.2 to 4.0, indicating a mild tendency to low impact. The measures of skewness and kurtosis were -0.035 and 0.025, respectively. The histogram shows an approximate normal distribution, and the box plot shows a narrow data distribution after eliminating case numbers 18 and 19 as outliers.

Table 6.12: Descriptive statistics of responses to questions 30a to 30d

<table>
<thead>
<tr>
<th></th>
<th>Q 30A</th>
<th>Q 30B</th>
<th>Q 30C</th>
<th>Q 30D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statistic</td>
<td>Mean</td>
<td>Median</td>
<td>Std. Dev.</td>
<td>minimum</td>
</tr>
<tr>
<td></td>
<td>2.94</td>
<td>3.00</td>
<td>.958</td>
<td>1</td>
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<tr>
<td></td>
<td>.133</td>
<td>.00</td>
<td>.882</td>
<td>1</td>
</tr>
<tr>
<td>Skewness</td>
<td>.258</td>
<td>.304</td>
<td>.024</td>
<td>.330</td>
</tr>
<tr>
<td>Kurtosis</td>
<td>-.343</td>
<td>.650</td>
<td>.396</td>
<td>.650</td>
</tr>
</tbody>
</table>

Q. 30 To what extent do you think that each of the following factors influences the potential adoption of Islamic accounting standards (AAOIFI) in the UAE?

Continuing the sub-sets of Question 30, survey respondents were asked to what extent each of four factors of a set of 10 would influence the potential adoption of AAOIFI standards in the UAE. Respondents recorded their responses in terms of a Likert scale graduated from 1 = ‘High Impact’ to 5 = ‘Low Impact’. Table 6.13 shows descriptive statistics of responses to the second set of four factors represented by Questions 30E to 30H.

Question 30E asked about the extent to which the foreign investment may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.13 presents the accumulated responses yielded a mean of 2.81 with standard deviation 1.011 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.8 to 3.8, indicating a tendency to moderately high impact. The measures of skewness and kurtosis were 0.285 and -0.277, respectively. The histogram shows an approximate normal distribution, and the box plot with narrow data spread, after eliminating case numbers 6, 31 and 43 as outliers.

Question 30F asked about the extent to which the UAE Stock Exchange may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.13 presents the accumulated responses yielded a mean of 2.85 with standard deviation 0.937 and median 3.0.
Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.9 to 3.8, indicating a mild tendency to support the opinion of a moderately high impact of stock market influence. The measures of skewness and kurtosis were 0.021 and 0.025, respectively. The histogram shows an approximate normal distribution; the box plot excluded case numbers 24 and 31 as outliers.

Question 30G asked about the extent to which the Government (e.g. the Ministry of Commerce and the Central bank) may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.13 presents the accumulated responses yielded a mean of 2.31 with standard deviation 0.961 and median 2.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.3 to 3.3, indicating a moderately high impact. The measures of skewness and kurtosis were 0.300 and -0.784, respectively. The histogram shows an approximate normal distribution and the box plot exhibited no outliers.

Question 30H asked about the extent to which the academics in the accounting field may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.13 presents the accumulated responses yielded a mean of 4.00 with standard deviation 0.792 and median 4.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 3.2 to 4.8, indicating the potential for the low impact. The measures of skewness and kurtosis were -0.492 and -0.047, respectively. The histogram shows an approximate normal distribution; case numbers 23 and 24 were excluded from the box plot data set as outliers.

Table 6.13: Descriptive statistics of responses to questions 30e to 30h

<table>
<thead>
<tr>
<th>Statistic</th>
<th>Q 30E</th>
<th>Std. Error</th>
<th>Statistic</th>
<th>Q 30F</th>
<th>Std. Error</th>
<th>Statistic</th>
<th>Q 30G</th>
<th>Std. Error</th>
<th>Statistic</th>
<th>Q 30H</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>2.81</td>
<td>.140</td>
<td>2.85</td>
<td>.130</td>
<td>2.31</td>
<td>.133</td>
<td>4.00</td>
<td>.110</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Median</td>
<td>3.00</td>
<td>3.00</td>
<td>2.00</td>
<td></td>
<td>4.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Std. Dev.</td>
<td>1.011</td>
<td>.937</td>
<td>.961</td>
<td></td>
<td>.792</td>
<td></td>
<td></td>
<td></td>
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<td>Maximum</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kurtosis</td>
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<td>.650</td>
<td>.025</td>
<td>.650</td>
<td>-.784</td>
<td>.650</td>
<td>-.047</td>
<td>.650</td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>

Q.30 To what extent do you think that each of the following factors influences the potential adoption of Islamic accounting standards (AAOIFI) in the UAE?

Continuing the sub-sets of Question 30, survey respondents were asked to what extent each of the final two factors of a set of 10 would influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.13 presents the accumulated responses yielded a mean of 2.31 with standard deviation 0.961 and median 2.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 1.3 to 3.3, indicating a moderately high impact. The measures of skewness and kurtosis were 0.300 and -0.784, respectively. The histogram shows an approximate normal distribution and the box plot exhibited no outliers.
standards in the UAE. Respondents recorded their responses in terms of a Likert scale graduated from 1 = ‘High Impact’ to 5 = ‘Low Impact’. Table 6.14 shows the descriptive statistics of responses to Questions 30I and 30J.

Question 30I asked about the extent to which local users’ needs may influence the potential adoption of AAOIFI standards in Islamic banks. Table 6.14 presents the accumulated responses yielded a mean of 3.79 with standard deviation 0.800 and median 4.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 3.0 to 4.6, indicating the expected low impact of local users’ needs in influencing the adoption of AAOIFI standards. The measures of skewness and kurtosis were -0.071 and -0.572, respectively. The histogram shows an approximate normal distribution and the box plot exhibited no outliers.

Question 30J asked about the extent to which Islamic principles may influence the potential adoption of AAOIFI standards by Islamic banks. Table 6.14 presents the accumulated responses yielded a mean of 3.48 with standard deviation 0.874 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.6 to 4.4, indicating the expected low impact of Islamic principles in influencing the potential adoption of AAOIFI standards. The measures of skewness and kurtosis were -0.214 and 0.274, respectively. The histogram shows an approximate normal distribution. The box plot excluded case number 32 as an outlier.

Table 6.14: Descriptive statistics of responses to questions 30I and 30J

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 30I</th>
<th>Std. Error</th>
<th>Q 30J</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>3.79</td>
<td>.111</td>
<td>3.48</td>
<td>.121</td>
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<tr>
<td>Median</td>
<td>4.00</td>
<td></td>
<td>3.00</td>
<td></td>
</tr>
<tr>
<td>Std. Dev.</td>
<td>.800</td>
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<td>.874</td>
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</tr>
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<td>Minimum</td>
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<tr>
<td>Range</td>
<td>3</td>
<td></td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Skewness</td>
<td>-.071</td>
<td>.330</td>
<td>-.214</td>
<td>.330</td>
</tr>
<tr>
<td>Kurtosis</td>
<td>-.572</td>
<td>.650</td>
<td>.274</td>
<td>.650</td>
</tr>
</tbody>
</table>
6.2.4.9 Areas likely to be impacted by adoption of AAOIFI standards

Survey respondents were asked about their perceptions of nine areas that are likely to be impacted by the adoption of AAOIFI standards in the Islamic banks. Respondents recorded their responses in terms of a Likert scale graduated from 1 = ‘High Impact’ to 5 = ‘Low Impact’. Table 6.15 shows the descriptive statistics for responses to the first four areas, represented in responses to Questions 31A to 31D.

Question 31A asked about the likely impact on debt rising due to the adoption of AAOIFI standards. Table 6.15 presents the accumulated responses yielded a mean of 3.54 with standard deviation 0.727 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.8 to 4.3, indicating a tendency to moderately low impact of AAOIFI adoption on debt rising. The measures of skewness and kurtosis were 0.340 and -0.254, respectively. The histogram showed an approximate normal distribution and the box plot exhibited no outliers.

Question 31B asked about the likely impact on capital management due to the adoption of AAOIFI standards. Table 6.15 presents the accumulated responses yielded a mean of 3.31 with standard deviation 0.729 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.6 to 4.0, indicating a mild tendency to moderately low impact of AAOIFI adoption on capital management. The measures of skewness and kurtosis were 0.395 and 0.175, respectively. The histogram showed an approximate normal distribution and the box plot exhibited no outliers.

Question 31C asked about the likely impact on earnings volatility due to the adoption of AAOIFI standards. Table 6.15 presents the accumulated responses yielded a mean of 3.63 with standard deviation 0.627 and median 4.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 3.0 to 4.0, indicating a moderately low impact of AAOIFI adoption on earnings volatility. The measures of skewness and kurtosis were -0.039 and -0.146, respectively. The histogram showed an approximate normal distribution and the box plot exhibited no outliers.

Question 31D asked about the likely impact on investment operations due to the adoption of AAOIFI standards. Table 6.15 presents the accumulated responses yielded a mean of 3.62 with standard deviation 0.690 and median 4.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.9 to 4.3, indicating a moderately low impact of
AAOIFI adoption on investment operations. The measures of skewness and kurtosis were -0.062 and -0.101, respectively. The histogram showed an approximate normal distribution and the box plot exhibited no outliers.

Table 6.15: Descriptive statistics of responses to questions 31a to 31d

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 31A Statistic</th>
<th>Std. Error</th>
<th>Q 31B Statistic</th>
<th>Std. Error</th>
<th>Q 31C Statistic</th>
<th>Std. Error</th>
<th>Q 31D Statistic</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
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<td>.101</td>
<td>3.63</td>
<td>.087</td>
<td>3.62</td>
<td>.096</td>
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<tr>
<td>Median</td>
<td>3.00</td>
<td>.727</td>
<td>3.00</td>
<td>.729</td>
<td>4.00</td>
<td>.627</td>
<td>4.00</td>
<td>.690</td>
</tr>
<tr>
<td>Minimum</td>
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<td>2</td>
<td>2</td>
<td>2</td>
<td>5</td>
<td>5</td>
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<td>Maximum</td>
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</tr>
<tr>
<td>Skewness</td>
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<td>.650</td>
<td>.175</td>
<td>.650</td>
<td>-.146</td>
<td>.650</td>
<td>-.101</td>
<td>.650</td>
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<tr>
<td>Kurtosis</td>
<td></td>
<td></td>
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<td></td>
</tr>
</tbody>
</table>

Q. 31 Please rate the areas that are likely to be impacted upon with AAOIFI adoption in your entity. Rank them from 1 to 5. ‘1’ represents High Impact and ‘5’ represents Low Impact?

Continuing the sub-sets of Question 31, survey respondents were asked about their perceptions related to the areas that are likely to be impacted upon by the adoption of AAOIFI standards adoption in the Islamic banks. Respondents recorded their responses in terms of a Likert scale graduated from 1 = ‘High Impact’ to 5 = ‘Low Impact’. Table 6.16 shows the descriptive statistics for responses to the second four areas, represented in responses to Questions 31E to 31H.

Question 31E asked about the likely impact on securitisation activities due to the adoption of AAOIFI standards. Table 6.16 presents the accumulated survey responses yielded a mean of 4.15 with standard deviation 0.668 and median 4.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 3.5 to 4.8, indicating a tendency to low impact. The measures of skewness and kurtosis were -0.184 and -0.706, respectively. The histogram shows an approximate normal distribution and the box plot exhibits no outliers.

Question 31F asked about the likely impact on prudential capital adequacy due to the adoption of AAOIFI standards. Table 6.16 presents the accumulated responses yielded a mean of 4.13 with standard deviation 0.658 and median 4.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 3.5 to 4.8, indicating a tendency to low impact. The measures of skewness and kurtosis were -0.146 and -0.629, respectively.
The histogram shows an approximate normal distribution and the box plot exhibited no outliers.

Question 31G asked about the likely impact on credit rating due to the adoption of AAOIFI standards. Table 6.16 presents the accumulated responses yielded a mean of 3.04 with standard deviation 0.885 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.2 to 3.9. Given that 58% of all responses were scored ‘3’ and the distribution of responses distinctly leptokurtic, it is clear that the indicators are strongly neutral. The measures of skewness and kurtosis were 0.276 and 0.782, respectively. The histogram showed a leptokurtic distribution. The box plot showed too many hard outliers to be meaningful, as in case numbers 22, 25, 26, 29, 33, 34, 38, 40, 41, 43, 44 and 46. In the subsequent Factor Analysis, this variable was deleted due to its low Measure of Sample Adequacy.

Question 31H asked about the impact on investor relations due to the adoption of AAOIFI standards. Table 6.16 presents the accumulated responses yielded a mean of 2.88 with standard deviation 0.992 and median 3.0. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.0 to 3.8, indicating a tendency to moderately high impact. The measures of skewness and kurtosis were 0.393 and 0.103, respectively. The histogram shows an approximate normal distribution; however. In the box plot, case numbers 29 and 44 were excluded as outliers.

Table 6.16: Descriptive statistics of responses to questions 31e to 31h

<table>
<thead>
<tr>
<th>Variables</th>
<th>Q 31E Statistic</th>
<th>Std. Error</th>
<th>Q 31F Statistic</th>
<th>Std. Error</th>
<th>Q 31G Statistic</th>
<th>Std. Error</th>
<th>Q 31H Statistic</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>4.15</td>
<td>.093</td>
<td>4.13</td>
<td>.091</td>
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<td>.123</td>
<td>2.88</td>
<td>.128</td>
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<tr>
<td>Median</td>
<td>4.00</td>
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<td>4.00</td>
<td></td>
<td>3.00</td>
<td></td>
<td>3.00</td>
<td></td>
</tr>
<tr>
<td>Std. Dev.</td>
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<td></td>
<td>.658</td>
<td></td>
<td>.885</td>
<td></td>
<td>.922</td>
<td></td>
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<td>4</td>
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<td>4</td>
<td></td>
</tr>
<tr>
<td>Skewness</td>
<td>-.184</td>
<td>.330</td>
<td>-.146</td>
<td>.330</td>
<td>.276</td>
<td>.330</td>
<td>.393</td>
<td>.330</td>
</tr>
<tr>
<td>Kurtosis</td>
<td>-.706</td>
<td>.650</td>
<td>-.629</td>
<td>.650</td>
<td>.782</td>
<td>.650</td>
<td>.103</td>
<td>.650</td>
</tr>
</tbody>
</table>

Q. 31 Please rate the areas that are likely to be impacted upon with AAOIFI adoption in your entity. Rank them from 1 to 5. ‘1’ represents High Impact and ‘5’ represents Low Impact.
Continuing the sub-sets of Question 31, survey respondents were asked to what extent the last area would influence the potential adoption of AAOIFI standards in the UAE. Respondents recorded their responses in terms of a Likert scale ranging from 1 = ‘High Impact’ to 5 = ‘Low Impact’. Table 6.17 shows the descriptive statistics of responses to Question 31I.

Question 31I asked about the likely impact on dividend policy of the adoption of AAOIFI standards. Table 6.17 presents the accumulated responses yielded a mean of 3.31 with standard deviation 0.897 and median 3. Two-thirds (Mean ± SD) of all responses were distributed about the mean in the range from 2.4 to 4.2, indicating a tendency to moderate low impact. The measures of skewness and kurtosis were -0.153 and -0.163, respectively. The histogram showed an approximate normal distribution. The box plot exhibited case number 40 as an outlier, which was excluded.

Table 6.17: Descriptive statistics of responses to question 31I

<table>
<thead>
<tr>
<th>Variables</th>
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<th>Std. Error</th>
</tr>
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<tr>
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</tr>
<tr>
<td>Median</td>
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</tr>
<tr>
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</tr>
<tr>
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<tr>
<td>Range</td>
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<td></td>
</tr>
<tr>
<td>Skewness</td>
<td>-.153</td>
<td>.330</td>
</tr>
<tr>
<td>Kurtosis</td>
<td>-.163</td>
<td>.650</td>
</tr>
</tbody>
</table>

6.2.4.10 Impediments to adopting AAOIFI standards by Islamic banks

Survey respondents were asked the open-ended question: ‘What are the most significant impediments to the adoption of AAOIFI standards by Islamic banks?’ The impediments suggested by respondents are presented in the following Table 6.18.
Table 6.18: Impediments to adoption of AAOIFI standards

<table>
<thead>
<tr>
<th>Impediments</th>
<th>Frequency</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Difficulty of institutional comparisons.</td>
<td>30</td>
<td>1</td>
</tr>
<tr>
<td>Not fully supported.</td>
<td>25</td>
<td>2</td>
</tr>
<tr>
<td>Limited acceptability.</td>
<td>24</td>
<td>3</td>
</tr>
<tr>
<td>Significant challenges for academicians and professionals.</td>
<td>16</td>
<td>4</td>
</tr>
<tr>
<td>Prevalence of number of accounting policies.</td>
<td>13</td>
<td>5</td>
</tr>
<tr>
<td>Inconsistent in adoption.</td>
<td>12</td>
<td>6</td>
</tr>
<tr>
<td>Individual accounting policy.</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>125</td>
<td></td>
</tr>
</tbody>
</table>

Q.32 What are the most significant impediments to adopting AAOIFI standards by Islamic banks?

6.2.4.11 AAOIFI goals in developing the standards

Survey respondents were asked the open-ended question: ‘What suggestions do you have to help the AAOIFI meet its goals of both timeliness in completing projects on its agenda and a high-quality due process in developing the standards?’ The overall suggestions proposed by respondents are presented in the following Table 6.19.

Table 6.19: Suggested goals for the AAOIFI

<table>
<thead>
<tr>
<th>Suggestions</th>
<th>Frequency</th>
<th>Rank</th>
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</thead>
<tbody>
<tr>
<td>Additional guidance by IASB.</td>
<td>37</td>
<td>1</td>
</tr>
<tr>
<td>Creation of advisory group.</td>
<td>24</td>
<td>2</td>
</tr>
<tr>
<td>Providing education.</td>
<td>20</td>
<td>3</td>
</tr>
<tr>
<td>Engagement of industry.</td>
<td>17</td>
<td>4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>98</strong></td>
<td></td>
</tr>
</tbody>
</table>

Q.33 What suggestions do you have to help the AAOIFI meet its goals of both timeliness in completing projects on its agenda and a high-quality due process in developing the standards?

6.2.5 Results of reliability and validity testing

The first aspect of reliability and validity testing that was undertaken used Cronbach’s alpha to determine the internal reliability or internal consistency of the scale. For this analysis, a threshold of \( \alpha \geq 0.5 \) was set for determining whether a scale would be adjusted or accepted as it was, based on previous research suggesting this was the lowest acceptable rating. However, questions 12, 13, 16, 17, 28, 29, 30, and 31 have been tested separately for Cronbach’s alpha. Hence, all of the factor scales identified in the research were actually at \( \alpha \geq 0.5 \) or above (following sections describe the findings). This indicated that overall, the factors and scales in
this study were internally highly reliable, in that they were reflective of the same underlying constructs.

The second issue in this section was validity. Validity refers not only to whether the scales were consistent, but whether they were actually addressing a real-world construct. Exploratory factor analysis (EFA) was used in order to determine whether this was appropriate. At least a minimum of six or seven variables can be subjected to factor analysis. Hence, questions 16, 30 and 31 were selected for Factor Analysis.

6.2.5.1 Internal consistency testing as reflected by Cronbach’s alpha

6.2.5.1.1 Scale of evaluation of standards provided by IFRS

The evaluation of IFRS standards in Question 12 in terms of four characteristics was traced through the four variables shown below:


The reliability of the scale measured in terms of Cronbach’s alpha, as shown in Figure 6.21, was found to be 0.806, which is excellent.

<table>
<thead>
<tr>
<th>Case Processing Summary</th>
</tr>
</thead>
<tbody>
<tr>
<td>N</td>
</tr>
<tr>
<td>Cases</td>
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<tr>
<td>Excluded</td>
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<tr>
<td>Total</td>
</tr>
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</table>

a. Listwise deletion based on all variables in the procedure.

<table>
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<tr>
<th>Reliability Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cronbach’s Alpha</td>
</tr>
<tr>
<td>0.806</td>
</tr>
</tbody>
</table>

Figure 6.21: Cronbach’s alpha for Question 12
6.2.5.1.2 Scale of factors which influence the adoption of IFRS

Factors which influence the Islamic banks’ adoption of IFRS were traced through four variables in Question 13, as shown below:


The reliability of the scale, measured in terms of Cronbach’s alpha, as shown in Figure 6.22 was found to be 0.874, which is excellent.

<table>
<thead>
<tr>
<th>Case Processing Summary</th>
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<tr>
<td>Cases</td>
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<tr>
<td>Excluded*</td>
<td>0</td>
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<tr>
<td>Total</td>
<td>52</td>
<td>100.0</td>
</tr>
</tbody>
</table>

a. Listwise deletion based on all variables in the procedure.

Figure 6.22: Cronbach’s alpha for Question 13

6.2.5.1.3 Scale of Islamic bank facilities

Islamic bank facilities were ranked in terms of eight characteristics in Question 16, traced through eight variables as shown below:


The reliability of the scale measured in terms of Cronbach’s alpha is shown in Figure 6.23. For the extracted Factor 1 (Islamic finance orientation) with five variables, namely the provision of free interest loans, provision of Islamic products and services, and run on Islamic law and principles, with a strong global network and sufficient time for transactions, the result was 0.859, which was excellent. However, for Factor 2 (price offerings) with three variables,
namely competitive product offerings, overdraft privileges on current account and lower service charges, the result was 0.659, which was just acceptable.
6.2.5.1.4 Scale of financial statements of Islamic banks

Selected elements of the financial statements of Islamic banks were traced through four variables in Question 17, as shown below:

17. A: Full disclosure; 17. B: Not related to interest; 17. C: Information to determine the amount of Zakat; and 17. D: The disclosure of the paid interest.

The reliability of the scale measured in terms of Cronbach’s alpha is shown in Figure 6.24. The result was 0.674, which is acceptable.
6.2.5.1.5 Scale of the quality of specific aspects of AAOIFI

The evaluation of the quality of specific aspects of the AAOIFI standards was traced through four variables appearing in Question 28, as shown below:


The reliability of the scale was measured in terms of Cronbach’s alpha as shown in Figure 6.25. The result was 0.834, which was excellent.
6.2.5.1.6 Scale of improvement in financial reporting quality by adoption of AAOIFI standards

The evaluation of quality improvements in financial reporting as a consequence of adopting AAOIFI standards, was traced through four variables used in Question 29, as shown below:


The reliability of the scale measured in terms of Cronbach’s alpha is shown in Figure 6.26. The result was 0.885 which is excellent.

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<tr>
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a. Listwise deletion based on all variables in the procedure.

<table>
<thead>
<tr>
<th>Reliability Statistics</th>
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</thead>
<tbody>
<tr>
<td>Cronbach's Alpha</td>
</tr>
<tr>
<td>.885</td>
</tr>
</tbody>
</table>

Figure 6.26: Cronbach’s alpha for question 29

6.2.5.1.7 Scale of factors influencing potential adoption of AAOIFI standards

The evaluation of factors that influence the potential adoption of AAOIFI accounting standards was traced through 10 variables used in Question 30, as shown below:


The reliability of the scale, measured in terms of Cronbach’s alpha, is shown in Figure 6.27. For extracted Factor 1, namely International & Global organisations with four variables,
namely international auditing firms, international lending organisations (i.e. the World Bank), multinational companies and global capital market, was calculated as 0.867, which is excellent.

For Factor 2, namely financial markets with two variables, that is, foreign investment and the UAE Stock Exchange, the Cronbach’s alpha was calculated as 0.817, which is again excellent.

However, for Factor 3, namely internal requirements with three variables, that is the academics in the accounting field, local users’ needs and Islamic principles; the Cronbach’s alpha was calculated as 0.565, which was barely acceptable.

### Case Processing Summary

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<tr>
<td>Total</td>
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<td>100.0</td>
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</table>

a. Listwise deletion based on all variables in the procedure.

### International & Global Organizations Policy (Factor 1)

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<tr>
<th>Cronbach’s Alpha</th>
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<td>4</td>
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</tbody>
</table>

### Financial Markets (Factor 2)

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<td>.817</td>
<td>2</td>
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### Internal requirements (Factor 3)

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<th>Cronbach’s Alpha</th>
<th>N of Items</th>
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</thead>
<tbody>
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<td>.565</td>
<td>3</td>
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</tbody>
</table>
6.2.5.1.8 Scale for areas likely to be impacted by adoption of AAOIFI standards

The evaluation of areas that are likely to be impacted by the adoption of AAOIFI standards was traced through nine variables used in Question 31, as shown below:


The reliability of the scale in terms of Cronbach’s alpha is shown in Figure 6.28 for Factor 1 (Financial policy) with six variables, namely debt raising, capital management, earnings volatility, credit rating, investor relations and dividend policy, was calculated as 0.898, and for Factor 2 (Financial activity) with three variables, namely investment operations, securitisation activities and prudential capital adequacy, was calculated as 0.862. In both cases the result was excellent.

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<tr>
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<td>Valid</td>
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<td>Excluded*</td>
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<td>Total</td>
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*Listwise deletion based on all variables in the procedure.

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<th>Financial activity (Factor 2)</th>
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<td>Cronbach’s Alpha</td>
<td>N of Items</td>
</tr>
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<td>6</td>
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</tbody>
</table>

Figure 6.28: Cronbach’s alpha for question 31
6.2.5.2 Factor analysis testing

6.2.5.2.1 Factor loading for Islamic bank facilities

Islamic bank facilities were traced through eight variables in Question 16, namely, provision of free interest loans; provision of Islamic products and services; run on Islamic law and principles; strong global network; sufficient time for transactions; competitive product offerings; overdraft privileges on current account; and, lower service charges.

To find the inherent constructs of groups, or factors, Factor Analysis was applied to all the eight variables. Table 6.20 shows the anti-image correlation of all the eight variables which is a measure of Sample Adequacy. An anti-image correlation higher than 0.50 indicates good sample adequacy and a particular variable having equal to, or more than, 0.50 anti-image correlation can participate in the Factor Analysis. We have found that all eight variables had an anti-image correlation higher than 0.05 thus these could be used for Factor Analysis.

Table 6.20: Measures of sample adequacy for question 16

<table>
<thead>
<tr>
<th>Anti-image Matrices</th>
<th>Q16A</th>
<th>Q16B</th>
<th>Q16C</th>
<th>Q16D</th>
<th>Q16E</th>
<th>Q16F</th>
<th>Q16G</th>
<th>Q16H</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anti-image Covariance</td>
<td>Q16A</td>
<td>.353</td>
<td>-.171</td>
<td>.056</td>
<td>-.084</td>
<td>.007</td>
<td>-.020</td>
<td>.061</td>
</tr>
<tr>
<td>Q16B</td>
<td>-.171</td>
<td>.213</td>
<td>-.145</td>
<td>-.056</td>
<td>-.086</td>
<td>.060</td>
<td>-.016</td>
<td>-.015</td>
</tr>
<tr>
<td>Q16C</td>
<td>.056</td>
<td>-.145</td>
<td>.385</td>
<td>-.085</td>
<td>-.072</td>
<td>-.051</td>
<td>-.008</td>
<td>-.018</td>
</tr>
<tr>
<td>Q16D</td>
<td>-.084</td>
<td>-.056</td>
<td>-.085</td>
<td>.491</td>
<td>.065</td>
<td>-.178</td>
<td>-.015</td>
<td>.107</td>
</tr>
<tr>
<td>Q16E</td>
<td>.007</td>
<td>-.086</td>
<td>-.072</td>
<td>.065</td>
<td>.619</td>
<td>-.125</td>
<td>-.147</td>
<td>.103</td>
</tr>
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<td>Q16F</td>
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<td>.060</td>
<td>-.051</td>
<td>-.178</td>
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<td>.615</td>
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<td>-.208</td>
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<tr>
<td>Q16G</td>
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<td>-.016</td>
<td>-.008</td>
<td>-.015</td>
<td>-.147</td>
<td>-.136</td>
<td>.702</td>
<td>-.223</td>
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<tr>
<td>Q16H</td>
<td>-.023</td>
<td>-.015</td>
<td>-.018</td>
<td>.107</td>
<td>.103</td>
<td>-.208</td>
<td>-.223</td>
<td>.750</td>
</tr>
<tr>
<td>Anti-image Correlation</td>
<td>Q16A</td>
<td>.754a</td>
<td>-.622</td>
<td>.153</td>
<td>-.201</td>
<td>.015</td>
<td>-.042</td>
<td>.123</td>
</tr>
<tr>
<td>Q16B</td>
<td>-.622</td>
<td>.717a</td>
<td>-.508</td>
<td>-.173</td>
<td>-.236</td>
<td>.167</td>
<td>-.042</td>
<td>-.038</td>
</tr>
<tr>
<td>Q16C</td>
<td>.153</td>
<td>-.508</td>
<td>.821a</td>
<td>-.195</td>
<td>-.147</td>
<td>-.105</td>
<td>-.015</td>
<td>-.034</td>
</tr>
<tr>
<td>Q16D</td>
<td>-.201</td>
<td>-.173</td>
<td>-.195</td>
<td>.839a</td>
<td>.118</td>
<td>-.325</td>
<td>-.025</td>
<td>.177</td>
</tr>
<tr>
<td>Q16E</td>
<td>.015</td>
<td>-.236</td>
<td>-.147</td>
<td>.118</td>
<td>.829a</td>
<td>-.203</td>
<td>-.223</td>
<td>.152</td>
</tr>
<tr>
<td>Q16F</td>
<td>-.042</td>
<td>.167</td>
<td>-.105</td>
<td>-.325</td>
<td>-.203</td>
<td>.714a</td>
<td>-.207</td>
<td>-.307</td>
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<tr>
<td>Q16G</td>
<td>.123</td>
<td>-.042</td>
<td>-.015</td>
<td>-.025</td>
<td>-.223</td>
<td>-.207</td>
<td>.728a</td>
<td>-.308</td>
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<tr>
<td>Q16H</td>
<td>-.045</td>
<td>-.038</td>
<td>-.034</td>
<td>.177</td>
<td>.152</td>
<td>-.307</td>
<td>-.308</td>
<td>.566a</td>
</tr>
</tbody>
</table>

a. Measures of Sampling Adequacy (MSA)

The Kaiser-Mayer-Olkin Measure of Sample Adequacy shown in Figure 6.29 was calculated as 0.761, which was reasonably good, and Bartlett’s Test of Sphericity was also found significant, which supported the feasibility of conducting the Factor Analysis.
Kaiser-Meyer-Olkin Measure of Sampling Adequacy  .761
Bartlett’s Test of Sphericity
   Approx. Chi-Square  168.735
   Df  28
   Sig.  .000

**Figure 6.29: KMO and Bartlett’s test for question 16**

The Scree Plot shown in Figure 6.30 shows the extraction of two factors whose Eigen values were more than 1. The distribution of these eight variables is shown in Table 6.22.

![Scree Plot](image)

**Figure 6.30: Scree plot for question 16**

Typically, five variables from Question 16A to Question 16E (that is, provision of free interest loans, provision of Islamic products and services, run on Islamic law and principles, strong global network and sufficient time for transactions) formed one factor, namely, Islamic finance orientation, and the remaining three variables, relating to Questions 16F, 16G and 16H (that is, competitive product offerings, overdraft privileges on current account and lower service charges) formed another factor, namely, price offerings. Factor loadings are shown as follows in Table 6.21.
### Table 6.21: Rotated component matrix for question 16

<table>
<thead>
<tr>
<th>Variables</th>
<th>Component 1</th>
<th>Component 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q16B: Islamic products and services</td>
<td>.921</td>
<td>.059</td>
</tr>
<tr>
<td>Q16A: Free interest loans</td>
<td>.841</td>
<td>-.033</td>
</tr>
<tr>
<td>Q16C: Run on Islamic law and principles</td>
<td>.818</td>
<td>.189</td>
</tr>
<tr>
<td>Q16D: Strong global network</td>
<td>.778</td>
<td>.111</td>
</tr>
<tr>
<td>Q16E: Sufficient time for transactions</td>
<td>.595</td>
<td>.316</td>
</tr>
<tr>
<td>Q16G: Overdraft privileges on current account</td>
<td>.113</td>
<td>.792</td>
</tr>
<tr>
<td>Q16H: Lower service charges</td>
<td>-.055</td>
<td>.767</td>
</tr>
<tr>
<td>Q16F: Competitive product offerings</td>
<td>.311</td>
<td>.707</td>
</tr>
</tbody>
</table>

Extraction Method: Principal Component Analysis  
Rotation Method: Varimax with Kaiser Normalization  

a. Rotation converged in 3 iterations.

The Total Variance Explained was calculated as 64.552 by two factors shown below in Table 6.22.
Table 6.22: Total variance explained for question 16

<table>
<thead>
<tr>
<th>Component</th>
<th>Initial Eigenvalues</th>
<th>Total Variance Explained</th>
<th>Rotation Sums of Squared Loadings</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>% of Variance</td>
<td>Cumulative</td>
</tr>
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<td>1</td>
<td>3.598</td>
<td>44.979</td>
<td>44.979</td>
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<tr>
<td>2</td>
<td>1.566</td>
<td>19.573</td>
<td>64.552</td>
</tr>
<tr>
<td>3</td>
<td>.774</td>
<td>9.676</td>
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</tr>
<tr>
<td>4</td>
<td>.662</td>
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<td>5</td>
<td>.515</td>
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<td>.423</td>
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<td>7</td>
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<td>8</td>
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<td>100.000</td>
</tr>
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</table>

Extraction Method: Principal Component Analysis
6.2.5.2.2 Factor loading for influence on the adoption of AAOIFI

The influence of selected factors on the potential adoption of AAOIFI in the UAE was traced through 10 variables which were: international auditing firms, international lending organisations (i.e. the World Bank), multinational companies, foreign investment, global capital market, foreign investment, the UAE Stock Exchange, the Government (e.g. the Ministry of Commerce and the Central bank), academics in the accounting field, local users’ needs, and Islamic principles.

Table 6.23 shows Measures of Sample Adequacy (MSA). Question 30G, ‘The Government (e.g. the Ministry of Commerce and the Central bank)’, shows an MSA less than the threshold value of 0.50 (that is, 0.294). Hence, Question 30G was removed from the Factor Analysis procedure. Though, Question 30E, ‘foreign investment’ had a borderline MSA of 0.495, less than 0.50, it was decided to retain this variable in the Factor Analysis Procedure as the difference between observed MSA and the threshold value of 0.50 was marginal.

Table 6.23: Measures of sample adequacy for question 30

<table>
<thead>
<tr>
<th>Anti-image Matrices</th>
<th>Q30A</th>
<th>Q30B</th>
<th>Q30C</th>
<th>Q30D</th>
<th>Q30E</th>
<th>Q30F</th>
<th>Q30G</th>
<th>Q30H</th>
<th>Q30I</th>
<th>Q30J</th>
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<td>Q30A</td>
<td>.339</td>
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<td>.175</td>
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<td>-.040</td>
<td>-.004</td>
<td>.083</td>
<td>.150</td>
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<td>.120</td>
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<td>Q30I</td>
<td>-.042</td>
<td>.051</td>
<td>.104</td>
<td>-.021</td>
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<td>-.051</td>
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<td>.058</td>
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<td>-.299</td>
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<td>.010</td>
<td>-.084</td>
<td>-.131</td>
<td>-.055</td>
<td>-.089</td>
<td>.128</td>
</tr>
<tr>
<td>Q30B</td>
<td>-.493</td>
<td>.798*</td>
<td>-.217</td>
<td>-.131</td>
<td>.091</td>
<td>.019</td>
<td>.179</td>
<td>.023</td>
<td>.102</td>
<td>.044</td>
</tr>
<tr>
<td>Q30C</td>
<td>.181</td>
<td>-.217</td>
<td>.676*</td>
<td>-.528</td>
<td>.045</td>
<td>.028</td>
<td>-.190</td>
<td>.208</td>
<td>.187</td>
<td>-.071</td>
</tr>
<tr>
<td>Q30D</td>
<td>-.485</td>
<td>-.131</td>
<td>-.528</td>
<td>.714*</td>
<td>-.171</td>
<td>.099</td>
<td>.130</td>
<td>-.081</td>
<td>-.047</td>
<td>-.030</td>
</tr>
<tr>
<td>Q30E</td>
<td>.010</td>
<td>.091</td>
<td>.045</td>
<td>-.171</td>
<td>.495*</td>
<td>-.679</td>
<td>-.127</td>
<td>.006</td>
<td>.193</td>
<td>-.119</td>
</tr>
<tr>
<td>Q30F</td>
<td>-.084</td>
<td>.019</td>
<td>.028</td>
<td>.099</td>
<td>-.679</td>
<td>.549*</td>
<td>.091</td>
<td>.134</td>
<td>-.090</td>
<td>-.068</td>
</tr>
<tr>
<td>Q30G</td>
<td>-.131</td>
<td>.179</td>
<td>-.190</td>
<td>.130</td>
<td>-.127</td>
<td>.091</td>
<td>.294*</td>
<td>.183</td>
<td>-.225</td>
<td>.239</td>
</tr>
<tr>
<td>Q30H</td>
<td>-.055</td>
<td>.023</td>
<td>.208</td>
<td>-.081</td>
<td>-.006</td>
<td>.134</td>
<td>.183</td>
<td>.639*</td>
<td>.079</td>
<td>.164</td>
</tr>
<tr>
<td>Q30I</td>
<td>-.089</td>
<td>.102</td>
<td>.187</td>
<td>-.047</td>
<td>.193</td>
<td>-.090</td>
<td>-.225</td>
<td>.079</td>
<td>.558*</td>
<td>-.452</td>
</tr>
<tr>
<td>Q30J</td>
<td>.128</td>
<td>.044</td>
<td>-.071</td>
<td>-.030</td>
<td>-.119</td>
<td>-.068</td>
<td>.239</td>
<td>.164</td>
<td>-.452</td>
<td>.608*</td>
</tr>
</tbody>
</table>

a. Measures of Sampling Adequacy(MSA)
The Kaiser-Meyer-Olkin Measure of Sampling Adequacy was calculated as 0.649 with Question 30G shown in the following Figure 6.31:

<table>
<thead>
<tr>
<th>Kaiser-Meyer-Olkin Measure of Sampling Adequacy</th>
<th>.649</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bartlett’s Test of Sphericity</td>
<td></td>
</tr>
<tr>
<td>Approx. Chi-Square</td>
<td>177.435</td>
</tr>
<tr>
<td>Df</td>
<td>45</td>
</tr>
<tr>
<td>Sig.</td>
<td>.000</td>
</tr>
</tbody>
</table>

**Figure 6.31: KMO and Bartlett’s test for question 30**

Table 6.24 shows Measures of Sample Adequacy in red colours after deletion of Question 30G, ‘The Government (e.g. the Ministry of Commerce and the Central bank)’. All the variables had shown an MSA at or more than the threshold value of 0.50, thus paving the way for the Factor Analysis procedure. The Kaiser-Meyer-Olkin Measure of Sampling Adequacy was calculated as 0.681 with Question 30G shown in figure 6.32. There was a marginal gain in the Kaiser-Meyer-Olkin Measure of Sampling Adequacy when Question 30G was deleted.

Table 6.24: Measures of sample adequacy for question 30 after deleting question 30g

<table>
<thead>
<tr>
<th>Anti-image matrices</th>
<th>Q30A</th>
<th>Q30B</th>
<th>Q30C</th>
<th>Q30D</th>
<th>Q30E</th>
<th>Q30F</th>
<th>Q30H</th>
<th>Q30I</th>
<th>Q30J</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anti-image Covariance</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q30A</td>
<td>.345</td>
<td>-.175</td>
<td>.065</td>
<td>-.154</td>
<td>-.003</td>
<td>-.030</td>
<td>-.017</td>
<td>-.060</td>
<td>.081</td>
</tr>
<tr>
<td>Q30B</td>
<td>-.175</td>
<td>.385</td>
<td>-.081</td>
<td>-.054</td>
<td>.050</td>
<td>.001</td>
<td>-.006</td>
<td>.077</td>
<td>.001</td>
</tr>
<tr>
<td>Q30C</td>
<td>.065</td>
<td>-.081</td>
<td>.480</td>
<td>-.196</td>
<td>.010</td>
<td>.022</td>
<td>.160</td>
<td>.088</td>
<td>-.016</td>
</tr>
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<td>Q30D</td>
<td>-.154</td>
<td>-.054</td>
<td>.480</td>
<td>-.196</td>
<td>.010</td>
<td>.022</td>
<td>.160</td>
<td>.088</td>
<td>-.016</td>
</tr>
<tr>
<td>Q30E</td>
<td>-.003</td>
<td>.050</td>
<td>-.010</td>
<td>-.060</td>
<td>.483</td>
<td>-.326</td>
<td>.011</td>
<td>.099</td>
<td>-.053</td>
</tr>
<tr>
<td>Q30F</td>
<td>-.030</td>
<td>.001</td>
<td>.022</td>
<td>.033</td>
<td>-.326</td>
<td>.480</td>
<td>.076</td>
<td>-.042</td>
<td>-.054</td>
</tr>
<tr>
<td>Q30H</td>
<td>-.017</td>
<td>-.006</td>
<td>.160</td>
<td>-.054</td>
<td>.011</td>
<td>.076</td>
<td>.844</td>
<td>.097</td>
<td>.096</td>
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<tr>
<td>Q30I</td>
<td>-.060</td>
<td>.077</td>
<td>.088</td>
<td>-.009</td>
<td>.099</td>
<td>-.042</td>
<td>.097</td>
<td>.707</td>
<td>-.295</td>
</tr>
<tr>
<td>Q30J</td>
<td>.081</td>
<td>-.001</td>
<td>-.016</td>
<td>-.029</td>
<td>-.053</td>
<td>-.054</td>
<td>.096</td>
<td>-.295</td>
<td>.693</td>
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<tr>
<td>Anti-image Correlation</td>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Q30A</td>
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<td>-.481</td>
<td>.160</td>
<td>-.477</td>
<td>-.007</td>
<td>-.073</td>
<td>-.032</td>
<td>-.122</td>
<td>.165</td>
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<tr>
<td>Q30B</td>
<td>-.481</td>
<td>.811</td>
<td>-.189</td>
<td>-.158</td>
<td>.116</td>
<td>.003</td>
<td>-.010</td>
<td>.148</td>
<td>.001</td>
</tr>
<tr>
<td>Q30C</td>
<td>.160</td>
<td>-.189</td>
<td>.705</td>
<td>-.517</td>
<td>.021</td>
<td>.047</td>
<td>.251</td>
<td>.150</td>
<td>-.027</td>
</tr>
<tr>
<td>Q30D</td>
<td>-.477</td>
<td>-.158</td>
<td>-.517</td>
<td>.724</td>
<td>-.158</td>
<td>.088</td>
<td>-.108</td>
<td>-.018</td>
<td>-.063</td>
</tr>
<tr>
<td>Q30E</td>
<td>-.007</td>
<td>.116</td>
<td>.021</td>
<td>-.158</td>
<td>.510</td>
<td>-.676</td>
<td>.018</td>
<td>.170</td>
<td>-.092</td>
</tr>
<tr>
<td>Q30F</td>
<td>-.073</td>
<td>.003</td>
<td>.047</td>
<td>.088</td>
<td>-.676</td>
<td>.558</td>
<td>.120</td>
<td>-.072</td>
<td>-.093</td>
</tr>
<tr>
<td>Q30H</td>
<td>-.032</td>
<td>-.010</td>
<td>.251</td>
<td>-.108</td>
<td>.018</td>
<td>.120</td>
<td>.623</td>
<td>.125</td>
<td>.126</td>
</tr>
<tr>
<td>Q30I</td>
<td>-.122</td>
<td>.148</td>
<td>.150</td>
<td>-.018</td>
<td>.170</td>
<td>-.072</td>
<td>.125</td>
<td>.600</td>
<td>-.421</td>
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<tr>
<td>Q30J</td>
<td>.165</td>
<td>.001</td>
<td>-.027</td>
<td>-.063</td>
<td>-.092</td>
<td>-.093</td>
<td>.126</td>
<td>-.421</td>
<td>.677</td>
</tr>
</tbody>
</table>

a. Measures of Sampling Adequacy (MSA)
Figure 6.32: KMO and Bartlett’s test for question 30 after deleting question 30g

The scree plot in Figure 6.33 is after the extraction of three factors whose Eigen values were more than 1. The distribution of these eight variables is shown in Table 6.25.

![Scree Plot](image)

Figure 6.33: Scree plot for question 30 after deleting question 30g

Table 6.25: Rotated component matrix for question 30 after deleting question 30g

<table>
<thead>
<tr>
<th>Variables</th>
<th>Component 1</th>
<th>Component 2</th>
<th>Component 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q30D: Global capital market</td>
<td>.904</td>
<td>.043</td>
<td>-.055</td>
</tr>
<tr>
<td>Q30B: International lending org.</td>
<td>.847</td>
<td>-.089</td>
<td>-.169</td>
</tr>
<tr>
<td>Q30A: International auditing firms</td>
<td>.834</td>
<td>.016</td>
<td>-.135</td>
</tr>
<tr>
<td>Q30C: Multinational companies</td>
<td>.785</td>
<td>-.012</td>
<td>.035</td>
</tr>
<tr>
<td>Q30E: Foreign investment</td>
<td>.034</td>
<td>.923</td>
<td>.047</td>
</tr>
<tr>
<td>Q30F: The UAE Stock Exchange</td>
<td>-.068</td>
<td>.889</td>
<td>.180</td>
</tr>
<tr>
<td>Q30J: Islamic principles</td>
<td>-.134</td>
<td>.171</td>
<td>.779</td>
</tr>
<tr>
<td>Q30I: Local users</td>
<td>-.190</td>
<td>-.120</td>
<td>.771</td>
</tr>
<tr>
<td>Q30H: Academics in the field</td>
<td>-.064</td>
<td>-.181</td>
<td>-.600</td>
</tr>
</tbody>
</table>

Extraction Method: Principal Component Analysis
Rotation Method: Varimax with Kaiser Normalization
a. Rotation converged in 4 iterations.

Typically, Questions 30A to 30D (namely, international auditing firms, international lending organisations (i.e. the World Bank), multinational companies and global capital market, respectively), were four variables that formed one factor, namely International & Global

The Factor loadings shown in Table 6.24 revealed that Question 30H, ‘Academics in the accounting field’, had a negative loading with factor 3. In order to have a simple and straightforward interpretation of factor loadings, we had reversed the observation of Question 30H. The Rotated Factor Loadings with reversed Question 30H is shown in Table 6.26.

**Table 6.26: Rotated component matrix for question 30 after deleting question 30g and reversing question 30h**

<table>
<thead>
<tr>
<th>Variables</th>
<th>Component 1</th>
<th>Component 2</th>
<th>Component 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q30D: Global capital market</td>
<td>.904</td>
<td>.043</td>
<td>-.055</td>
</tr>
<tr>
<td>Q30B: International lending organisations</td>
<td>.847</td>
<td>-.089</td>
<td>-.169</td>
</tr>
<tr>
<td>Q30A: International auditing firms</td>
<td>.834</td>
<td>.016</td>
<td>-.135</td>
</tr>
<tr>
<td>Q30C: Multinational companies</td>
<td>.785</td>
<td>-.012</td>
<td>.035</td>
</tr>
<tr>
<td>Q30E: Foreign investment</td>
<td>.034</td>
<td>.923</td>
<td>.047</td>
</tr>
<tr>
<td>Q30F: The UAE Stock Exchange</td>
<td>-.068</td>
<td>.889</td>
<td>.180</td>
</tr>
<tr>
<td>Q30J: Islamic principles</td>
<td>-.134</td>
<td>.171</td>
<td>.779</td>
</tr>
<tr>
<td>Q30I: Local users</td>
<td>-.190</td>
<td>-.120</td>
<td>.771</td>
</tr>
<tr>
<td>Q30H_R: Academics in the accounting field</td>
<td>.064</td>
<td>.181</td>
<td>.600</td>
</tr>
</tbody>
</table>

Extraction Method: Principal Component Analysis
Rotation Method: Varimax with Kaiser Normalization
a. Rotation converged in 4 iterations.

Table 6.27 shows the total variance explained by the three extracted factors, calculated as 69.869, which is reasonably good.
Table 6.27: Total variance explained for question 30

<table>
<thead>
<tr>
<th>Component</th>
<th>Initial Eigenvalues</th>
<th>Total Variance Explained</th>
<th>Rotation Sums of Squared Loadings</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>% of Variance</td>
<td>Cumulative %</td>
</tr>
<tr>
<td>1</td>
<td>3.106</td>
<td>34.510</td>
<td>34.510</td>
</tr>
<tr>
<td>2</td>
<td>1.936</td>
<td>21.514</td>
<td>56.024</td>
</tr>
<tr>
<td>3</td>
<td>1.246</td>
<td>13.845</td>
<td>69.869</td>
</tr>
<tr>
<td>4</td>
<td>.899</td>
<td>9.990</td>
<td>79.859</td>
</tr>
<tr>
<td>5</td>
<td>.611</td>
<td>6.787</td>
<td>86.646</td>
</tr>
<tr>
<td>6</td>
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</tr>
<tr>
<td>7</td>
<td>.314</td>
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<td>95.073</td>
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<td>8</td>
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</tr>
<tr>
<td>9</td>
<td>.186</td>
<td>2.062</td>
<td>100.000</td>
</tr>
</tbody>
</table>

Extraction method: Principal component analysis
6.2.5.2.3 Factor loading for areas likely to be impacted by AAOIFI adoption

Areas likely to be impacted by the adoption of the AAOIFI standards were traced through nine variables which were: debt raising, capital management, earnings volatility, investment operations, securitisation activities, prudential capital adequacy, credit rating, investor relations, and dividend policy.

Table 6.28 shows the Measures of Sample Adequacy for Question 31, and as all the anti-image correlations were found to be more than 0.50, these were fit for the Factor Analysis procedure.

Table 6.28: Measures of sample adequacy for question 31

<table>
<thead>
<tr>
<th>Anti-image Matrices</th>
<th>Q31A</th>
<th>Q31B</th>
<th>Q31C</th>
<th>Q31D</th>
<th>Q31E</th>
<th>Q31F</th>
<th>Q31G</th>
<th>Q31H</th>
<th>Q31I</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anti-image Covariance</td>
<td>.363</td>
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<td>-.149</td>
<td>.001</td>
<td>.043</td>
<td>.036</td>
<td>-.110</td>
<td>.014</td>
<td>.051</td>
</tr>
<tr>
<td>Q1B</td>
<td>-.108</td>
<td>.270</td>
<td>-.090</td>
<td>-.006</td>
<td>-.015</td>
<td>.020</td>
<td>.059</td>
<td>-.093</td>
<td>-.048</td>
</tr>
<tr>
<td>Q31C</td>
<td>-.149</td>
<td>-.090</td>
<td>.334</td>
<td>-.095</td>
<td>-.046</td>
<td>-.025</td>
<td>.050</td>
<td>.044</td>
<td>-.046</td>
</tr>
<tr>
<td>Q31D</td>
<td>.001</td>
<td>-.006</td>
<td>-.095</td>
<td>.337</td>
<td>-.116</td>
<td>-.006</td>
<td>-.075</td>
<td>-.011</td>
<td>.034</td>
</tr>
<tr>
<td>Q31E</td>
<td>.043</td>
<td>-.015</td>
<td>-.046</td>
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<td>.295</td>
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<td>-.005</td>
<td>-.070</td>
<td>.096</td>
</tr>
<tr>
<td>Q31F</td>
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<td>.020</td>
<td>-.025</td>
<td>-.006</td>
<td>-.168</td>
<td>.381</td>
<td>.098</td>
<td>.050</td>
<td>.052</td>
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<tr>
<td>Q31G</td>
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<td>.050</td>
<td>-.075</td>
<td>-.005</td>
<td>-.098</td>
<td>.236</td>
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<td>-.081</td>
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<td>Q31H</td>
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<td>.044</td>
<td>-.011</td>
<td>-.070</td>
<td>.050</td>
<td>-.065</td>
<td>.195</td>
<td>-.114</td>
</tr>
<tr>
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<td>-.052</td>
<td>-.081</td>
<td>-.114</td>
<td>.261</td>
</tr>
</tbody>
</table>

The Kaiser-Meyer-Olkin Measure of Sampling Adequacy was calculated as 0.826, which was excellent, as shown in figure (6.35).

| Kaiser-Meyer-Olkin Measure of Sampling Adequacy | .826 |
| Bartlett’s Test of Sphericity | Approx. Chi-Square | 334.893 |
| Df | 36 |
| Sig. | .000 |

Figure 6.34: KMO and Bartlett’s test for question 31

The scree plot shown in Figure 6.35 suggested the extraction of two Factors. Questions 31A, B, C, G, H and I (debt raising, capital management, earnings volatility, credit rating, investor relations and dividend policy, respectively) formed one factor, namely Financial policy; and
Questions 31D, E and F (investment operations, securitisation activities, and prudential capital adequacy, respectively) formed the second factor, namely Financial activities.

![Scree plot for question 31](image)

**Figure 6.35: Scree plot for question 31**

Table 6.29 shows the Factor loadings for extracted factors and Table 6.30 shows the Total Variance Explained by the two factors to be 72.513, which was commendable.

**Table 6.29: Rotated component matrix for question 31**

<table>
<thead>
<tr>
<th>Variables</th>
<th>Component 1</th>
<th>Component 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q31B: Capital management</td>
<td>.868</td>
<td>.202</td>
</tr>
<tr>
<td>Q31I: Dividend policy</td>
<td>.814</td>
<td>.163</td>
</tr>
<tr>
<td>Q31H: Investor relations</td>
<td>.802</td>
<td>.346</td>
</tr>
<tr>
<td>Q31A: Debt raising</td>
<td>.759</td>
<td>.215</td>
</tr>
<tr>
<td>Q31C: Earnings volatility</td>
<td>.640</td>
<td>.411</td>
</tr>
<tr>
<td>Q31G: Credit rating</td>
<td>.629</td>
<td>.562</td>
</tr>
<tr>
<td>Q31E: Securitisation activities</td>
<td>.210</td>
<td>.893</td>
</tr>
<tr>
<td>Q31F: Prudential capital adequacy</td>
<td>.182</td>
<td>.861</td>
</tr>
<tr>
<td>Q31D: Investment operations</td>
<td>.403</td>
<td>.768</td>
</tr>
</tbody>
</table>

*Extraction Method: Principal Component Analysis*
*Rotation Method: Varimax with Kaiser Normalization*
*a. Rotation converged in 3 iterations.*
### Table 6.30: Total variance explained for question 31

<table>
<thead>
<tr>
<th>Component</th>
<th>Initial Eigenvalues</th>
<th>Total Variance Explained</th>
<th>Rotation Sums of Squared Loadings</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>% of Variance</td>
<td>Cumulative %</td>
</tr>
<tr>
<td>1</td>
<td>5.325</td>
<td>59.170</td>
<td>59.170</td>
</tr>
<tr>
<td>2</td>
<td>1.201</td>
<td>13.343</td>
<td>72.513</td>
</tr>
<tr>
<td>3</td>
<td>.966</td>
<td>10.729</td>
<td>83.241</td>
</tr>
<tr>
<td>4</td>
<td>.422</td>
<td>4.685</td>
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</tr>
<tr>
<td>5</td>
<td>.353</td>
<td>3.924</td>
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<td>6</td>
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</tr>
<tr>
<td>9</td>
<td>.119</td>
<td>1.322</td>
<td>100.000</td>
</tr>
</tbody>
</table>

Extraction method: Principal component analysis
6.3 Analysis of unstructured interviews

After analysis of the questionnaires, this section of Chapter 6 discusses the qualitative findings of the research generated from in-depth unstructured interviews with managers and members of the Fatwa and Shariah Supervisory Board in the Islamic banking sector, and members of the board of trustees of AAOIFI. These findings will serve to explain the quantitative and documentary findings and examine in further detail the significant issues relating to the suitability of IFRS and AAOIFI accounting standards in the UAE.

6.3.1 Background of interviewees

Table 6.31 shows a list of the interviewees with their general background outlined. All except one have a PhD degree. Also, all the interviewees have more than 12 years’ work experience in Islamic financial institutes, averaging 16.6 years.

Table 6.31: Information about interviewees

<table>
<thead>
<tr>
<th>Interviewee</th>
<th>Level of education</th>
<th>Experience in Islamic institutes</th>
<th>Islamic bank</th>
<th>Background information</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>PhD</td>
<td>12 years</td>
<td>1</td>
<td>Member of the Fatwa and Shariah Supervisory Board</td>
</tr>
<tr>
<td>2</td>
<td>MBA</td>
<td>19 years</td>
<td>2</td>
<td>Regional Manager</td>
</tr>
<tr>
<td>3</td>
<td>PhD</td>
<td>14 years</td>
<td>3</td>
<td>Member of the Fatwa and Shariah Supervisory Board</td>
</tr>
<tr>
<td>4</td>
<td>PhD</td>
<td>22 years</td>
<td>4</td>
<td>Member of the board of trustees</td>
</tr>
<tr>
<td>5</td>
<td>PhD</td>
<td>16 years</td>
<td>1</td>
<td>Branch manager</td>
</tr>
</tbody>
</table>

6.3.2 Reasons for introduction of Islamic accounting standards in the UAE

The first question asked related to the reasons for the introduction of Islamic Accounting Standards in the UAE. In general the issue of the introduction of Islamic Accounting Standards in the UAE arises because the UAE is predominantly an Islamic country and like all other Islamic countries, its people put a high emphasis on religious principles. This is why when it comes to the Islamic principles of Riba, Zakah, Mudharaba, Musharaka, and so on, Islamic financial institutions feel
compelled to discard the accounting principles set by the IASB and use Islamic principles.

The interviewees stated that as the whole of the Islamic world was coming into prominence with phenomenal economic growth, it became imperative for the financial experts in this part of the world to develop a new unified accounting standards system that would cater for the whole region.

The interviewees stated that Islamic authorities all over the world had gradually started opting for Islamic accounting standards developed by the AAOIFI. Being a vital supporter of the Islamic world, UAE too had to show compatibility with the standards. In 2004, with the introduction of the Dubai International Financial Centre (DIFC), the UAE gave its approval to the adoption of the AAOIFI Islamic accounting standards. The interviewees also pointed out that Islamic accounting standards are based more on Islamic beliefs than on the technicalities of accounting; every practising Muslim does look for a Shariah-followed transaction. That is why AAOIFI came into existence with its Shariah-abiding laws that were suited well to the nature of financial transactions taking place in the UAE. The interviewees stated that with the adaptation of Shariah law-based accounting principles, UAE’s several Islamic banks and other prominent financial institutions would start applying these principles in domestic and international transactions. Domestic transactions, in particular, would be benefitted by its adoption as the concerned natives would start believing that their transactions were now Islamic.

6.3.3 Identification of first efforts made towards developing Islamic accounting standards in the UAE

The second question asked related to when and where the first efforts were made towards developing Islamic accounting standards in the UAE. All interviewees agreed that the primary body which was quite influential and very instrumental in the implementation of Islamic accounting standards in the UAE was the Dubai International Finance Centre (DIFC). The DIFC, which is one of the most important financial hubs of UAE, has adopted the accounting principles set by AAOIFI. The DIFC acts as an independent jurisdiction and has its own courts and laws that are governed by the Law. The main aim of the DIFC is to provide businessmen with an
opportunity to expand their businesses in and out of the emerging markets of the region (DIFC 2013). The DIFC was the first organisation to follow Islamic Accounting Standards in the UAE.

6.3.4 Interview results regarding problems and difficulties with IFRS

The third question asked was about particular problems in the current adoption of IFRS. One of the interviewees said that there were serious concerns presented by the investors in the UAE regarding the application of the IFRS principles in Islamic countries. Another interviewee argued that there was always a problem of compliance with regard to the IFRS. Islamic accounting standards not only adhere to the Shariah Law but also take into account all the positive aspects of conventional accounting principles of IFRS. In this way, they not only take care of domestic transactions but also of international transactions that demand compatibility with IFRS and IFRS. So, he suggested developing some of the IFRS to comply with Shariah instead of issuing Islamic Accounting Standards. Other interviewees said that since the UAE is always perceived as one of the most important financial hubs in the region, the problem of which accounting system to choose became more pertinent and difficult for the users in the UAE. Recently it became clear that UAE, not being a member of the International Federation of Accountants (IFAC), did not commit to international pressures and discarded IFRS principles. Later, it opted for Islamic accounting standards.

6.3.5 Interviewees’ suggestions for solving these problems

The fourth question asked was about how the problems will be solved. One interviewee said that AAOIFI addressed most of the problems of Islamic countries regarding the following of IFRS, including UAE, by laying out a policy framework that tried to include Islamic principles in its standards. Another interviewee said that the accounting standards and principles set up by AAOIFI solved most of the problems of UAE’s several Islamic banks and other financial institutions. These accounting principles laid out by AAOIFI were very transparent and easy to follow. Simultaneously, these accounting principles were in accordance with the holy teachings of Quran and practices of Prophet Muhammad (pbuh), thus it won the trust and confidence of investors and native citizens of the UAE.
The opinion of another interviewee was that the financial experts of the country were in two minds whether they should stick to the IASB norms (as they had been doing for quite a while) or go for a completely unique accounting standards system. Many countries of the Middle-East region had already started complying with the Islamic accounting standards, and this new system was gradually gaining approval from all over the world, in particular, surprisingly in western countries such as UK. Another interviewee said that AAOIFI will not solve the problem. He suggested that regulators should keep adopting IFRS and develop some of IFRS to comply with Shariah. He also suggested improving the duties of Fatwa and Shariah Supervisory Board on the permissibility of Shariah principles in the Islamic banks.

6.3.6 Identification of key parties involved in implementation of Islamic accounting standards in the UAE

The fifth question asked was about the key parties involved in the implementation of Islamic Accounting Standards in the UAE. The interviewees agreed that the DIFC was one of the foremost and earliest to embrace AAOIFI’s accounting standards and played a vital role in establishing UAE’s connection with the AAOIFI norms. The DIFC is one of the most influential financial institutions in the UAE which connects both the eastern and western part of the region and is a driving force for economic development of the region. The UAE’s emergence as one of the most business-friendly global destinations in the world owes a lot of credit to the DIFC.

One interviewee added that the Dubai Financial Services Authority (DFSA) complies with the most stringent and transparent accounting principles and embraces both IASB and the Islamic accounting standards system. One of the main reasons behind the tremendous success of the DIFC as an independent corporate entity is that the DIFC has its own financial risk-regulator. This regulator is more popularly known as the DFSA. The DFSA issues licenses and supervises the financial services conducted by the DIFC. All the financial transactions conducted under the DIFC are authorized by the DFSA. The DFSA is known for its commitment to high regulatory standards and thus gives the companies an assurance that they can establish their businesses on the platform provided by the DIFC under its safe regulatory regime.
Another interviewee said that together with other autonomous independent authorities such as the DIFC courts and DIFC, DFSA amplifies the business operations of several prominent business corporations of the UAE. The other noteworthy authorities that were instrumental in the introduction of Islamic accounting standards were AAOIFI and the Finance Ministry of the UAE. However, it seemed to be an absence of knowledge of Shariah principles in the UAE financial institutes. In this way, the whole process of the implementation of Islamic accounting standards in the UAE would be taken care of.

6.4 Conclusion

The purpose of this chapter was to report the results of the surveys conducted by questionnaires and personal interviews. It began by describing the responses of professionals and managers in Islamic banks regarding accounting needs in the United Arab Emirates. Moreover, the views of key players regarding issues of Islamic accounting standards were reported. After this, the problems, difficulties and cultural issues that may be a barrier to the potential adoption of AAOIFI standards were described. Also the benefits of the potential adoption and factors that will influence or benefit from adoption were reported. This chapter presented the results from both the questionnaire survey, and the interviews, separately. In the next chapter the results will be combined and discussed in greater depth in order to answer the research questions.
Chapter 7 – Discussion of Results and Conclusion

7.1 Introduction

The chapter is organised in five main sections as follows. The first section discusses the study’s findings regarding the UAE Islamic banks’ need for accounting standards following Shariah principles, disclosure of financial reports by Islamic banks, the characteristics of International Financial Reporting Standards (IFRS), factors that influenced the adoption of IFRS, and perceptions of survey respondents regarding the merits and demerits of the adoption of IFRS. This section also explores the respondents’ views concerning the comparison of IFRS and Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) accounting standards. A detailed discussion ensues regarding the factors and issues that may act as barriers and challenges to the adoption of AAOIFI accounting standards by Islamic banks in the UAE. Consideration is given to the costs and difficulties that Islamic banks may face during the process of transitioning to the accounting standards of AAOIFI. This is followed by a discussion of the advantages and disadvantages that may arise in adopting the AAOIFI accounting standards in the Islamic banks. The second section of this chapter addresses the limitations of the current study, and conclusions are drawn in the third section. The fourth section outlines the contribution of this research, and the fifth and final section proposes avenues for further research.

7.2 Discussion of results

This section will discuss the results of the two different methods of research chosen for this study, namely personal interviews and a questionnaire survey. These findings relate to the perceptions and feedback provided by professionals and managers in Islamic banks and their need for accounting standards, and also to the perceptions of the key players with regard to Islamic accounting standards in the UAE and the adoption of AAOIFI accounting standards. Ultimately, this section considers the research findings in the context of the research questions, and the theoretical framework and the extant literature.
7.2.1 Accounting standards and information needs in Islamic banks

Islamic banks’ reporting should provide important information and data for users to assist them in the process of decision making (Hussein 2004). This section presents the findings related to the surveys conducted about Islamic bank services and activities in the UAE. These findings identified the key features of Islamic financial transactions in Islamic banks, and the need for accounting standards and disclosure in the financial reports. This section discusses the findings that answer the research questions related to the needs of accounting information in the UAE Islamic banks, and respondents’ perceptions of whether Islamic banks in the UAE need a corresponding alternative set of accounting standards rather than the currently adopted IFRS.

The survey respondents were requested to provide comments and feedback regarding particular Islamic transactions and services in relation to the accounting standards of Islamic banks. The responses were recorded in terms of a Likert scale ranging from 1 to 5, and the answers received were generally scored in the range from ‘Strongly Agree’ to ‘Strongly Disagree’. The key problems and issues raised in the questionnaire may be explained in terms of several themes. There were two key models of Islamic bank applications presented in the questionnaire, namely, the trading model and the financing model. In the financing model, Islamic banks focused solely on providing finance on the basis of Shariah principles. However, there is a concern regarding the application of IFRS for particular financial transactions of the Islamic banks, questioning whether there should be a different framework of accounting to record the financial transactions of Islamic banks. On the other hand, in the trading model, Islamic banks focused on risk-sharing which is a component of trade rather than risk-transfer which is seen in conventional banking. Islamic banking introduces concepts such as profit sharing, safekeeping, joint venture, cost plus, and leasing. Whatever model was utilized by the respective Islamic bank reflected how their business activities treated accountability in their system of financial reporting.

7.2.1.1 Islamic banks and interest rates

The survey respondents were asked to what extent the financial reports of Islamic banks included financial instruments not related to interest rates. They were also
asked whether the financial reports of Islamic banks included the disclosure of paid interest, if it existed at all, and the steps which should be taken to avoid such interest rate transactions in the future.

As a starting point, according to most survey respondents the interest rate is the core factor differentiating the services of Islamic banks from commercial banks. Notwithstanding the Islamic perspective on interest rates, survey responses in this particular study show that certain transactions related to Islamic banks have involved an interest component. Some respondents indicated that even though there had been interest involved in some transactions by Islamic banks, they did not possess the requisite knowledge to be clear as to the details, particularly given the disclosures involved the rate of interest being recorded under different terms in a category of special commissions. Some respondents indicated that the tendency to classify interest as a special commission was due to the attention that Muslim investors directed towards the term, interest. It was also mentioned that there is interest applied on late payments by Islamic banks. This approach may have been intended to ensure that Islamic banks were compared on a similar basis to commercial banks. It was confirmed by some of the respondents that Islamic banks provided loans which involved the payment of interest. One questionnaire respondent suggested that such interest charged by Islamic banks should be provided to charities.

7.2.1.2 Following Shariah principles in Islamic banks

Islamic banks exist to produce Islamic financial services (see Chapter 4, p.67). Thus, survey respondents were asked about Islamic banking services and transactions, and to what extent they agreed that Islamic bank financial transactions follow Shariah principles and how these transactions differ from those of commercial banks. Though Islamic banks have attempted to follow the requirements of Shariah principles, they vary in their interpretation of which principles are the most significant to achieve compliance. Some respondents were of the opinion that general concepts of Islamic financial transactions which applied in the Islamic banks were not enough to fully comply with the expectations of Muslims society regarding the Islamic framework accountability.
Some interviewees mentioned that although the Islamic banks adopting IFRS attempted to follow the requirements of Shariah principles, they might still be non-compliant through misunderstanding societal interests and thus the framework of accountability may be compromised. A Member of the Fatwa and Shariah Supervisory Board in Islamic Bank 4 stated:

Islamic accounting standards are based more on Islamic beliefs than on technicalities of accounting as every Muslim does look for a Shariah followed transaction. That is why AAOIFI came into the existence with its Shariah abiding laws that suited well to the nature of financial transactions taking place in the UAE.

Respondents pointed out that Islamic banks have transactions that could not sustain the application of the accounting concepts of IFRS as these were skewed towards conventional banking practices and do not reflect the Islamic financial principles of Islamic financial institutions. Some respondents added that IFRS has been drafted to account for conventional products and can be adopted only in specific parts by the Islamic banks in the UAE.

Hence, there exists a feeling amongst the majority of respondents that the Shariah principles are not given a higher priority and influence over IFRS in current considerations of Islamic financial transactions in the Islamic banks. This contributed to the suggestion that Islamic banks attempted to hide the fact that they were ignoring the interests of local investors among the current adoption of IFRS.

7.2.1.3 Disclosure of information by Islamic banks

The financial reports should provide complete disclosure and serve local needs, specifically the requirements of Shariah, such as Zakat (Benston 2000). The survey respondents were asked to what extent the financial reports of the Islamic banks included full disclosure of any and all relevant information which facilitates the users’ economic and religious decision making.

Most respondents remarked that Islamic banks had complied by implementing the corporate guidelines of Shariah principles to provide more significant information, and specific disclosures. Some respondents were also of the view that the current level of compliance inadequacy relating to disclosure, together with the simultaneous
limitations of enforcement bodies, considerably reduced the user’s ability to make correct decisions.

Additionally, respondents indicated that the listed Islamic banks in the stock market are subject to monitoring by the UAE securities and commodities authority. Since the development of the UAE securities and commodities authority, the listed Islamic banks have been obliged to provide additional information along with their financial reports, thus enhancing financial analysis and better informing investors. Respondents also agreed that local investors and stockholders need this additional information such as a Shariah compliance report along with the financial reports of the listed Islamic banks. This statement agrees with Moore’s (1997) opinion that the securities and commodities authority assisted investors and stockholders to obtain information important for making investment decisions. Some respondents also made additional comments that the requirements of disclosure of additional information which confirm Shariah compliance of Islamic banks transactions will improve and develop the stock market of these Islamic banks by attracting more Muslim investors and protecting the interests of Islamic society.

Despite the improvements in disclosure as a result of the development of the UAE securities and commodities authority, the majority of the respondents in this study were still dissatisfied with the current state of information transparency and disclosure in terms of the practicality of Shariah principles. Therefore, the findings suggest that the relevant disclosures of financial reports of Islamic banks from the perspective of Shariah principles have a limited influence on the current adoption of accounting standards in the Islamic banks.

7.2.1.4 Fatwa and Shariah Supervisory Board among Islamic banks

The interviewees were asked how to solve the problems of Islamic banks’ transactions which were not following the Shariah principles. The findings reveal that specific interviewees showed willingness for the Fatwa and Shariah Supervisory Board to work more closely with Islamic banks to improve the disclosure of information requested by Shariah, such as Zakat, for the investors. One of the interviewees noted that even though there has been inadequate disclosure, there has been recent improvement in disclosure, resulting from the presence of the Fatwa and
Shariah Supervisory Board. Some of respondents suggested that there is no need to adopt AAOIFI accounting standards because the assistant and supervisory role of Fatwa and Shariah Supervisory Board prove the compliance with Shariah principles in the Islamic banks. However, other respondents also suggested improving the role of the Fatwa and Shariah Supervisory Board regarding the permissibility of Shariah principles in the Islamic banks, rather than adopting AAOIFI accounting standards.

7.2.1.5 Zakat disclosure

The payment of Zakat is the duty of all Muslims; some researchers have argued that the primary objective of accounting in Islam is to enable Muslims to determine the amount of Zakat (see Chapter Two). One of the key objectives related to accounting from the perspective of Islamic banks in Muslim society, is enabling each and every investor to determine the value of Zakat being owed by them (Lewis 2001). Furthermore, a company’s manager is accountable for disclosing information that enables Muslims to calculate the appropriate amount of Zakat, which represents one of the orientations of accounting as fulfilling the accountability of humans to Allah (Adnan and Gaffikin, 1997).

The survey respondents were asked to what extent the financial reports of Islamic banks included information that enables Muslims to determine the amount of Zakat which facilitates the users’ economic and religious decision making. A majority of the respondents agreed that the financial reports of Islamic banks with the existing adoption of IFRS do not have methods for providing information regarding Zakat, even though some respondents showed willingness for the Fatwa and Shariah Supervisory Board to work more closely with the Islamic banks to improve the disclosure of information regarding Zakat, such required by the users.

Some respondents, who believed that financial reports which include certain items such as goodwill and capitalised expenses were suitable for the calculation of Zakat, commented that they provided all relevant information for such a calculation. However, it was agreed by most respondents that that IFRSs financial reports do not have all the details necessary to calculate the amount of Zakat, and that Zakat is based on wealth creation and on rules not easily derived from traditional financial statements.
One of the interviewees was also asked to what extent the financial reports of Islamic banks, under IFRSs, included information that enables Muslims to determine the amount of Zakat. He said that from an Islamic perspective, the emphasis on social accountability would mean that financial reports should enable Muslims to determine Zakat liability. So, Zakat must be taken into consideration. All banks must pay this to the government and this must be indicated in their financial statements. He also commented that conventional Western treatment of assets on a balance sheet under IFRSs is clearly not appropriate for these calculations, and cannot provide the necessary information for the correct computation of the amount of Zakat payable. He added that Islamic banks also do not include sufficient information that enables Muslims to determine the amount of Zakat. He was also of the view that the current level of compliance inadequacy relating to Zakat disclosure considerably reduced the user’s ability to make correct decisions.

Most respondents mentioned that Islamic banks had complied by implementing the corporate guidelines of Shariah principles to provide more significant Zakat disclosure. The respondents indicated strong support for the idea that relevant and sufficient information related to Zakat is not included in financial reports of Islamic banks under IFRS.

Some respondents also made additional comments that the requirements of disclosure of Zakat which confirm Shariah compliance of Islamic banks transactions will improve and develop the stock market of these Islamic banks by attracting more Muslim investors and protecting the interests of Islamic society. Therefore, some respondents suggested that Islamic banks should have separate financial reporting for Zakat purposes, based on the correct Zakat standard. Thus, some respondents suggest that there is a need for an accounting system capable of correctly computing and disclosing the amount of Zakat payable. The findings reveal that one of the key objectives related to accounting from the perspective of Islamic banks is enabling users to determine the value of Zakat being owed by them. Shariah principles heavily emphasize the importance of the rules of Zakat. It is regarded as an important religious rule and needs separate accounting treatments.

On the other hand, some respondents mentioned that some standards, such as Zakat standards, should be based on other standards such as AAOIFI, which are set only for
Islamic transactions. However, they argued that the omission of *Zakat* standards in IFRSs did not present a problem and that having a *Zakat* standard in AAOIFI is not particularly advantageous as this standard has little influence through *Shariah* and almost represents only the income tax, and IFRSs had more advantages. So, this study finds, somewhat surprisingly, that the specifications for *Zakat* currently in practice in Islamic banks do not represent barriers to the full adoption of IFRSs.

Therefore, the findings suggest that *Shariah* principles is not considered a priority, in particular regarding *Zakat* payments in Islamic banks’ financial reporting, and economic purposes being favoured over *Shariah*, thus giving rise to conflicts with *Zakat* purposes. Hence, *Zakat* disclosures of financial reports from the perspective of *Shariah* principles have a limited influence on the current adoption of accounting standards in the Islamic banks.

### 7.2.2 Adoption of accounting standards issued by the International Accounting Standards Board (IASB) in Islamic banks

The survey respondents were asked about currently adopted IFRS in the Islamic banks, and they were asked to evaluate the characteristics of IFRS in particular transactions of Islamic banks. Some interviewees mentioned that all countries despite their religion should adopt IFRS, and thus they do not support the introduction of Islamic accounting standards in the UAE. A branch manager in Islamic Bank 1 stated:

> The United Arab Emirates was already religiously compliant with IFRS, so there are no difficulties in keeping a track of all these financial records.

However, specific issues were identified by the survey respondents with respect to the technical application of IFRS in the Islamic banks. For example, the application of International Accounting Standard Number 37 (IAS 37) in the Islamic banks involves a degree of uncertainty because it is potentially problematic for *Shariah* compliance. IFRS 37 deals with provisions and contingent liabilities from a conventional western perspective.

However, specific issues were identified by the survey respondents with respect to the technical application of IFRS in the Islamic banks. For example, the application of
International Accounting Standard Number 37 (IAS 37) in the Islamic banks involves a degree of uncertainty because it is potentially problematic for Shariah compliance.

Vinnicombe and Park (2007) provided a comparison of AAOIFI’s FAS (Financial Accounting Standard) no.11 vis-à-vis IAS 37 revealed some substantive differences. FAS 11 is on provisions and reserves. IAS 37 is on Provisions, Contingent Liabilities and Contingent Assets. FAS 11 requires that the Islamic bank shall disclose in the notes any deductions, either as a percentage or an amount, from Mudarabah income (Profit sharing). It takes the form of a contract between two parties – one who provides the funds and the other who provides the expertise. The division of any profit is agreed in advance). FAS 11 introduces the Profit Equalization Reserve (PER) and Investment Risk Reserve (IRR) to ensure stable distribution rate of return as well as ensuring capital recovery prior to realization of distributable profit.

However, IAS 37 provisions, contingent liabilities and contingent assets outline the accounting for provisions liabilities of uncertain timing or amount together with contingent assets and contingent liabilities (possible obligations and present obligations that are not probable or not reliably measurable). Provisions are measured at the best estimate (including risks and uncertainties) of the expenditure required to settle the present obligation, and reflects the present value of expenditures required to settle the obligation where the time value of money is material. The key principle established by the standard is that a provision should be recognized only when there is a liability resulting from past events. Also a provision for onerous contracts is recognised when the expected benefits to be derived from a contract are lower than the unavoidable cost of meeting its obligations under the contract. (Vinnicombe and Park 2007).

The survey respondents generally commented that the IFRS can be applied in developing nations, though they have been created to meet the specific needs of developed nations. It was indicated by all respondents that the accounting standards currently adopted by Islamic banks in the UAE are the IFRS. The IFRS were considered to have provided characteristics of comparability and understandability with respect to the Islamic banks, although 21% of the respondents opposed this viewpoint.
It is the belief of certain researchers that creditors and investors were the most frequent users of financial reports (Ainley 2007). This was also indicated by respondents as one of the key objectives being targeted by IFRS is to improve financial reports to be most useful for decision making by creditors and investors. However, in accordance with the Islamic framework of accountability, this did not apply in Muslim societies as each and every single user comprising the society is supposed to be considered, and hence it is relevant that there must be disclosure of information to the society as a whole. Additionally, all factual and true information, as well as information which presents the institution in an unfavourable light, needs to be disclosed according to Shariah principles (Lewis 2001).

7.2.2.1 Factors that influenced the adoption of IFRS

This section discusses the findings that answer research questions related to factors and issues that influence the current adoption of IFRS in the UAE Islamic banks and considers to what extent these issues create difficulties in the application of IFRS and the benefits of applying IFRS in the UAE Islamic bank.

Respondents observed that UAE regulators i.e. the central bank and Ministry of Commerce obliged the Islamic banks to follow IFRS, and in doing so they conferred more importance to the protection of the rights and interests of other investors who hold more power, than Muslim investors. The findings also reveal factors such as, foreign investment, globalization, conventional banks and financial institutions, Islamic society, specific terminology religion and culture that influence the Islamic banks’ accounting systems, and determine the extent to which these systems are appropriate and sufficient for the information requirements of users. Certain factors which were identified by the respondents are discussed in the following sections.

7.2.2.1.1 Regulators and the adoption of IFRS

The survey respondents were asked about the extent to which the Government may influence the adoption of accounting standards in the Islamic banks. The results of this study confirm that the regulators of Islamic banks in the UAE (e.g. the Ministry of Commerce and the central bank) play a significant role in the provision of guidelines when reporting and recording financial transactions in the Islamic banks (see Chapter 3, p.40). The majority of respondents agreed that the decisions taken by
regulators in the UAE required that financial reports prepared by Islamic banks should be based on the IFRS. Islamic banks that comply with the disclosure requirements in accord with Shariah principles should also prepare financial reports based on the requirements and guidelines of the Fatwa and Shariah Supervisory Board.

The interviewees were asked also about the key parties who were involved in the implementation of accounting standards in the UAE Islamic banks. Some interviewees indicated that the central bank plays a basic role in determining the monetary policy of the country and it also controls the banking sector. They added that other players have also had a significant impact on the decision for adoption of IFRS by the Islamic banks, including the federal law, higher Shariah authority and the Ministry of Religious Endowments.

Thus, the study’s findings indicate that IFRS were applied by the Islamic banks, because the regulators of Islamic banks in the UAE had more power than other factors to implement IFRS in the Islamic banks. In this instance the other factors such as culture and religion did not have much importance in influencing the current adoption of accounting standards in Islamic banks.

7.2.2.1.2 Foreign Direct Investment (FDI) and foreign parties

The survey respondents were asked about the extent to which foreign investment may influence the potential adoption of accounting standards in Islamic banks. Respondents believed that the adoption of IFRS facilitated the growth of Foreign Direct Investment (FDI) in the UAE. The study’s findings reveal that the motivation underlying the current adoption of IFRS in Islamic banks has been mainly due to the growing economic motivation for increasing foreign direct investment, with complete adoption being one of the objectives of the Islamic banks (see Chapter 4, p.75).

Most of respondents agreed that these IFRS are important for foreign parties, for example, in the case of FDI and accounting firms internationally, instead of parties at the local level. Thus one of the key findings of this research is that respondents in the Islamic banks indicated that financial reports of Islamic banks have to be focused more on the requirements of foreign investors and international organizations and firms, than on the local users. Moreover, other respondents added that the benefits are
likely to include ease of establishment for foreign Islamic banks in free-trade zones of the country as they do not have to bear the additional cost of preparing accounts according to different accounting practices.

7.2.2.1.3 Conventional banks and financial institutions

The survey respondents were asked about the advantages to Islamic banks of adopting IFRS. The majority of respondents believed that one of the greatest benefits in adopting IFRS would be the ease of comparability of financial statements with the reporting requirements of conventional banks and other financial institutions, because of the need for uniformity and consistency with the reporting requirements of these conventional banks and institutions. The study also shows that most respondents, professionals and managers in the surveyed Islamic banks, preferred to continue dealing with IFRS because these standards are similar to the requirements of other financial institutions so the training being provided to staff members is consistent and transferable. This helps in ensuring that these employees can be transferred to different banks and financial institutions, without encountering specific issues that may arise from variations within the standards of accounting (Chapter 4, p.79).

7.2.2.1.4 Islamic society and local users

The survey respondents were asked about the extent to which local users’ needs may influence the potential adoption of AAOIFI standards in Islamic banks. It was indicated by some respondents that local accounting standards are most suitable for satisfying users’ needs. However, the major finding, somewhat surprisingly, was that the regulators involved in the implementation of accounting standards in the UAE do not tend to prioritize the requirements of Islamic society with regard to financial reports for key users.

Interviewees were also asked about the problems faced because of the adoption of IFRS and how the problems were solved. Some interviewees emphasized a serious concern among the investors in the UAE Islamic institutions regarding the application of the IFRS. A member of the Fatwa and Shariah Supervisory Board of Islamic Bank 3 stated:
As the whole of the Islamic world was coming into prominence with phenomenal economic growth, it became imperative for the financial experts for this part of the world to come up with a new unified accounting standards system that would cater for the whole region.

Another interviewee regarded the Islamic societies as key users. A member of the Fatwa and Shariah Supervisory Board of Islamic Bank 1 stated:

There was always a problem of compliance of Islamic institutions with regard to the IFRS. I personally agree with the prevailing view that adoption of IFRS reduces the local investors’ confidence in the mechanism of action of Islamic institutions and the extent of its commitment to implement Islamic law; the fact that IFRS carry the principles and foundations of the western system would cause difficulty of compatibility with the Shariah law.

On the other hand, most interviewees didn’t believe there is a fundamental problem concerning the application of IFRS in the UAE Islamic banks. One interviewee claimed that this in itself is a problem facing Islamic banks, satisfying public opinion which may affect their interests. A regional manager in Islamic Bank 2 stated:

From my point of view, the Muslim users are concerned about the current application of the Islamic transactions in the UAE Islamic banks simply because IFRS don’t carry the title of an Islamist. Local investors are focusing on the visible and not secured. Most of Muslim investors do not know the details of the mechanism of Islamic financial transactions in the Islamic banks and they don’t know how the application of Islamic standards would be in Islamic banks.

However, most respondents indicated that certain specifications or features of local accounting standards for Islamic banks in an Islamic nation are not considered a significant contemporary issue. Thus, the findings show the low impact of the factors influencing Islamic society and local users on the current adoption of accounting standards in the Islamic banks.

7.2.2.1.5 Specific terminology

The survey respondents were asked about the disadvantages of adopting IFRS into Islamic banks. The study’s findings uncovered an issue regarding the application of IFRS in conjunction with Shariah principles. Respondents indicated that the utilization of specific terminology in the accounting standards literally reflected the conventional terms applied to transactions in Islamic banks. It had also been pointed out by some respondents that there were technical issues involved in the application
of IFRS to the recording of specific transactions in the Islamic banks. Some of the concerns mentioned by respondents related to the application of the definition of insurance over the operations of *Takaful* (Islamic insurance), concepts related to leasing of *Ijarah* (Islamic mortgage) and the time value of money to record the financial instruments.

### 7.2.2.1.6 Culture and religion

The survey respondents were asked about their perceptions of the reasons that customers chose to do business with Islamic banks. The respondents nominated religion and culture as the main reasons motivating customers to deal with Islamic banks rather than conventional banks in the UAE. Another problem of culture, as evident from the response of participants, was the limited knowledge regarding IFRS in the Islamic community in general. Some respondents indicated that Islamic banks attempted to accommodate issues of culture and religion although the majority of respondents indicated that this was not a main problem. Thus, respondents indicated that the culture and compliance with *Shariah* principles do not seem to have a high priority with regard to the implementation of IFRS in Islamic banks. Some respondents noted that features of the *Shariah* principles and cultural practices cannot be considered strong factors that may influence the adoption of accounting standards in Islamic banks.

Some interviewees went to say that, in their opinion, the cultural and religious considerations are not important for the financial transactions in Islamic banks, indicating that one of the greatest disadvantages of IFRS adoption would be the conflict with Islamic principles for some Islamic products. A branch manager in Islamic Bank 1 stated:

> I personally do not see any problems with the adoption of IFRS. On the contrary, it adds credibility and the evolution of financial institutions in the country. However, we must not mix between the *Shariah* law and financial system, since the financial system requires us to keep pace with the global financial world.

On the other hand, it is the belief of certain survey respondents that not all of the accounting standards of IFRS are suitable for the Islamic banks’ environment as certain standards may be difficult to apply, or at least difficult with regard to *Shariah*
principles, and claimed that IFRS removed the essence of Shariah principles by emphasizing the concepts of time value of money and interest. Some respondents indicated that Islamic societies are very different from other societies and IFRS may not be compatible with the religion and culture of Muslim societies, or may be conflict with local commercial laws. Specific respondents commented that the there was a problem of not having a national accounting standards for the UAE. This problem was mentioned by respondents with experience in Islamic banks’ applications, advising that attempts should be made to prevent such issues arising. A few respondents also suggested that AAOIFI accounting standards have to be applied instead of IFRS in accordance with the Islamic religious root. AAOIFI standards may contribute to the production of systems of accounting within Islamic society that are significantly different from the systems of accounting in developed nations where factors such as religion and cultures do not exist (Karim 2007).

However, one significant question that was raised in this research was whether the adoption of AAOIFI standards can be considered adequate for Islamic banks, and whether it could be considered suitable for Muslim nations wherein the needs of accounting may differ from those of western nations. An analysis of the results revealed some specific and unique issues with regard to the adoption of AAOIFI accounting standards in Islamic banks. There can be significant pressure on Islamic banks involved in compliance with the Shariah principles as they are framed based on Islamic law. Such strict application of the Shariah law can sometimes discourage business and its expansion. The Shariah principles cannot be applied to every commercial entity as the AAOIFI accounting standards were especially designed for Islamic financial institutions and banking, and such standards may be inappropriate for other commercial enterprises (see Chapter 3, p.49).

Although, some respondents suggested that the full adoption of IFRS cannot cater for Shariah-compliant transactions, it seemed evident from the presentation of findings that religion and culture have a limited impact on the adoption of accounting standards of the Islamic banks.
7.2.2.2 Preference for adoption of IFRS although conflicting with Shariah principles

All Islamic banks should disclose all relevant information that helps to serve the accounting needs of the users (Moore 1997). However, this study’s findings indicate that, in the Islamic banks’ financial reports, the interests of Muslim users have been compromised by failing to fully follow the Shariah principles in those financial reports. Some of survey respondents expressed dissatisfaction with the lack of disclosure regarding specific Islamic transactions associated with the adoption of IFRS by the Islamic banks. It was agreed by most respondents that not all of the accounting standards of IFRS would be suitable for Muslim societies. Certain standards may be considered difficult to apply to some Islamic bank transactions such as Zakat, Ijarah, Musharakha and Mudharaba indicating that IFRS will conflict with the principles of Shariah with regard to some transactions.

Most of the respondents agreed that IFRS may not be compatible with the Shariah principles, but when respondents were asked about their preferences regarding the choice of implementing IFRS or AAOIFI standards, the majority of the respondents held the view that the adoption of IFRS would be more beneficial for them in comparison to the adoption of AAOIFI accounting standards in Islamic banks. Respondents agreed that the IFRS have appropriate and desirable benefits in comparison to the AAOIFI accounting standards. This is because the IFRS will involve greater benefits to the operations, services and accounting needs of the Islamic banks. IFRS will provide credibility all over the world, facilitate Islamic banking investments and allow users of financial statements to judge the ability of the entity to generate cash and cash equivalents in the future. The survey respondents also assumed that one of the greatest benefits would be that Islamic banks in the UAE would have access to better and larger sources of finance from international organizations such as World Bank and IMF, which both rely on the use of IFRS as a condition for granting loans. The respondents also suggested that the adoption of IFRS will bring about a significant change in the reporting practices of Islamic banks, and reduce information asymmetry and human bias.
Thus, the majority of respondents were of the opinion that it is appropriate for Islamic banks to continue adopting IFRS and comply with supervision and guidelines from the Fatwa and Shariah Supervisory Board.

7.2.2.3 The role of key players in adopting IFRS and AAOIFI standards

It has been indicated by some respondents that the financial rules and regulation of IFRS are in favour of conventional banking. Since the Muslim community is the major part of the UAE economy, it was suggested by some respondents that Islamic banks need to start adopting AAOIFI accounting standards which are acceptable to Muslims in society. Some previous studies such as Dale (2007) indicated that information disclosed in financial reports will be on the basis of the regulators’ interests and their exercise of appropriate power. It was also indicated by some respondents that the regulators of accounting standards have greater ability, relative to the users of accounting information, to protect their interests with regard to the accounting regulations in Islamic banks. This issue can also be explained in terms of the weak laws in the economic system and which are not always helpful for Islamic banks when in need of help and support (see Chapter 4, p.77).

However, the respondents noted that Islamic banks usually failed to consider the key interests of society, when it is supposed that those interests are extremely important. Some respondents also indicated that Islamic banks should be working more closely with the Ministry of Commerce and central bank to update accounting regulations and compel the Islamic banks in the stock market to implement the regulations that will assist Muslim investors in making appropriate decisions. The central bank of the UAE has the responsibility to control and enforce the accounting regulations in Islamic banks (Essays, UK 2013). This suggests that the current extent of transparency and disclosure as given in the IFRS are in sympathy with the interests of the preparers of accounting standards, rather than the interests of the users.

The study reveals that IFRS were followed in the Islamic banks, but were sometimes in conflict with Islamic concepts and Shariah principles, and this led to a lack of uniform disclosure in accounting reports in the Islamic banks. Specific respondents pointed out a number of irregularities in Islamic banks’ transactions; for example the management of the Islamic banks don’t pay Zakat directly; it is the responsibility of
shareholders to pay their own Zakat. It is expected that such irregularities will to some extent be subject to compliance with Shariah principles due to the introduction of AAOIFI accounting standards.

It has been suggested by some researchers that the Accounting and Auditing Organization for Islamic Financial Institutions could play an important role developing uniformity in Accounting Standards (Shanmugam, Perumal & Ridzwa 2004). Some respondents suggested that Islamic banking should have a proper regulatory and institutional framework in the UAE. This will improve the uniformity of financial reporting in Islamic banking services and will also be helpful to all customers and investors.

The interviewees were asked about the first efforts made toward introducing Islamic accounting standards in the UAE. It has been indicated by the interviewees that the Dubai International Finance Centre (DIFC) was the first organization that followed Islamic Standards in the UAE. Some interviewees mentioned that DIFC is an independent corporate entity and has its own financial risk regulator. This regulator is known as the Dubai Financial Services Authority or (DFSA). DIFC together with other autonomous independent authorities such as the DIFC courts and Dubai Financial Services Authority (DFSA) lobbied regulators and accounting standards setters in the UAE to adopt Islamic accounting standards to establish legislation that economically benefited its business operations in the UAE. Thus, evidence exists which suggests that interest groups lobbied for the adoption of AAOIFI accounting standards.

The interviewees indicated that DIFC was one of the foremost entities, and the earliest, to embrace AAOIFI’s accounting standards and played a vital role in establishing UAE’s connection with the AAOIFI. A member of the Fatwa and Shariah Supervisory Board of Islamic Bank 3 stated:

Dubai International Finance Centre is the first which started operating with the launch of the Islamic accounting standards in the UAE. It is one of the most important financial hubs of the UAE which was the first organisation to adopt the accounting principles set by AAOIFI. It also, acts as an independent jurisdiction and it has its own courts and laws that are governed by the Law.
The majority of respondents illustrated that both *Shariah* principles and the commercial law of UAE have influenced Islamic financial transactions within Islamic banks. It was clear from the respondents’ comments that AAOIFI standards were developed to support compliance with *Shariah* principles and Islamic culture and to follow the commercial law of UAE. However, it was also clear from the answers of the respondents that there exists weaknesses in the enforcement process, as the current interest of local users and entities are insufficient for enforcing the adoption of AAOIFI standards by Islamic banks in the UAE. Respondents agreed that almost all the financial institutions in the UAE adopt IFRS, and the supervisory authority is the central bank and the Ministry of Commerce. Islamic banks also follow this pattern.

### 7.2.3 Comparison between IFRS and AAOIFI accounting standards

This section discusses the findings that answer the research questions related to respondents’ perceptions regarding the main differences between the application of AAOIFI accounting standards and the IFRS, identifying the system that better satisfies users’ needs. There was a general agreement among the respondents that the adoption of the AAOIFI accounting standard may result in the availability, or greater disclosure, of more detailed information to local investors with respect to *Shariah* principles. However, the respondents agreed that foreign investors will receive greater benefit from adopting the IFRS rather than the AAOIFI standards.

#### 7.2.3.1 Comparing the financial reports of Islamic banks under IFRS and AAOIFI accounting standards

According to IASC all relevant information needs to be disclosed in financial reports (IASC 1989). Respondents agreed that the financial reports prepared under AAOIFI accounting standards will provide more information for Muslim users than those prepared under IFRS, improving the disclosure of relevant information to facilitate local users’ economic and religious decision making.

The findings focus on some differences between the application of IFRS and AAOIFI standards in the Islamic banks, indicating that a majority of respondents believed that the application of the IFRS to all transactions of Islamic banks would be very difficult and rigorous in nature. For example, lease transactions, contracts of a restricted nature and investment accounting, were major areas of differences. These differences have
been raised for two major reasons. First, the IFRS have been developed according to the requirements of the western society objectives and cultures. Second, there were significant differences in understanding the principles and practices between Islamic banks and conventional banks.

According to respondents, financial reports are based on two key models of Islamic banks, namely a trading model and a financing model. In the financing model, Islamic banks focused solely on providing finance on the basis of Shariah principles. Some respondents expressed concern regarding the application of IFRS for particular financial transactions of the Islamic banks, questioning whether there should be a different framework of accounting to record the financial transactions of Islamic banks.

Some respondents felt that applying AAOIFI standards is the only option for Islamic banks if they want to address the specific requirements of accounting for Muslim users. However, the majority of respondents showed a preference for the financial reports that had been prepared under IFRS because of their understandability and their implementation at reasonable cost and also because IFRS allow for the exercise of appropriate professional judgment. This implied that IASB is perceived by respondents as more rigorous and more capable regulatory body vis-a-vis the AAOIFI.

### 7.2.3.2 Comparing the application of Zakat under IFRS and AAOIFI accounting standards

Zakat is one of the major differences between IFRS and AAOIFI standards. A question in the questionnaire survey asked to what extent the financial reports of Islamic banks included information that enables Muslims to determine the amount of Zakat. The respondents indicated strong support for the idea that relevant and sufficient information related to Zakat is not included in financial reports of Islamic banks under IFRS. They added that Islamic banks do not include sufficient information that enables Muslims to determine the amount of Zakat. For example, the respondents noted that the IFRS allow the use of fair value measurement of investment property under (IAS 40) which doesn’t provide accurate information for Zakat. However, under AAOIFI standards it must be measured at historical cost under
(FAS 9) which provides accurate information for Zakat as agreed by the majority of respondents. Some respondents indicated that IFRS also did not consider the Zakat entry as a charity obligation.

One of the key objectives related to accounting from the perspective of Islamic banks in Muslim society, is enabling each and every investor to determine the value of Zakat being owed by them (Lewis 2001). Shariah principles heavily emphasize the concepts of Zakat. It is regarded as an important religious rule and needs separate accounting treatments. The holy Quran stated the basic principles on Zakat and the duty of paying Zakat in the following Ayat (verses):

> Righteousness is not turning your faces towards the east or the west. Righteous are those who believe in GOD, the Last Day, the angels, the scripture, and the prophets; and they give the money, cheerfully, to the relatives, the orphans, the needy, the traveling alien, the beggars, and to free the slaves; and they observe the Contact Prayers (Salat) and give the obligatory charity (Zakat); and they keep their word whenever they make a promise; and they steadfastly persevere in the face of persecution, hardship, and war. These are the truthful; these are the righteous. (Qur’an 2: 177)

A majority of the respondents agreed that the financial reports of Islamic banks with the existing adoption of IFRS do not have methods for providing information regarding Zakat, even though some effort has been made through Islamic banks by the Fatwa and Shariah Supervisory Board to follow the principles of Shariah.

Specific respondents noted that this leads to most Muslim investors not relying on financial reports issued by the Islamic banks. This implies the inappropriateness of the application of IFRS within the framework of Islamic accountability. As a consequence, the users of Islamic accounting did not have the ability to make fully-informed decisions. On the other hand, the majority of respondents also considered that adopting AAOIFI standards by Islamic banks could provide data associated with the requirements of Shariah principles. This could be prepared and disclosed in accordance with assessments of fair value which could also be relevant for Zakat calculations.
7.2.3.3 Issues of language

It has been found by some researchers, such as Karim (2009), that there exists a positive relationship among nations where English is considered the key language where IFRS are being adopted. It may be argued that in nations where an Anglo-American culture is present, the adoption of IFRS is relatively easy. This is due mainly to the fact that the key language of IASB is English (Karim 2009). In Shariah law, the official language is Arabic. However, an official translation in Arabic has been included in the available AAOIFI standards. With respect to these findings, it is noted that most of the respondents did not mention the issue of language as a significant problem; only a few respondents explicitly indicated that language could be a problem.

One of the survey respondents mentioned that Islamic banks are still experiencing issues of language, due specifically to not having appropriate resources. Another questionnaire respondent suggested that the accounting terminology related to AAOIFI standards should preferably be translated into Arabic for Islamic banks.

Translations from English to Arabic are problematic, as Arabic is less close in relation to English, than it is to German and French (IASC 1989). Therefore, there is the possibility that a particular English translation into Arabic may not necessarily be correctly understood or applied.

7.2.4 Potential adoption of AAOIFI by Islamic banks

This section discusses the findings regarding the research questions such as the potential benefits and other impacts of applying the AAOIFI accounting standards, respondents’ perceptions of the underlying factors and issues that may influence the adoption of AAOIFI accounting standards in the UAE Islamic banks, and to what extent these issues might act as barriers, difficulties and costs related to the adoption of AAOIFI accounting standards.

7.2.4.1 Appropriateness of AAOIFI accounting standards

The appropriateness of AAOIFI accounting standards to Islamic banks was also examined in the surveys. The interviewees were asked about the reasons behind the introduction of AAOIFI in the UAE. Some interviewees mentioned that the reason for
introducing the Islamic accounting standards in the UAE is the growing demand by some Islamic institutions for AAOIFI standards. They also mentioned the influence of some institutions in neighbouring countries, such as the influence in the Gulf area which has already introduced the Islamic accounting standards and this has an impact on the institutions in the UAE due to the strong partnership of UAE with these countries. A member of the Fatwa and Shariah Supervisory Board in Islamic Bank 4 stated:

As we know Islamic authorities all over the world have gradually started opting for Islamic accounting standards developed by the AAOIFI. Of course, as the UAE is an important country in the Islamic world, it had to show compatibility with the AAOIFI accounting standards.

One interviewee also mentioned that the UAE is not a member of the International Federation of Accountants (IFAC) which means it did not have to submit to the international pressure to adopt IFRS and can abandon the IFRS principles later and then adopt the Islamic accounting standards.

Previous studies, such as Hitchins, Hogg and Mallett (2001), argued that the AAOIFI standards creation was based on Shariah principles. It was commented by some respondents that Islamic banks should cease adoption of IFRS with which Muslims investors in the Islamic environment were unfamiliar, and instead use the standards of the AAOIFI which take into account the Shariah requirements. Some respondents remarked that Islamic banks must follow the rules set out in the Shariah principles; the applicability of IFRS is difficult to implement in particular financial transactions, such as Ribaa, Zakat, Mudharaba and Musharaka which were designed to follow Islamic principles. So, the findings suggest that AAOIFI standards will gain advantage from the specific issues involved in applying IFRS with respect to the identified Islamic financial transactions in Islamic banks. Therefore, the respondents opined that the AAOIFI standards were based on the objective of implementing Shariah principles in accounting practices with regard to these issues.

The findings also reveal that there were some sectors in the UAE economy that prefer to implement AAOIFI accounting standards where financing was prohibited, and to support financing in other areas with the use of instruments such as Murabaha (Profit
sharing), *Ijarah* (Lease financing) and *Istisnah* (Advance purchase). A member of the *Fatwa* and *Shariah* Supervisory Board in Islamic Bank 3 stated:

Also, in other sectors such as the real estate development sector; some developers in the UAE are leading the global Islamic economy with serviced apartments that are *Shariah* compliant from their direct financing to their properties. Some developers also launched the fully certified *Shariah*-Compliant serviced apartment hotels in the UAE.

Furthermore, it was stated by some survey respondents that AAOIFI accounting standards did not allow the application of the principle of time value of money with respect to a contract of exchange where there are deferred payments involved. There is a strict prohibition on transactions based on debt and interest payments in the AAOIFI standards.

Questions were also asked of the survey respondents about their perceptions of the impact of applying the AAOIFI accounting standards in the UAE Islamic banks. It has been remarked by some respondents that Islamic banks should seek and follow the *Shariah* principles. An analysis of the survey respondents’ answers revealed that *Shariah* principles tended to have a significant influence on the application of Islamic financial transactions in Islamic banks.

**7.2.4.2 Potential benefits of AAOIFI accounting standards**

The survey respondents were asked about the main reasons for preferring the AAOIFI accounting standards, and whether the benefits of AAOIFI standards for Islamic banks in the later stages of implementation would outweigh the initial costs incurred. The respondents noted that the impact of AAOIFI accounting standards will improve the disclosure of any relevant information in the financial reports which will facilitate the users’ economic and religious decision making in the Islamic banks. Some respondents claimed that AAOIFI was created for Islamic financial institutions and it’s more acceptable to the Muslim communities. Other respondents also indicated that AAOIFI accounting standards will lead to a representation of Islamic financial products in Islamic banks and cover all Islamic financial transactions. Moreover, some survey respondents indicated that AAOIFI accounting standards are compatible with the beliefs and culture of local investors, and abide by the principles of *Shariah*. 
Another significant issue was highlighted in the respondents’ comments. It was pointed out by the respondents that AAOIFI standards promote the concepts of fairness, justice and social balance, as suggested in the Shariah principles. Shariah law embodies principles of justice and fairness and aims to secure a balanced society in an Islamic community. Hence interest rates, gambling and taking excessive risk, were prohibited to protect the social lives of Muslims.

Moreover, some interviewees mentioned that the adoption of AAOIFI standards will enhance the confidence of investors regarding Islamic financial institutions in the UAE, and it will benefit and increase the size of its investments. A member of the Fatwa and Shariah Supervisory Board in Islamic Bank 1 stated:

AAOIFI standards solved most of the common requirements of UAE’s Islamic banks and other financial institutions. These accounting standards are very transparent and easy to follow. Simultaneously, these accounting principles were in accordance with the holy teachings of Quran, thus it won the trust and confidence of investors and native citizens of the UAE.

However, the results of the questionnaire survey indicated that there were significant differences of opinion among the respondents regarding the advantages of adopting the AAOIFI accounting standards. The majority of survey respondents expressed a low level of agreement with the argument that the benefits of AAOIFI standards for the Islamic banks in the later stages of implementation would outweigh the initial costs incurred.

### 7.2.4.3 Implementation of AAOIFI accounting standards

The survey respondents were asked whether Islamic banks would implement AAOIFI standards unilaterally or outsource part of the task to auditors and analysts to complete the transition process. Thus, respondents indicated that Islamic banks would act independently in transitioning through the implementation of AAOIFI standards; however, the respondents recognized that accountants of Islamic banks should be required to have knowledge of Islamic ethical and legal aspects. In this light, some respondents indicated that the accounting and auditing organization for Islamic financial institutions will be beneficial in adopting its accounting standards as there seemed to be an absence of knowledge of Shariah principles amongst the majority of the professionals and employees in Islamic banks. Survey respondents also suggested
that AAOIFI should take guidance from IASB, create an advisory group, provide education to the accounting professionals of Islamic banks and engage professionals from the finance industry to meet its goals of both timeliness in completing projects on its agenda and adopting a rigorous due process in developing its standards.

Shariah principles were a major source of guidance in the development of the AAOIFI standards. The findings indicated that the extent, to which Shariah principles are observed within the settings of AAOIFI accounting standards, is dependent on the efforts of AAOIFI key players. The development of AAOIFI accounting standards was based on Muslim societies’ religious needs to solve accounting problems (see Chapter 3, p.51). Thus, in the light of an increased number of operations at an international level, where the Islamic banks are contributing significantly to international trade with other Muslim countries, some respondents mentioned that the development of AAOIFI standards is beneficial because these can provide clear guidelines to record the Shariah financial transactions in an Islamic way in Islamic banks.

Survey respondents were also asked about their perceptions of which areas of the financial services that are likely to be affected by the implementation of AAOIFI accounting standards in the Islamic banks. Respondents indicated that they expected a high impact as a consequence of the implementation of AAOIFI standards on investor relations and credit rating. However the responses indicated the neutral impact of the implementation of AAOIFI standards on capital management, earnings volatility, dividend policy, investment operations and debt management. Nonetheless, the responses indicated that there will be a low impact as a consequence of implementation of AAOIFI standards on prudential capital adequacy and securitization activities.

On the other hand, the respondents thought that the cost of the implementation of AAOIFI accounting standards would comprise both time and resources. Respondents also felt that AAOIFI standards would be more time consuming for implementation as compared to the IFRS. Some respondents noted that although AAOIFI standards have their own limitations as far as coverage and costs are concerned, they expected that over a period of time these standards would become more widely applied and covered through the introduction of new provisions arising from operational experience.
7.2.4.4 Problems of implementing AAOIFI standards

The respondents were asked about the most significant impediments to the adoption of AAOIFI standards by Islamic banks. Based on the study’s findings, it can be concluded that the implementation of AAOIFI standards in Islamic banks will give rise to certain problems (see Chapter 3, p.63). These will include an absence of appropriate knowledge and experience that may provide assistance to employees of Islamic banks in the application of professional judgment, issues related to fair value, alternative methods in regard to certain standards, the scope of comparisons with the financial statements of other financial institutions, costs of training, the need for adaptation of IT systems and consultancy services.

Financial statements prepared under accounting standards that differ from IFRS will possibly give rise to problems of comparability, creditability and reliability relative to financial statements prepared globally (Lovett 2002). Some interviewees mentioned that the adoption of AAOIFI accounting standards would not be an optimal solution for Islamic banks. Because, the issue of implementation of AAOIFI standards will give rise to economic and investment problems, for example, they will increase restrictions on foreign investments. For this, they thought it is better to find solutions suitable for Islamic financial transactions through the creation of a mechanism to apply specific IFRS. A regional manager in Islamic Bank 2 stated:

We cannot fix a problem by creating other problems. On the contrary, in my opinion, the adoption of AAOIFI standards will create new accounting and economic problems which may be difficult to avoid them. Most anticipated problems will be how to deal with international transactions and how to attract foreign investors.

7.1.4.5 Factors that influenced the potential adoption of AAOIFI accounting standards by Islamic banks

This section discusses the findings that answer research questions related to factors that may influence the potential adoption of AAOIFI accounting standards in the UAE Islamic banks, and these issues might act as barriers to their adoption. Certain factors and issues which were identified by the respondents are discussed in the following sections.
7.2.4.5.1 Local users

The adoption of AAOIFI accounting standards by Islamic banks requires the implementation of structures and processes to protect society’s interests (Chapter 4, p.73). The survey respondents were asked about the extent to which local users’ needs may influence the potential adoption of AAOIFI standards in Islamic banks. Some survey respondents indicated that there was a current lack of regulations to assist in protecting the interests of society, and in particular, bank customers.

Archer (2005) argued that higher disclosure results in competitive benefits. Some survey respondents thought that the AAOIFI standards may provide greater disclosure of Shariah requirements in comparison to the IFRS currently being adopted by Islamic banks in the UAE. There was a complete agreement amongst survey respondents that the adoption of AAOIFI may result in more detailed disclosures and the provision of more information in terms of the Shariah principles for local bank users. The study’s findings indicate that the adoption of AAOIFI standards will focus more on the bank’s investors compared to the bank’s executives.

However, some interviewees mentioned that investors may become confused with IFRS, because it is compatible with the global financial system but it is not compatible with Shariah principles. One interviewee commented that AAOIFI accounting standards only changed those principles of IFRS which were in conflict with Shariah principles; however other disclosure and accounting principles were the same as in IFRS. A branch manager in Islamic Bank 1 stated:

> on the other hand, you must know the fact that AAOIFI accounting standards should not only abide by the Shariah, but also they should take into account all the positive aspects of conventional accounting standards of IFRS.

At the same time, a survey respondent remarked that the needs of local users seemed to have limited influence on the adoption of IFRS or the benefits flowing from the adoption of the AAOIFI accounting standards. As noted previously, one of the key advantages of having AAOIFI accounting standards would be an increase in the degree of disclosures which may serve the needs of local and Muslim users. Accordingly, AAOIFI accounting standards are regarded by respondents as being more consistent with the objectives of accounting in Islamic banks, and the alignment with Shariah principles.
However, the majority of respondents indicated that the system of accounting in the Islamic banks may be driven by the needs of foreign investment rather than the needs of local investment. Therefore, the findings suggest that local users have a limited influence on the adoption of accounting standards in the Islamic banks, and they don’t have the power necessary to protect their interests in Islamic banks.

7.2.4.5.2 Education background

Some survey respondents tended to believe that one of the disadvantages of AAOIFI standards was that the implementation of these standards was highly dependent on the education background of Islamic bank employees and their understanding of, and familiarity with, the Shariah principles.

Most respondents also agreed that the AAOIFI standards when used in conjunction with international transactions, would take more processing time. The study’s findings further suggest that other implementation costs, such as changes required in systems of software and consulting services, may be incurred through the adoption of AAOIFI standards. Indeed, the majority of respondents believed that huge difficulties will be encountered in terms of the time and resources by Islamic banks in financial reporting if changes were made in the adoption of the accounting standards of Islamic banks. The issue of how Islamic banks will attempt to weigh the costs and changeover benefits of the potential adoption of AAOIFI standards is an important issue to be resolved, and was highlighted by the respondents.

Many respondents also indicated that even with the current level of training offered by AAOIFI, the number of training sessions and their appropriateness are still not adequate. Some respondents further indicated that the training session organizers have influenced those who implement the accounting standards in Islamic banks, to specifically prefer AAOIFI accounting standards, instead of other accounting standards such as IFRS. This led to the suggestion that accounting staff in Islamic banks will require more training sessions which will involve a major expenditure to be incurred by these Islamic banks to adopt AAOIFI accounting standards. Even though this will enhance their knowledge related to accounting standards, doubts can be raised with regard to the advantages of the training sessions’ content related to enhancing knowledge of AAOIFI accounting standards. Respondents also pointed out
that there is a lack of adequate resource materials related to AAOIFI accounting standards in Islamic banks. Solutions were suggested by some respondents with respect to the issues involved in adopting AAOIFI standards. The respondents suggested that there is a need to develop an accurate understanding of the Islamic Shariah principles. They also pointed out the need for providing proper education and training to the employees of Islamic banks related to accounting and banking principles, the development of related reading content and study materials regarding Islamic accounting principles, and encouraging more research to be undertaken on these issues.

Therefore, the findings suggest that the lack of knowledge by professionals in Islamic banks regarding AAOIFI standards, tended to significantly influence the non-adoption of AAOIFI accounting standards by Islamic banks.

7.2.4.5.3 Foreign Direct Investment (FDI)

The survey respondents were asked about the extent to which foreign investment may influence the potential adoption of AAOIFI standards in Islamic banks. A majority of the respondents indicated that the increased involvement of FDI had been an important advantage in adopting IFRS in Islamic banks, and at the same time was a significant disadvantage for adopting AAOIFI accounting standards. The financial statements of all firms in the UAE are prepared in accordance with IFRS, which will be readily comparable to foreign firms which will encourage foreign investments (Zoubi & Al-Khazali 2004). A majority of respondents also indicated that adopting IFRS assisted the entry of foreign investors due to the ease of understanding IFRS. As more individuals become involved in stock investments, there will be an increased need to use the accounting standards that are well-understood across the globe compared to the accounting standards based on Shariah principles. As more Islamic banks trade within the global market, there will be an increased need for the preparation of financial statements that can be readily understood more widely across the globe than those reports prepared on the basis of AAOIFI accounting standards. Some interviewees also mentioned that they do not see any compelling reason to introduce AAOIFI standards in the UAE. They believed that with the bright prospects occasioned by UAE’s substantial oil and gas resources driving its economy, investors
the world over will see the opportunity to invest in the UAE and gain benefits from the country’s development. A regional manager in Islamic Bank 2 stated:

Therefore I do not see any need to use AAOIFI in the UAE because it interferes with the functioning of foreign institutional investors.

Some respondents also commented that a number of other developing nations have recently been making attempts to attract international investment. These nations are unlikely to set local accounting standards or adopt Islamic accounting, which despite being considered suitable for the requirements of their nation, could be a deterrent to international investors.

Some respondents also indicated that a number of Islamic banks have recently made attempts to attract foreign investment and therefore, there was no scope for also adopting accounting standards that may be suitable for the requirements of the Shariah principles. The findings of this study confirm Heffernan’s (2003) point of view, which stated that financial reports were prepared in developing countries in accord with the needs of FDI, irrespective of the needs of the local users, and thus did not take into consideration the culture and religious factors.

This study’s findings suggest that with regard to Islamic banks, the attraction of FDI and the economic consequences has been a major consideration in the adoption of IFRS by Islamic banks in the UAE. Thus, the findings confirm that FDI tended to have a significant influence in the non-adoption of AAOIFI accounting standards by Islamic banks.

### 7.2.4.5.4 Big Four and global organizations

The survey respondents were asked about the extent to which the Big Four accounting firms (PricewaterhouseCoopers, Deloitte Touche Tohmatsu, Ernst & Young, and KPMG) and global organizations may influence the potential adoption of AAOIFI standards in Islamic banks. The majority of respondents suggested that multinational organizations and international accounting firms, especially the big four, gained benefit from the current adoption of IFRS. These Big Four firms were also noted as having significant influence over the scope of adoptions.
There exists a strong relationship between the Big Four accounting firms, Multi-National Corporations (MNCs) and FDI, as they are known to be working to adopt IFRS (Karim 2007). Various audit firms in the UAE are recognised as being regional offices of large international firms, whereas other audit firms were recognized as being small and relatively independent (Haniffa & Cooke 2002). Some respondents also indicated that winning the confidence of investors was more probable when financial statements were audited by international accounting firms, especially those affiliated with one of the big four, rather than being audited by local and independent accounting firms.

The interviewees were asked about the key parties who were involved in the implementation of accounting standards in the UAE Islamic banks. Some interviewees commented that the main player that determines the adoption of the accounting standards in the Islamic banks is the central bank. But the active role played by other entities must be taken into account, such as the World Bank and the International Monetary Fund (IMF), both major players in pushing UAE towards adoption of IFRS. The Big Four international accounting firms which are operating in the UAE require their clients to prepare financial reports under IFRS. Thus, the findings confirm that the big four and the global organizations tended to have a significant influence in the non-adoption of AAOIFI accounting standards by Islamic banks.

7.2.4.5.5 Comparability with other financial institutions

The study also shows another disadvantage of the AAOIFI accounting standards within the accounting system of Islamic banks, related to the comparability of certain transactions of Islamic banks with those of other listed financial institutions.

The AAOIFI standards differ from the IFRS with regard to fundamental principles, such as, the provisions and contingent liabilities under IFRS compared to those published by the AAOIFI standards, will be insufficient to draw firm conclusions regarding the implications of Islamic financial transactions (Vinnicombe & Park 2007). However, the study’s findings reveal that the AAOIFI standards comply with Shariah principles, and for the international investor it is very difficult to analyse and compare financial transactions based on AAOIFI accounting standards. Some
respondents indicated that it was not possible that all IFRS were depicted in accordance with Shariah principles, and hence there were contradictions between IFRS and AAOIFI accounting standards.

Thus, the findings confirm that the difficulties in comparing certain transactions of financial statements under AAOIFI accounting standards with those of other IFRS financial statements, tended to have a significant influence for Islamic banks in choosing not to adopt AAOIFI accounting standards by Islamic banks.

7.2.4.5.6 Influence of developed nations on developing nations

The needs of accounting can be considered differently with regard to developing nations compared to those of developed nations, due to variations in culture and a number of other factors (see Chapter 3, p.47). The impact of the developed nations has become apparent in regulating the systems of accounting and businesses, which facilitated the adoption of IFRS by financial institutions in developed nations (Haskins 2004). The survey respondents agreed that IFRS was created to meet the needs of developed countries.

The accounting profession in developing nations may be facing huge constraints with respect to IFRS adoption (Karim 2009). However, the survey respondents disagreed with the proposition that the IFRS were impractical for developing nations. The respondents also agreed that the standards of accounting formulated for the needs of Islamic developing nations i.e. AAOIFI accounting standards, may not be best suitable for Islamic banks. Accordingly, the respondents revealed that the UAE being a developing nation may not necessarily represent a barrier or challenge in adopting the systems of accounting from developed nations i.e. IFRS. Some respondents noted that Islamic banks engage international auditors from developed nations and are thus involved in the transference of accounting technology to, and influencing the accounting practices of, developing nations. In addition, some survey respondents noted that adoption of IFRS by developing nations may be important for Islamic banks’ accounting, as their financial reporting requirements need to provide investors with important accounting information.

The study’s findings suggest that even though the Islamic banks made attempts to follow the requirements of Shariah principles, they might still be in conflict with
those requirements through ignorance of the local interest by not adopting AAOIFI accounting standards. Nonetheless, the findings confirm that the developed nations tended to have a significant influence on developing nations to adopt IFRS.

7.3 Conclusion

To achieve the main objectives of this research, a pragmatic approach was applied. This process allowed the researcher to adopt a research design based on a combination of quantitative and qualitative methods. A general picture was formed of the challenges and barriers confronting the potential adoption of AAOIFI standards in Islamic banks. A more detailed investigation was based on qualitative methods extended by interpretive processes, allowing meaningful conclusions to be drawn from the main findings. This study’s findings enhanced an in-depth understanding of the factors influencing the adoption of IFRS in Islamic banks, together with an assessment of the extent to which AAOIFI standards are needed to meet Shariah requirements.

The research findings demonstrate that there was a general consensus amongst the UAE Islamic banks’ respondents regarding the adoption of IFRS and their related benefits. It was agreed by the respondents that the adoption of IFRS improved financial reporting by the Islamic banks with regard to relevance, reliability, comparability and comprehension resulting in an increase in the level of confidence of local investors in the financial reports of Islamic banks and in foreign investment opportunities. Various benefits were also indicated relating to time savings and expenditure involved in the adoption of IFRS. The findings, however suggest that some respondents were of the view that the IFRS were not entirely suitable for adoption within Islamic banks.

The main research findings reveal that financial reports have to be directed towards the main user groups of analysts, collaborative creditors, international firms and organizations and foreign direct investors. These were the most crucial users groups towards whom financial reports of reporting entities are usually targeted. Such findings suggest in consequence, the adoption of IFRS. Most respondents also indicated that key players involved with the implementation of IFRS in the Islamic banks, did not implement accounting standards accurately, and thus did not protect
the Islamic banks’ best interests. Even though respondents acknowledged the importance of foreign direct investors and international firms and organizations as important users of financial reports, the research findings indicate that some respondents were not completely satisfied with the disclosure and transparency levels of IFRS as implemented by the Islamic banks. This may influence the ability of accounting users to make well-informed decisions. The findings also suggest that Islamic banks’ current financial reporting might be limited in achieving the local users’ objectives consistent with the Shariah principles.

The research reveals that key players associated with accounting standards in the Islamic banks tend to avoid enhanced financial disclosure for their own self-interest, perhaps suggesting why significant effort is often expended in lobbying for regulation of accounting in the Islamic banks. However, the research findings indicate that a stronger regulatory oversight was needed for the continued operation of IFRS. It was also suggested by some respondents that an important role was played by the UAE central bank in implementing IFRS effectively in Islamic banks.

According to some respondents, significant issues of culture and religion have arisen as a consequence of the IFRS adoption by the Islamic banks, such as the specific terminology of Shariah principles and language translation from English to Arabic. This also indicates a probable issue for listed Islamic banks in the stock market and may also present a challenge for Islamic banks at the local level because of resource limitations. The research findings indicate that interest is included in certain transactions by various Islamic banks reporting in the stock market. Research respondents have suggested that disclosure by Islamic banks was insufficient for the purposes of applying Shariah principles, such as disclosing data that helps to calculate the Zakat amount.

Even though most of the respondents were not satisfied with the present level of disclosure and the inclusion of interest in some transactions, they were more satisfied with the financial reports prepared under the IFRS regime as compared to those prepared in accordance with AAOIFI standards. The research findings confirm that the factors of religion and culture have a limited effect on systems of accounting.
However, the findings indicate that even though the AAOIFI standards served the needs of accounting at the local level with respect to religious and cultural purposes, they could be significantly enhanced for economic purposes. It was further suggested by the respondents that factors related to economic issues are over-ridden by religious and cultural factors in the accounting systems of Islamic banks. Additionally, the accounting standards included a political component indicating that those regulating the systems of accounting protected their interests to the possible disadvantage of accounting and financial report users. The findings also indicate that there is limited knowledge of AAOIFI standards by Islamic bank professionals and managers, and that can be attributed to their ineffectual education and training. Thus, the research findings show unanimity with regard to the difficulty in understanding Shariah principles and Islamic standards, the lack of in-depth knowledge of Islamic financing opportunities, the inadequate number of interested candidates and Islamic financial experts engaged in accounting and a shortage of literature and research available on the subject of Islamic accounting and banking.

It was also revealed from an analysis of the respondents’ answers that there are deficiencies in accounting practices reflected in the environment and culture of Islamic banks locally, as well as the influence of western culture on the regulations in Islamic banks. Some respondents in this research suggested that a substitute for the AAOIFI standards may be of benefit for Islamic banks insofar as it may make possible a choice amongst available standards appropriate for Islamic banks to achieve harmonization of accounting processes. Henceforth, it was thought by respondents that before the adoption of AAOIFI standards, the cost should be questioned as well.

The findings reveal that factors such as the influence of religion, culture and local investors, may have limited effect on the current adoption of accounting standards in the Islamic banks, as compared to economic and political factors such as regulators, foreign investment, and global financial institutions which have major influences on the Islamic banks to adopt IFRS. Furthermore, the findings ensure an awareness of issues that may develop when Islamic banks commence the transition to AAOIFI standards, such as the prevention of FDI, affecting the relationship with the big four accounting firms, giving rise to certain costs of time and sources and limiting the
comparability with financial statements of other financial institutions. The current study’s findings also indicate that the degree of agreement amongst respondents supports the adoption of IFRS; however, the respondents’ opinions do not also reflect a perception that all the IFRS are suitable for application with regard to Shariah transactions.

Most respondents were in disagreement regarding a decision to fully adopt AAOIFI standards by Islamic banks, as they did not believe that the consequent financial reports would improve the quality of reporting by the Islamic banks. Therefore, the findings suggest not replacing IFRS, but to find a way to comply with AAOIFI standards alongside the adoption of IFRS by Islamic banks in the UAE. This may demonstrate that such application will support the achievement of the specific purposes of Shariah principles, such as enhanced disclosure using just values for calculation of Zakat.

### 7.4 Limitations of this study

In light of the research analysis and findings, the researcher believes that the objectives of this study have been achieved and the research questions fully answered. However, there are limitations to the study that might affect the generalisability of its findings.

First, this study is subject to limitations related to the research methods employed, i.e. the questionnaire survey and interviews. At the outset, the researcher was sometimes restricted in gaining access to the Islamic banks. Some Islamic banks would not at first allow their staff to participate in the research. In an attempt to overcome this objection, the benefits of the research for Islamic banks were stressed, and the researcher openly and transparently offered the findings to the interviewees when the research was concluded. As well, and especially with regard to the personal interviews, not all population groups were considered. For instance, regulators in the central bank refused to participate due to their time constraints, and religious scholars were also difficult to contact and access to them could not be obtained.

Furthermore, a personal bias of individual survey respondents may also have been present. This could be reflected in the form of an unwillingness of respondents to provide proper and authentic information, or else they may have intentionally tried to
hide original facts or provide false statements. Some respondents may not have provided honest opinions, perhaps hoping to conceal their lack of relevant knowledge, or not wishing to provide answers that may discredit their Islamic bank, all of which potentially contribute to misleading research outcomes. This issue applies to all studies that use self-administered questionnaires for data collection. Though these represent limitations of the present study they may be starting points for future research design.

Another limitation of the survey method related to the possible misunderstanding and misinterpretation of the questions included in the questionnaire provided to the respondents, which could have subsequently led to inaccuracies in the collected data for the research. Semantic difficulty could arise using the questionnaire and interview methods, forming a gap in the understanding of the researcher and interpretation by respondents, introducing artificial distortions in the results. In the interviews, a partial solution to this potential problem was to allow interviewees ample time to concentrate and recall all events and influences of relevance. The researcher also tried to ask the same question more than once and in different ways to check on the consistency and probable accuracy of responses provided.

Moreover, the relatively small sample of survey respondents and interviewees may have caused some unintended distortions in the outcomes. This might affect the generalizability of this study’s results, perhaps also exacerbated by the structure of the sample, being based on the views of professionals and managers alone and presuming the level of their knowledge of IFRS. However, other possible users may hold different views. This is, of course, a limitation of interpretative research.

Finally, conducting a research study in the field of Islamic accounting standards is challenging in itself, because much of the extant literature relates to Islamic institutions in the area of general finance rather than in the accounting area. A significant difficulty confronted by the researcher, related to the lack of sources about Islamic accounting standards developed in the context of AAOIFI.

### 7.5 Research contribution

The main focus of this study related to the reasons for development of AAOIFI standards, the feasibility of its implementation, and the differences between IFRS and
AAOIFI standards. The study’s findings will be useful to the management and shareholders of Islamic banks for gaining insights into the effects, benefits and drawbacks of the Islamic accounting standards issued by the AAOIFI.

The purpose of this study was to better understand the framework of AAOIFI accounting standards and the requirement that AAOIFI accounting standards be globally adopted by Islamic banks. The study’s findings will help to comprehend the impact of the adoption of IFRS in Islamic banks together with an assessment of the extent to which AAOIFI standards needed to be adopted by Islamic banks to meet the requirements of Shariah principles.

This study makes a contribution to the literature of AAOIFI standards’ adoption in Islamic banks. The study also focuses on the manner in which key actors in the accounting profession attempted to defend conflicting interests regarding the selection of standards of accounting, by lobbying based on a comparison of costs and related benefits. This study suggests that concerned Islamic banks should refer to the financial standards reports disseminated in developing nations. This would help in gathering the elements of evidence that may influence consideration of the suitability of the AAOIFI standards and serve to educate regulators interested in enhancing the accounting standards in several Muslim nations concerned with the adoption of AAOIFI standards. The study recommends that regulators of Islamic banks need to consider the appropriate accounting system for meeting their obligations to local investors.

This study implies that there are issues in applying Shariah when there is an application of IFRS by users in order to record the financial transactions of Islamic banks. This suggests an urgent need by the standard setters and regulators in Islamic countries to address the different and unique technical aspects of the financial transactions of Islamic banks. In general, this would be a major contribution to ensure the compliance of Islamic banks’ transactions with Shariah principles, and at the same time, an attempt may be made to minimize the practices that are highly divergent. This may of course hinder the present harmonization efforts being made by IASB and the Islamic banks. Furthermore, there is a significant need for collaboration amongst the regulators, standard setters and academics world-wide to address
technical guidance to report the financial transactions of Islamic banks under IFRS along with compliance with Shariah principles.

7.6 Suggestions for further research

This is the first study of the suitability of AAOIFI standards for Islamic banks in the UAE. The questionnaire survey sample included professionals and managers in the UAE Islamic banks at the time of data collection. Further research may extend to include conventional banks, which may provide other findings.

This study was carried out prior to the potential adoption of AAOIFI accounting standards by Islamic banks in the UAE. As a result, future studies may extend to Islamic banks in other GCC countries, such as the Qatar Islamic Bank and Bahrain Islamic Bank, which have already used AAOIFI standards and these future studies may provide significant, comparable findings.

The findings of this research reports the responses regarding the potential impact of AAOIFI accounting standards upon the Islamic banks which was obtained from the feedback of professionals, managers and key players involved in Islamic banks and accounting standards. Future research may attempt to obtain feedback and responses from academics, consultants of Shariah, related auditors and regulators of central bank and the Ministry of Commerce.

It is also suggested for future research in the discipline of Islamic accounting research, that an attempt be made to investigate and find out how the academics perceive the adoption of Islamic accounting standards rather than simply providing contingent practical responses.
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Appendices

Appendix 1: Standards developed by AAOIFI

**Accounting standards:**

1. Objective of financial accounting for Islamic banks and financial institution (IFIs).
2. Concept of financial accounting for IFIs.
3. General presentation and disclosure in the financial statements of IFIs.
4. *Murabaha* and *Murabah* to the purchase order.
5. *Mudharaba* financing.
7. Disclosure of bases for profit allocation between owners’ equity and investment account holders.
8. Equity of investment account holders and their equivalent.
9. Salam and Parallel Salam.
10. *Ijarah* and *Ijarah Muntahia Bittamleek*.
11. *Zakat*.
12. *Istisnah* and Parallel *Istisnah*.
15. Disclosure of Bases for Determining and Allocating Surplus or Deficit in Islamic Insurance Companies.
16. Investment Funds.
17. Provisions and Reserves in Islamic Insurance Companies.
19. Investments.
20. Islamic Financial Services Offered by Conventional Financial Institutions.
21. Contributions in Islamic Insurance Companies.
22. Deferred Payment Sale


25. Consolidation.


**Auditing standards:**
1. Objective and principles of auditing.
3. Terms of Audit Engagement.
5. The Auditor’s Responsibility to Consider Fraud and Error in an Audit of Financial Statements.

**Governance standards:**
2. *Shariah* Review.
3. Internal *Shariah* Review.
4. Audit and Governance Committee for IFIs.
5. Independence of *Shariah*Supervisory Board.
6. Statement on Governance Principles for IFIs.
7. Corporate Social Responsibility.

**Ethics standards:**
1. Code of ethics for accountants and auditors of IFIs.
2. Code of ethics for employees of IFIs.

**Shariah standards:**
1. Trading in currencies.
2. Debit Card, Charge Card and Credit Card.
3. Default in Payment by a Debtor.
5. Guarantees.


8. Murabaha to the Purchase Order.

9. Ijarah and Ijarah Muntahia Bittamleek.

10. Salam and Parallel Salam.

11. Istisnah and Parallel Istisnah.

12. Musharaka and Modern Corporations.


14. Documentary Credit.

15. Jua’la.


17. Investment Sukuk.

18. Possession (Qabd).

19. Loan (Qard).

20. Commodities in Organised Markets.

21. Financial Papers (Shares and Bonds).

22. Concession Contracts.

23. Agency.


25. Combination of Contracts.

26. Islamic Insurance.

27. Indices.


29. Ethics and stipulations for Fatwa.

30. Monetization (Tawarruq)

31. Gharar Stipulations in Financial Transactions
32. Arbitration
33. Waqf
34. Ijarah on Labour (Individuals)
35. Zakat
36. Contingent obligations
37. Credit facilities
38. Online financial transactions
39. Rahn (pledge)
40. Investment account and profit distribution
41. Reinsurance
42. Disposal of rights
43. Bankruptcy
44. Liquidity management (http://www.aaoifi.com)
Appendix 2: Laws Governing Banks and Financial Institutions and their Operation in the UAE

The most relevant Laws, Decrees, Resolutions and Decisions in the field of Banking, Finance and related areas in the UAE are the following:

4. Federal Law No. 5 of the 1985 concerning Civil Transactions.
6. Central Bank Resolution No.123/7/92 regarding Regulation of Money Changing Business in the UAE.
Appendix 3: Questionnaire Survey

Section 1: About you

Please provide some background information about yourself. Answer the following questions by ticking the appropriate box □ or letter. Please mark only one box unless otherwise stated.

1. What is your age range?
   A. 29 and below
   B. 30 – 39
   C. 40 – 49
   D. 50 – 59
   E. 60 and above

2. What is your gender?
   □ Male
   □ Female

3. What is your highest level of education?
   A. PhD
   B. Master's Degree
   C. Bachelor's Degree
   D. Diploma
   E. Professional Qualification
   F. High School and Lower

4. Which professional accounting association are you a member of?
   * You may select more than one
   A. ACCA
   B. ICAEW
   C. CPAA
   D. ICAA
   E. None

5. How many years have you worked in financial institutions?
   * You may select more than one
   □ No. of years ………

6. What is your current job title in your Islamic bank? ………………
Section 2: Islamic Banking Among IFRS

7. How do you differentiate Islamic banking services?
   A. None
   B. Interest rate/profit
   C. Convenience
   D. Cost of banking

8. Why in your opinion have customers chosen Islamic Banks?
   A. Religion
   B. Culture
   C. Ethical
   D. Cheap products

9. Does your Islamic bank adopt (IFRS)?

10. Do you agree with the statement that IFRS is developed by the developed countries hence not practical for developing countries?

11. Can you consider the IFRS to have the characteristics of understandability, and comparability in your Islamic bank?

12. Please indicate to what extent you agree or disagree with the following statements. The standards provided by the IFRS...

<table>
<thead>
<tr>
<th></th>
<th>Strongly agree (1)</th>
<th>Somewhat agree (2)</th>
<th>Neutral (3)</th>
<th>Somewhat disagree (4)</th>
<th>Strongly disagree (5)</th>
</tr>
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<tbody>
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<td>12. A:</td>
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<td>12. B:</td>
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<td>12. C:</td>
<td></td>
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<td></td>
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<tr>
<td>12. D:</td>
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</tbody>
</table>
13. Please indicate the extent to which you agree with each statement about the factors that influenced the adoption of IFRS by your Islamic bank.

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly agree (1)</th>
<th>Somewhat agree (2)</th>
<th>Neutral (3)</th>
<th>Somewhat disagree (4)</th>
<th>Strongly disagree (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank growth greatly influenced the adoption of IFRS.</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
</tr>
<tr>
<td>The legal system greatly influenced the adoption of IFRS.</td>
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<td>□</td>
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<tr>
<td>The external environment (e.g. World Bank, IMF etc) greatly influenced the adoption of IFRS.</td>
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<td>□</td>
<td>□</td>
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<tr>
<td>The existence of capital market greatly influenced the adoption of IFRS.</td>
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<td>□</td>
</tr>
</tbody>
</table>

14. What would you say are the merits of adopting IFRS into your Islamic bank?

....................................................................................................................................

15. What in your opinion are the demerits of adopting IFRS into your Islamic bank?

....................................................................................................................................

16. Please rank your Islamic bank facilities for following items:

<table>
<thead>
<tr>
<th>Facilities</th>
<th>Highly satisfied (1)</th>
<th>Satisfied (2)</th>
<th>Neutral (3)</th>
<th>Dissatisfied (4)</th>
<th>Highly dissatisfied (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provision of interest-free loans</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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<tr>
<td>Provision of Islamic products and services</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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<tr>
<td>Run on Islamic law and principles</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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<tr>
<td>Strong global network</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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<tr>
<td>Sufficient time for transaction</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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<tr>
<td>Competitive Product Offerings</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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</tr>
<tr>
<td>Overdraft privileges on current account</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
</tr>
<tr>
<td>Lower service charge</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
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</tbody>
</table>
17. To what extent do you think that the financial reports of your Islamic bank include the following elements?

<table>
<thead>
<tr>
<th>Element</th>
<th>Fully included (1)</th>
<th>Somewhat included (2)</th>
<th>Neutral (3)</th>
<th>Somewhat Not included (4)</th>
<th>Not included (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>17. A: Full disclosure of any and all relevant information which facilitates the users’ economic and religious decision-making.</td>
<td></td>
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<tr>
<td>17. B: Financial instruments not related to interest.</td>
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<tr>
<td>17. C: Information that enables Muslims to determine the amount of Zakat</td>
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<tr>
<td>17. D: The disclosure of the paid interest, the reasons for this payment and the steps which should be taken to avoid such interest in the future.</td>
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</tbody>
</table>

18. Please indicate the extent to which you agree or disagree with the following statements. Islamic banks financial reporting should be different from commercial banks reporting because …

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly agree (1)</th>
<th>Somewhat agree (2)</th>
<th>Neutral (3)</th>
<th>Somewhat disagree (4)</th>
<th>Strongly disagree (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>18. A: readers of Islamic banks reports have different needs</td>
<td></td>
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<tr>
<td>18. B: Islamic banks exist to produce Islamic financial services</td>
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</tbody>
</table>

Section.3 : IFRS vs. AAOIFI Standards

19. IFRS allows the use of fair value measurement in investment property; however, under AAOIFI standards, investment property should be measured at historical cost. To what extent do you agree with the following statements?

*Please tick the box that most closely represents your answers.

A. The use of historical cost measurement in investment property provides useful accurate information for Zakat purposes.
B. The use of fair value measurement in investment property provides useful accurate information for Zakat purposes.

C. Either the use of historical cost measurement or the use of fair value measurement in investment property provides useful accurate information for Zakat purposes.

D. Neither the use of historical cost measurement nor the use of fair value measurement in investment property provides useful accurate information for Zakat purposes.

20. If you compare IFRS to the AAOIFI standards, which one would be more time consuming of implementation?
   A. IFRS.
   B. AAOIFI.
   C. Both would be time consuming.
   D. Both would not be time consuming.

21. If you compare the IFRS to AAOIFI standards, which one do you prefer to implement?
   A. IFRS.
   B. AAOIFI.
   C. Both are preferable.
   D. Both are not preferable.

22. What are the main reasons for your preferences? 
   Please state your reasons:

(I).................................................................................................................................

(II).................................................................................................................................

Section 4: The Potential Adoption of AAOIFI standards

23. Does your Islamic bank have a policy of convergence with or adopting Islamic accounting standards (AAOIFI Standards)?
   A. No, we do not have plans for convergence / adoption at this time.
   B. Yes, we have already converged with / adopted AAOIFI.
   C. Yes, we will be converging with / adopting AAOIFI.
   D. Don’t know.
24. Do you think that the first time adoption of AAOIFI standards for your Islamic bank will cost the bank both with the time and resources?

A. Just time.
B. Just resources.
C. Both time and resources.
D. Nor time or resources.

25. Do you think that the benefits of AAOIFI standards for your Islamic bank in later stages of implementation would outweigh the initial costs incurred?

Yes  No

☐  ☐

26. Would it be easy for the accounting department to complete the transition process of the shift towards the AAOIFI standards for your Islamic bank by themselves, or will they be hiring the services of auditors and analysts?

Yes  No

☐  ☐

27. For the application of AAOIFI standards for your Islamic bank do you think an accountant is required to have knowledge of Islamic ethical and legal Islamic aspects?

Yes  No

☐  ☐

28. Please rate the quality of each of the following aspects of the AAOIFI:

<table>
<thead>
<tr>
<th>Aspect</th>
<th>Excellent (1)</th>
<th>Good (2)</th>
<th>Neutral (3)</th>
<th>Fair (4)</th>
<th>Poor (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>28. A: The credibility of the AAOIFI’s standards</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
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<tr>
<td>28. B: The overall quality of the AAOIFI’s standards</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
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<tr>
<td>28. C: The AAOIFI’s outreach to its constituents</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>28. D: The AAOIFI organization in general</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
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</tbody>
</table>
29. To what extent do you agree that the adoption of Islamic accounting standards (AAOIFI) in the UAE would improve the quality of financial reporting:

<table>
<thead>
<tr>
<th></th>
<th>Strongly agree (1)</th>
<th>Somewhat agree (2)</th>
<th>Neutral (3)</th>
<th>Somewhat disagree (4)</th>
<th>Strongly disagree (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>29. A: Relevance</td>
<td></td>
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<tr>
<td>29. B: Reliability</td>
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<td>29. C: Comparability</td>
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<td>29. D: Understandability</td>
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</table>

30. To what extent do you think that each of the following factors influence the potential adoption of Islamic accounting standards (AAOIFI) in the UAE:

<table>
<thead>
<tr>
<th></th>
<th>High Impact (1)</th>
<th>Somewhat High Impact (2)</th>
<th>Neutral (3)</th>
<th>Somewhat Low Impact (4)</th>
<th>Low Impact (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>30.A: International auditing firms</td>
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<tr>
<td>30.B: International lending organizations (i.e. the World Bank)</td>
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<td>30.C: Multinational companies</td>
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<td>30.D: Foreign investment</td>
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<tr>
<td>30.E: Global capital market</td>
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<td>30.F: The UAE Stock Exchange</td>
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<td>30.G: Academics in accounting fields</td>
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<td>30.H: The government (e.g. the Ministry of Commerce and central bank)</td>
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<td>30.I: Local users’ needs</td>
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<td>30.J: Islamic principles</td>
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31. Please rate the areas that are likely to be impacted upon with AAOIFI adoption in your entity. Rank them from 1 to 5. ‘1’ represents High Impact and ‘5’ represents Low Impact.

<table>
<thead>
<tr>
<th></th>
<th>High Impact (1)</th>
<th>Somewhat High Impact (2)</th>
<th>Neutral (3)</th>
<th>Somewhat Low Impact (4)</th>
<th>Low Impact (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>31. A: Debt raising</td>
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<td>31. B: Capital management</td>
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<td>31. C: Earnings volatility</td>
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<td>31. D: Investment operations</td>
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<td>31. E: Securitization activities</td>
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<tr>
<td>31. F: Prudential capital adequacy</td>
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</table>
31. G: Credit rating

31. H: Investor relations

31. I: Dividend policy

32. What are the most significant impediments to the adoption of AAOIFI standards by Islamic banks?

33. What suggestions do you have to help the AAOIFI meet its goals of both timeliness in completing projects on its agenda and a high-quality due process in developing the standards?

Thank You for Your Time and Participation. Your cooperation and contribution to this study is greatly appreciated. Information provided will be held in strictest confidence if you would like to receive a summary report of the findings of the study, please provide an email address for contact purposes.

E-mail address: _________________________________
Appendix 4: Histogram and box plot figures related to measures of skewness and kurtosis in Chapter 6 (distribution of results)

Histograms and Box Plots of Survey Responses to Questions 12A to 12D:
Histograms and Box Plots of Survey Responses to Questions 13A to 13D:
Histograms and Box Plots of Survey Responses to Questions 16A to 16D
Histograms and Box Plots of Survey Responses to Questions 16E to 16H:

Q 16E

Histogram

Box Plot

Q 16F

Histogram

Box Plot

Q 16G

Histogram

Box Plot
Histograms and Box Plots of Survey Responses to Questions 17A to 17D:

Q 17A

Q 17B
Histograms and Box Plots of Survey Responses to Question 18A:
Figure 6.19: Histogram and Box Plot of Survey Responses to Question 18B:

Histograms and Box Plots of Survey Responses to Questions 28A to 28D:
Histograms and Box Plots of Responses to Questions 29A to 29D:
Histograms and Box Plots of Responses to Questions 30A to 30D:

**Q 30A**

**Histogram**

**Box Plot**

**Q 30B**

**Histogram**

**Box Plot**

**Q 30C**

**Histogram**

**Box Plot**
Histograms and Box Plots of Responses to Questions 30E to 30H:

Q 30E

Histogram

Box Plot

Q 30F

Histogram

Box Plot
Histograms and Box Plots of Responses to Questions 30I to 30J:
Histograms and Box Plots of Responses to Questions 31A to 31D:

Q 31A

Q 31B
Histograms and Box Plots of Responses to Questions 31E to 31H
Histogram and Box Plot of Responses to Question 31I: