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PRIMARY RESEARCH

Accounting for *Ijārah*–Reviewing the Need for Exclusive Accounting Standards

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Abstract.

Purpose: This paper compares the presentation of *ijārah* Muntahia Bittamleek (IMBT), as outlined by conventional and Islamic accounting standards, to re-examine the need for exclusive accounting standards for presenting *ijārah* instrument by IFIs operating in Pakistan.
Methodology: IMBT instrument is presented using both Islamic and conventional accounting standards, and experts' opinions are gathered (accountants, academics, and Islamic bankers) on quality of reported financial information. Finally, the statistical significance of the difference in the quality score is tested.
Findings: Results show that IFRS pose a significant advantage regarding presentation of IMBT, which reduces the need for exclusive accounting standards for presenting ijārah instrument in Pakistan.
Significance: Earlier studies by Morshed (2022); El-Halaby et al. (2020); Ullah (2020) do not apply Islamic and conventional financial reporting standards to Islamic financial instruments when making comparisons. Additionally, most studies do not consider recent updates in conventional standards due to the standardization efforts by IASB and FASB. This paper addresses both these gaps emerging from the literature.
Practical Implication: The study exhibits valuable policy implications for regulators regarding adopting conventional accounting and reporting standards for IFIs. Regulatory intervention may favor improving the IFRS framework's applicability on IMBT by collaborating with other international standard-setting bodies. Finally, the regulatory bodies should create an instrument-wise handbook to guide IFIs in applying IFRSs for Sharīáh-compliant presentation.

KAUJIE Classification: K5, L11, L24, L33
JEL Classification: E48, G21, M41, M48

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INTRODUCTION

Islamic finance is one of the rapidly growing fields in the modern economy. The financial products that the Islamic financial institutions (IFIs) deal with are developed explicitly in compliance with the Sharīáh[1] principles, aimed at achieving *maqāṣid al*-Sharīáh identified by Al-Ghazali (translated by Hammad (2018)). These products are structured differently, excluding *ribā* (interest) and other Sharīáh prohibitions (Usmani, 2010). To cater to these products' unique reporting needs, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) has created an integrated framework of Sharīáh, accounting, and governance standards for IFIs. This integrated framework of standards is aimed at governance, control, and reporting of the IFIs. Financial reporting is an integral part of this framework, as it defines the process of reporting financial data (Warren et al., 2012). However, global standard-setting bodies, like the International Accounting Standards Board (IASB), have also created financial reporting standards to accommodate the overall need for comparability. These IASB-issued standards are called International Financial Reporting Standards (IFRSs), which are based on IFRS Framework (referred to as the 'conventional' framework) (IFRS, 2022).

As Islamic products are required to comply with the principles of Sharīáh, they possess (i) process flows, (ii) sequences, and (ii) resulting rights and obligations for contracting parties that are distinctive from those of their conventional counterparts. Considering that the purpose of financial reporting is to ensure that true and fair information is shared with the stakeholders, the economic substance of the transactions must be appropriately depicted in the reporting of IFIs. Due to the significant differences between Islamic and conventional financing instruments, the conventional standards might not properly present Islamic instruments' substance. If this is the case, a separate set of accounting standards is necessary for Islamic instruments. Therefore, AAOIFI has devised an accounting framework (referred to as the 'Islamic' framework) and has issued Financial Accounting Standards (FASs) (AAOIFI, 2022) for reporting Islamic financing instruments.

Therefore, there are two competing views in the literature on reporting of IFIs. These are: (i) preparing exclusive accounting standards for IFIs, and (ii) harmonizing the financial reporting of IFIs with their conventional counterparts. For example, ijārah Muntahia Bittamleek (IMBT) is a prevalent Islamic mode which is one of the most used long-term financing instruments by the IFIs. The overall structure of IMBT is very similar to lease financing used by conventional institutions (Hilmy et al., 2021). However, there are some significant differences in the legal form of these two instruments. For example, the IFI takes ownership of the ijārah asset before leasing it to the customer (AAOIFI, 2020). The structure of a simple IMBT instrument is shown below.

[1]Islamic jurisprudence is derived from Qur'ān and Sunnah.

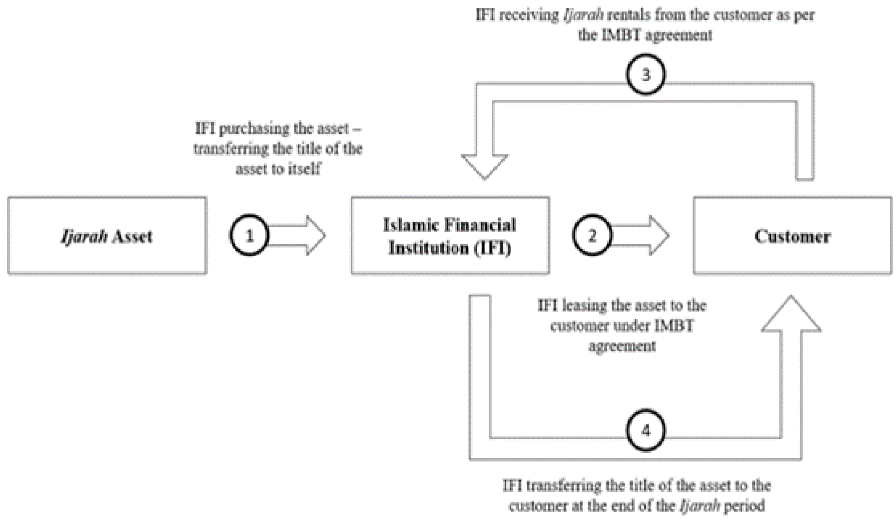

FIGURE 1. Structure of IMBT

The financial reporting of IMBT is substantially different under conventional and Islamic frameworks (Hilmy et al., 2021; Khalid, 2021). Therefore, there is a need to critically assess the quality of the financial information presented under these two frameworks. Earlier studies conducted by El-Halaby et al. (2020); Morshed (2022); Ullah (2020) (advocating the case of exclusive accounting standards for IFIs) do not apply the conventional and Islamic accounting standards to the same instrument when making comparisons. Additionally, most studies do not consider the updates made in the conventional financial reporting standards due to standardization efforts by global standard-setting bodies like IASB and Financial Accounting Standards Board (FASB).

Therefore, this paper aims to address these identified gaps and re-examine the possibility of harmonization in the two accounting frameworks by evaluating the accounting treatment of *ijārah Muntahia Bittamleek* (IMBT) as practised in Pakistan. More specifically, the research objective of this study is to compare the quality of the presentation of Islamic and conventional accounting standards used to present IMBT. Thus, this paper demonstrates the presentation of IMBT using both Islamic and conventional reporting standards and gathers the opinion of experts on these extracts. To achieve this objective, the paper attempts to answer the research question of whether, for IMBT, the quality of financial information presented per conventional standards is superior to the quality of financial information presented per Islamic standards.

The next section of the study provides a thorough review of the existing literature. Section 3 explains the methodology devised to answer the research question and test the hypothesis. Section 4 provides a critical analysis of accounting treatments and reporting of IMBT under both frameworks and interprets the experts' opinions on the quality of reporting. The final section provides the conclusion and explains the implications of the findings.

REVIEW OF LITERATURE

Financial accounting helps present relevant and reliable financial information to help stakeholders make informed decisions (Weil et al., 2013). As such, financial accounting is closely associated with the phrases like information asymmetry and draws its essence from agency theory (Jensen & Meckling, 1976). This theory aims to remove the information asymmetry between the entity's management and relevant stakeholders. Therefore, when dealing with the financial information the management presents, the quality of this information must be considered. To ensure presentation of quality financial information, IASB issued the 'Conceptual Framework for Financial Reporting' (IFRS Framework) (IASB, 2010). This framework defines the qualitative characteristics that help present useful information for the users. One of those qualitative characteristics is 'comparability', which is defined by IASB as the characteristic *"that enables users to identify and understand similarities in, and differences among, items"* (IASB, 2010). It is closely associated with 'consistency' which means: (i) an entity applies the same principles over time, and (ii) the same principles are applied by different entities reporting in the same environment (Zafari et al., 2019). Therefore, it is vital that the information presented is globally comparable and consistent.

Islamic financial products are substantially different from the financial products that conventional financial institutions deal with (Ayub, 2021; Al-Salem et al., 2009). It is essential that the financial reports are both comparable and faithfully presented (Maurer, 2010). Many scholars have raised doubts about the ability of conventional accounting standards to correctly depict Islamic financial instruments' economic substance (El-Halaby et al., 2020; Mohammed et al., 2019; Khan et al., 2018; Kadri & Ibrahim, 2018; Sarea, 2013). Therefore, AAOIFI has issued separate accounting standards for IFIs (AAOIFI, 2020) to ensure that the economic substance of Islamic products is correctly depicted in the reporting of IFIs. Scholars like El-Halaby et al. (2020); Khan et al. (2018); Kadri & Ibrahim (2018) have linked the adoption of AAOIFI standards with the efficiency and performance of IFIs. While others, like Ibrahim & Ling (2016), have directly compared the quality of IASB and AAOIFI accounting standards, concluding that IASB's standards are too shallow to present Islamic financial products accurately. The work of Mohammed et al. (2019) contradicts this finding, stating that the conventiaonal standards can be used to present Islamic financial instruments. However, the study concludes that issuing new accounting standards (confirming that Islamic products are different from conventional products) is essential for public acceptance. Similarly, the study by Ahmed et al. (2021) also emphasized the importance of public perception of IFIs.

However, the importance of comparability and consistency cannot be overlooked. Accounting standards need to depict the substance of the transactions, but this must be done consistently and comparably (Wüstemann & Wüstemann, 2010). Suandi (2013) and ACCA-KPMG (2010) have highlighted the need for comparability in IFIs by concluding that currently, IFIs are following different reporting standards, causing difficulty in comparison. Similarly, Voronova & Umarov (2021) also highlighted the focus on globalization and convergence of financial reporting of IFIs. Additionally, AAOIFI's 'Conceptual Framework for Financial Reporting' (AAOIFI, 2020) is very similar to the IASB's IFRS Framework in terms of the qualitative characteristics of the accounting information (AAOIFI, 2020; IASB, 2010). Based on these similarities, scholars like Naim (2010) and Shafii et al. (2013) have argued that harmonizing the accounting practices of IFIs is a more cost-effective option for the financial reporting of IFIs.

One popular long-term financing mode used by IFI is *ijārah* (Yasser & Kalim, 2021), which comprised over 39%[2] of the total financing provided by IFIs in Pakistan for the quarter ended June 2022 (SBP, 2022). Due to its operational similarities with operating lease, scholars have compared different aspects of their accounting treatments (Morshed, 2022; Hilmy et al., 2021; Khalid, 2021; Ullah, 2020; Hanif, 2016; Atmeh & Serdaneh, 2012). AAOIFI issued FAS-32 in 2019 (AAOIFI, 2020), which supersedes its predecessor, FAS-8[3]. The accounting standard issued by IASB that is applied to lease transactions is IFRS-16[4] (IASB, 2016), which supersedes its predecessor IAS-17[5]. The changes done in AAOIFI-issued FAS-32[6] are consistent with IASB-issued IFRS -16, considering both new standards discourage off-balance sheet financing for lessees (Liviu-Alexandru, 2018). Morshed (2022) and Ullah (2020) performed a comparative analysis of FAS-32 and IFRS-16 and concluded that an exclusive set of accounting standards is unnecessary for IFIs. Conversely, numerous earlier studies examining the treatment of FAS-8 and IAS-17 have criticized the application of IAS-17 on leases. These studies claim that IAS-17 fails to capture the true legal form of the transaction (Atmeh & Serdaneh, 2012; Gupta, 2015; Shiyuti et al., 2012)[7]. Additionally, Hanif (2016) conducted a descriptive analysis, concluding that the accounting treatments under these two standards are significantly different due to the different contractual forms (loan vs rent). Considering the legal framework of Pakistan, the Security and Exchange Commission of Pakistan (SECP) has adopted[8] IFAS-2[9], adapted from FAS-8 (SECP, 2007). IFAS-2 has not yet been updated based on the changes done by AAOIFI in FAS-32. As such, the issue of off-balance sheet financing continues in the accounting treatment of IFAS-2 (ACCA, 2014).

Generally, the exclusive accounting standards for IFIs cause three main issues: (1) inconsistency in reporting of IFIs operating in different jurisdictions (Hussan & Sulaiman, 2016; Hijazi & Tayyebi, 2010), (2) low volume of content available for the accounting treatment of IFIs (PWC, 2010), and (3) causing an overall confusion in the reporting and interpretation of results of IFIs, as conventional institutions are following different standards (Andari, 2019). Table 1 lists the countries and reporting standards used for the presenting financial information of IFIs. Harmonizing the financial reporting of IFIs can help resolve these issues, as it

[2]These include products that are based either exclusively on *ijārah* or hybrid with other contracts (like in diminishing *mushārakah*)
[3]Full name: Financial Accounting Standard 8- *ijārah*
[4]Full name: International Financial Reporting Standard 16–Leases
[5]Full name: International Accounting Standard 17–Leases
[6]Full name: Financial Accounting Standard-32-*ijārah*
[7]This study focused on *al-ijārah thummalbai'*, which is similar to a hire-purchase (HP) agreement in conventional terms. The accounting treatment for HP and finance lease is the same (ACCA, 2022).
[8]This standard was issued by the Institute of Chartered Accountants of Pakistan (ICAP) and adopted by the SECP (SECP, 2007)
[9]Full name: Islamic Financial Accounting Standard 2– *al-ijārah*

would remove the inconsistency in the reporting of IFIs and their conventional counterparts. Additionally, an immense volume of literature is available on the conventional accounting framework, which was first introduced in 1989 (Deloitte, 2022).

TABLE 1
Countries and Reporting Standards

Number	Country	Financial Reporting Standards Used
1	Bahrain	AAOIFI (FASs)
2	Qatar	
3	Syria	
4	Sudan	
5	Saudi Arabia	IASB (IASs and IFRSs)
6	Malaysia	
7	UAE	
8	Kuwait	
9	Pakistan	Local GAAPs
10	Iran	
11	Bangladesh	
12	Egypt	

Source: Hijazi & Tayyebi (2010)

The quality of the presented information can be evaluated from the qualitative characteristics of the financial information (Siddiqui et al., 2022; Tsoncheva et al., 2014; Maines & Wahlen, 2006). AAOIFI and IASB define these in their respective accounting frameworks (AAOIFI, 2010; IASB, 2010). Tsoncheva et al. (2014) defined the determinants for four qualitative characteristics[10] to evaluate the quality of the presented financial information. Therefore, to answer the research question stated earlier, this study tests the following hypothesis:
H0 [null hypothesis] = quality score of the presentation for Islamic and conventional accounting standards for IMBT is NOT significantly different.
H1 [alternate hypothesis] = quality score of the presentation for Islamic and conventional accounting standards for IMBT is significantly different.

Overall, the literature mainly supports exclusive accounting standards for IFIs. However, it also makes a compelling case for the harmonization of the accounting practices of IFIs with conventional institutions. Literature links the preference for exclusivity to factors like the importance of public perception (Mohammed et al., 2019) and the unique nature of Islamic financial products (Ibrahim & Ling, 2016). However, these studies do not apply AAOIFI and IASB financial reporting standards on the same instrument when comparing. Additionally, these studies do not consider the modifications made to the conventional standards due to the standardization efforts of IASB and FASB (Agostini & Agostini, 2018). Therefore, this study examines the possibility of harmonizing financial reporting for IFIs by presenting the

[10](i) Relevance, (ii) Understandability, (iii) comparability, and (iv) faithful representation.

IMBT instrument as per IFRS-16 and IFAS-2 and comparing the quality of the presented information with experts' opinions.

METHODOLOGY

This study uses a consequential approach[11] to answer the research question of the study, considering that we are interested in the quality of the presented financial information (which is the final step (or 'consequence') of the overall accounting process). This approach is based on the underlying assumption that if the quality of the financial reporting is superior to the conventional accounting framework, then there is no need to develop exclusive accounting standards for reporting of IFIs. Therefore, this paper examines the difference in the reporting of IMBT due to IFRS-16 and IFAS-2. For this purpose, the paper divides the analysis into two subsections. The first subsection presents the IMBT instrument using test data (hypothetical example) according to IFRS-16 and IFAS-2 and comments on the resulting presentation. The second subsection compares the quality of the presented financial information based on experts' opinions.

The determinants used to evaluate the quality of the financial information were adapted from Tsoncheva et al. (2014). Experts' opinions were collected from (i) accountants (licensed accountants working in Pakistan), (ii) academics (reputable scholars in the field of Islamic banking and finance and accounting in Pakistan), and (iii) bankers (working in IFIs in Pakistan) on the extract of the financial information prepared. From the responses received, a scorecard was created **(the questions can be requested from the corresponding author)**. The responses were indexed by calculating the average of the responses received. Finally, a two-tailed 'paired two-sample for means t-test' was used to check the statistical significance of the difference in the quality score of the experts, with a 5% significance level. This test has been selected to test the significance of the difference between the responses because it is consistent with the data (that is, the responses being compared are from the same participants).

Sample Selection and Survey Instrument

Primary data was collected through a questionnaire using Tsoncheva et al. (2014) qualitative characteristics measures. 13 questions were used to collect the experts' opinions on the selected qualitative characteristics of the presented financial information for IMBT.

The needed expertise for the respondents requires a blend of (i) a thorough knowledge of the accounting standards (both conventional and Islamic) and (ii) a thorough understanding of the structure of Islamic financial instruments. The availability of this combination is quite rare. Therefore, due to the scarcity of experts in Pakistan, a convenience sampling technique was used for selecting the experts. A total of 50 experts were approached to collect the data, of whom 31 respondents recorded their responses. The survey results were then analyzed in light of the research objective of this paper.

[11] The consequential approach is based on the consequentialism theory, which builds on the notion that a phenomenon can be judged on its consequences or results (Lenglet et al., 2017).

RESULTS AND ANALYSIS

The analysis is divided into two subsections; (i) preparing financial extracts for IMBT following IFRS-16 and IFAS-2, and (ii) collecting and analyzing the survey results on these prepared extracts.

Presentation of IMBT

To examine the presentation of IMBT, a hypothetical example is used to present the IMBT as per IFRS-16 and IFAS-2. The IFIs act as the *mu'jir* (i.e. lessor) in the arrangement of IMBT. Therefore, the main focus of the study is restricted to the accounting treatment of lessors.

Application of IFAS-2

IFAS 2 covers the financial reporting of *ijārah* contracts (SECP, 2007). IMBT is an *ijārah* contract which ends with the transfer of ownership of the underlying asset to the lessee. The standard states that the underlying asset should appear in the lessor's balance sheet. The lessor should recognize the rentals on accrual basis, and the asset should be depreciated following IAS 16[12]. This is similar to the accounting treatment of operating leases in IAS-17. However, IFRS-16 has superseded this standard to discourage off-balance sheet financing arising due to the accounting treatment of operating leases for lessees.

There are two significant issues in the presentation of IMBT as per IFAS-2. The first issue is that the transfer of title for the leased asset after the lease period expires (Khalid, 2021) makes the substance of this arrangement similar to a finance lease (IASB, 2016). Therefore, it can be argued that IFAS-2 does not adequately cover the substance of the transaction (as no performance obligation appears for the lessor and no 'right of use asset' (ROU) appears for the lessee). Accurately depicting the economic substance of the transaction is quite essential (Ebrahim & Abdelfattah, 2021; Ehsan et al., 2021), as AAOIFI (2010) explicitly states in section 8/3/3 that transitions' should be accounted for in accordance with substance as well as legal form. Although AAOIFI's framework is silent in case there is an inconsistency between the two Hamour et al. (2019), however a famous Sharī'ah maxim supports the idea that 'economic substance over legal form', which is *"matters are determined according to intentions"* (Zakariyah, 2015).

Additionally, if the 'substance over legal form' concept is ignored in financial reporting, it would mean that consolidation is no longer relevant for IFIs [13]. The special purpose vehicles (SPVs) of IFIs will be regarded as separate legal entities, presenting independent accounts which are not consolidated with the parent, which will not be a true and fair representation of the financial results.

The second issue here is that IFRS-2 enables off-balance sheet financing for the lessee by not recognizing the future obligation of the lessee relating to the *ijārah* -rentals. Additionally, the lessee is entitled to future benefits from the right to use the asset. As the definition of

[12]Full name: International Accounting Standard 16 - Property Plant and Equipment

[13]Consolidation is done where an entity controls another entity. Legally both entities are separate; however, the economic substance of the arrangement is such that the parent entity has control over the subsidiary's operations, policies, and decisions. Thus, both companies can be seen as one single 'economic' entity (IASB, 2010).

asset under both the financial reporting frameworks (AAOIFI, 2010; IASB, 2010) is similar, ROU asset meets the definition of an asset and must be presented on the lessee's balance sheet (AAOIFI, 2020). As these items remain off-balance sheet, this impairs the quality of the financial reporting.

Application of IFRS-16

To apply IFRS-16, we first need to establish whether the IMBT gives rise to an operating or a finance lease (this distinction is important from the perspective of the lessor (IASB, 2010)). The general criteria are as follows:

TABLE 2
Criteria for Finance Lease

Criteria	Explanation	Our Example
Ownership	Whether the ownership transfers to the lessee after the lease term?	**Yes** – the title transfers by execution of Hiba.
Bargain purchase option	Does the lessee have the option to purchase the leased asset at a below-market price after the lease term?	**Yes** – the asset is being transferred as a gift.
Lease term	The lease term period is at least 75% of the asset's useful life.	**No** – *Ijārah* term is assumed to be two years. It can be argued that two years is a short period compared to the asset's overall useful life.
Present value	The present value of the minimum lease payments should be at least 90% of the asset's fair value at the contract's inception.	**Yes** – generally, the IFI will recover the asset's cost and include a markup on the transaction.

Source: Bragg (2017) and Author

The answer to three out of four of these questions is 'YES'. Therefore, this transaction will most likely be treated as a finance lease under IFRS-16. IFRS-16 has two approaches to account for a finance lease. These are (IASB/FASB, 2009): (1) de-recognition approach (where the leased asset is derecognized in the books of the lessor), and (2) performance obligation approach (where the lessor does not derecognize the leased asset).

The performance obligation approach is more relevant to IMBT, as the lessor retains some control over the leased asset (the risks and rewards of the leased assets are not entirely transferred to the lessee). Here, instead of de-recognition of the leased asset, the lessor needs to recognize the receivable revenue and the performance obligation arising from the contract (which is the right of the lessee to use the asset) (Karwowski, 2018). The leased asset appears in the lessor's financial statements until the title is transferred to the lessee.

The initial entries for IFAS-2 and IFRS-16 are the same. However, under IFRS-16, we will need to record the rent receivable in the statement of financial position (henceforth referred to as balance sheet) of the IFI and the performance obligation arising from this transaction. This treatment will bring the off-balance sheet performance obligation of the IFI on its balance sheet. The following table summarizes and compares the presentation of IMBT under the two accounting frameworks:

TABLE 3
Summary of the Presentation

Phase	IFAS 2	IFRS 16	Comparison
Phase I *Ijārah* -Asset purchased by IFI	Recorded and depreciated following IAS 16.	Recorded and depreciated following IAS 16 or IAS 40 (depending on the nature of the asset).	No significant difference, although the IFRS framework allows a more thorough recognition of the *ijārah* -Asset based on its nature and classification.
Phase II *Ijārah* -Asset leased to the customer under the IMBT agreement	The rentals should be recognized on an accrual basis, so no entry is needed at this phase.	IFI will follow the performance obligation approach and record its performance obligation. The present value of the *ijārah* rentals is recorded as '*ijārah* rent receivable'.	Significant difference in the presentation of the IMBT. IFRS-16 shows the present value of the future receivable amount and the corresponding performance obligation.
	Ijārah -Asset still appears on the books of IFI as an asset.	*Ijārah* -Asset still appears on the books of IFI as an asset.	No such figures appear under IFAS 2.
Phase III IFI receives the *ijārah* rentals from the customer over the *ijārah* period	The rentals are recognized on an accrual basis, so the IFI records rental income as they become due.	The IFI records the income on an accrual basis, adjusting the performance obligation created at the inception of the IMBT.	Over the lease term, the same revenue is recorded in the statement of comprehensive income under both standards. However, the balance sheets show a different picture.

Experts' Survey

The sample selected for the study consisted of accountants (42%), academics (19%), and bankers (39%). Out of total, 44% were licensed accountants, and 30% were Islamic finance experts. A total of 58% of experts had an experience of more than 10 years, out of which 23% had experience of more than 15 years. The results of the quality score are summarized in Table 4.

TABLE 4
IMBT Quality Score Summary

IMBT	Quality Score			
	Relevance (R)	Faithful Representation (F)	Comparability (C)	Total
IFRS 16	14.18	12.33	12.26	38.77
IFAS 2	14.08	9.27	10.61	33.96
Difference	0.1	3.06	1.65	4.81

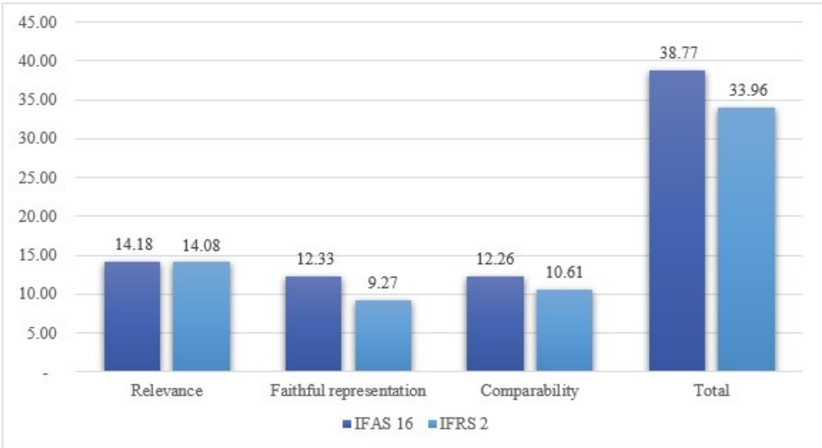

FIGURE 2. IMBT Quality Score Comparison

The graph shows that the IFRS presentation's total quality score is higher. The experts believe the presentation of IFRS-16 is better than IFAS-2 for the IMBT instrument. If the three characteristics are evaluated separately, it can be seen that the experts have given an approximately equal score to the relevance of the financial data presented. However, the financial information presented under the application of IFRS-16 is superior in terms of faithful representation and comparability. This is because IFRS-16 brings the performance obligation of the IFIs to the face of the balance sheet.

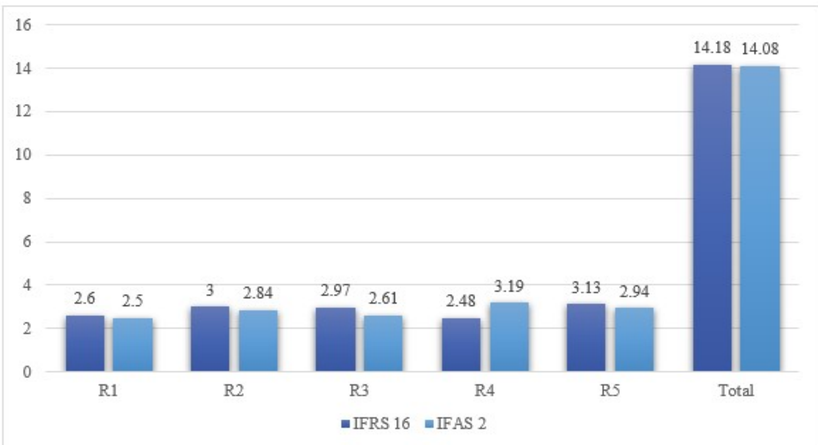

FIGURE 3. Relevance Comparison (IMBT)

Additionally, by following the IFRS-16, IFIs will follow the same accounting standards that conventional institutions follow, enabling a better comparison of the financial information by investors and other users. This contradicts the findings of Atmeh & Serdaneh (2012) and Gupta (2015), who argue against the compatibility of the IFRS framework for Islamic financial instruments.

Figure 3 considers the three qualitative characteristics individually. The difference in the overall quality scoring of relevance is very low. The quality score indicates that the scoring for IFAS-2 is only higher for R4 (which focused on Sharīáh compliance). As such, although IFRS-16 has a higher quality score, experts believe that IFAS-2 enables better Sharīáh compliance. However, the overall quality score corroborates the findings of Morshed (2022) and Ullah (2020), favoring the IFRS framework.

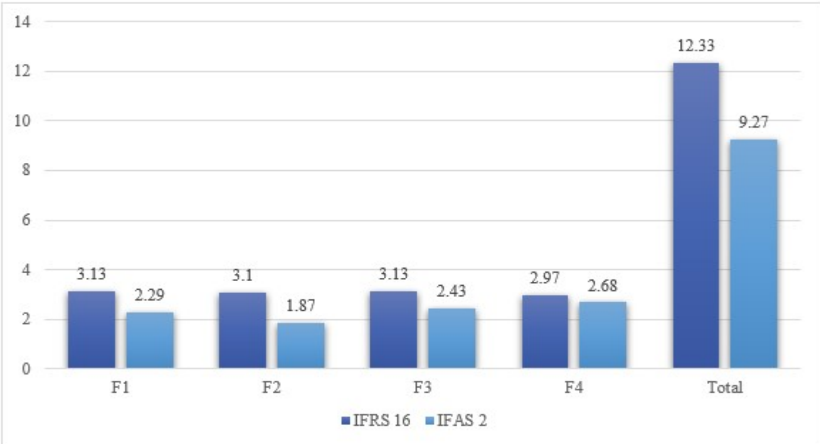

FIGURE 4. Faithful Representation Comparison (IMBT)

For faithful representation (Figure 4), all the questions show a superior scoring for IFRS-16. The highest difference is observed in F2, which focuses on treating off-balance sheet aspects (IFRS-16 accounts for the performance obligation and shows it on the balance sheet).

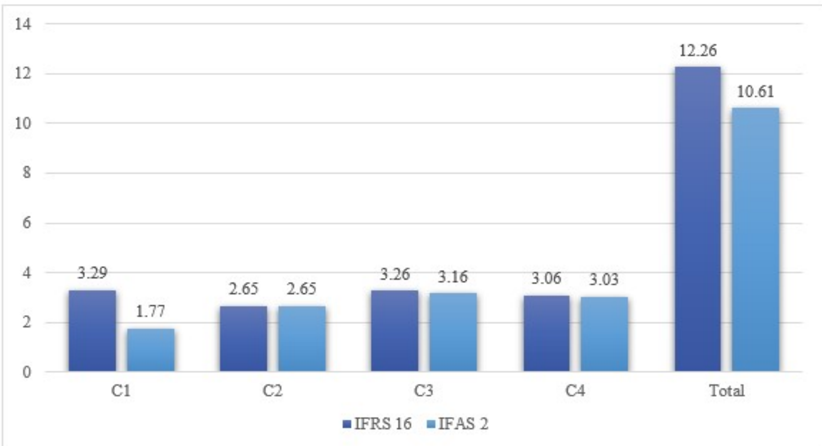

FIGURE 5. Comparability Comparison (IMBT)

The final characteristic (comparability) comparison shows a very slight difference in the score for IFRS-16 and IFAS-2 for all the questions asked, except for C1, which covers the aspect of consistency between reporting of the financial and non-financial sector at a global level. The score for IFRS-16 is much higher than IFAS-2 in this case.

Generally, after looking at the detailed scoring of the three characteristics, the overall score for IFRS-16 is higher than IFAS-2. The main reason for this can be attributed to faithful representation (targeting treatment of off-balance sheet transactions) and comparability (targeting global consistency). This contradicts the findings of Shiyuti et al. (2012). The quality score also shows that although IFRS-16 shows a higher quality score, IFRS-2 ensures higher Sharīáh compliance for IMBT (R4). This is consistent with the findings of El-Halaby et al. (2020) which confirms that public perception plays an essential role in the acceptability of the accounting framework.

From the scoring received from experts, it can be established that IFRSs are perceived to have superior quality in terms of relevance, faithful representation, and comparability. To further compare the quality score of the experts, Figures 6 and 7 show a breakup of the responses of the accountants, Islamic bankers, and academics.

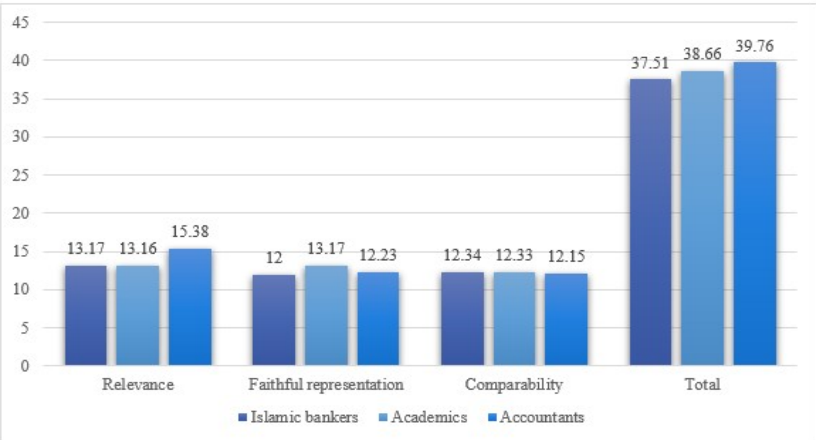

FIGURE 6. IFRS Profession Based Quality Score

Figure 6 shows that accountants rate the relevance of IFRS-16 higher than Islamic bankers or academics, where accountants give the highest index for the relevance of IFRS-16. Figure 6 also demonstrates that IFRS-16 has the lowest index score for Islamic bankers. The main reason for this is the reduced quality score of relevance and faithful representation for Islamic bankers. This means, in the opinion of Islamic bankers, the IFRSs do not present relevant information (as compared to its IFAS counterpart). This also shows that Islamic bankers show the lowest acceptance of the IFRS framework, which is consistent with the findings of Atmeh & Serdaneh (2012) and Shiyuti et al. (2012).

Figure 7 compares the quality score for IFAS-2, where academics show the lowest, and Islamic bankers show the highest quality score. The relevance receives the highest quality score, indicating that Islamic bankers believe that IFRS-2 enables more relevant presentation. In contrast, academics and accountants give a lower score to faithful representation under

IFAS-2 (as it ignores the economic substance of transactions). This finding corroborates the findings of Morshed (2022) and Ullah (2020).

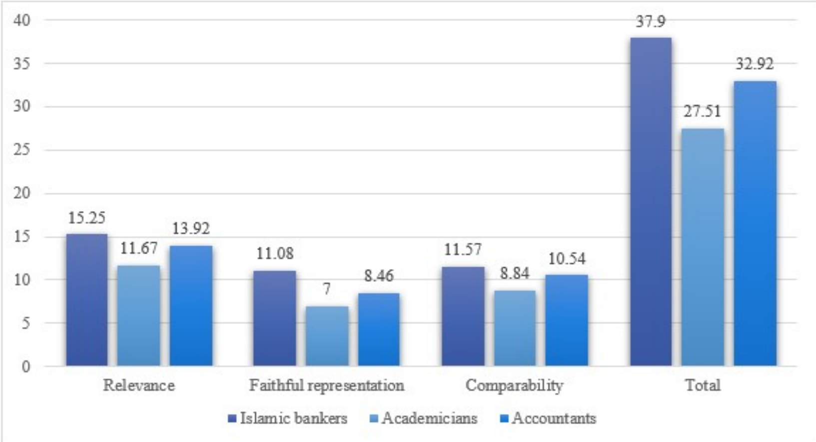

FIGURE 7. IFAS Profession Based Quality Score

To summarize the survey findings, IFRS-16 is considered superior to IFAS-2 for the presentation of IMBT. This is mainly because IFRS-16 discourages off-balance sheet factors and improves global comparability. This finding contradicts the conclusion of Ibrahim & Ling (2016) that the IFRS standards cannot capture the substance of Islamic financial instruments. The overall quality score of IFRS-16 is higher than IFAS-2 by 4.81 (Table 4). The difference in the quality score by experts is summarized in Table 5:

TABLE 5
Summary of Quality Score of Experts for IMBT

Expert Group	IFRS 16 Quality Score	IFAS 2 Quality Score	Difference (preference)
Islamic bankers	37.51	37.9	0.39 (IFAS higher)
Academicians	38.66	27.51	11.15 (IFRS higher)
Accountants	39.76	32.92	6.48 (IFRS higher)
Total (Figure 2)	38.77	33.96	4.81 (IFRS higher)

From the summary shown above, Islamic bankers show a preference for IFAS-2, whereas academics and accountants show a preference for IFRS-16. The preference for IFAS-2 by Islamic bankers can be due to the inclusion of finance income and cost arising in the statement of comprehensive income of the IFIs due to the discounting of the rental receivables and performance obligation, which is consistent with the findings of El-Halaby et al. (2020); Kadri & Ibrahim (2018) and Khan et al. (2018).

T-Test

The results of the t-test performed are shown in the table below:

TABLE 6
T-Test of Difference in the Quality Score

	IFRS 16	IFAS 2
Mean	38.677	33.806
Variance	25.092	42.294
Observations	31	31
Hypothesized Mean Difference	0	
Df	30	
Level of Significance	0.05	
t Stat	3.766	
P(T¡=t) two-tail	0.000***	
t Critical two-tail	2.042	

*** shows the significance at 1 percent

The result from the t-test shows a significant difference between the quality score given to the IMBT by the experts. One of the main reasons for this difference is that IFRS-16 covers the economic substance of the transaction. This result corroborates the conclusion of Mohammed et al. (2019) that IFRSs are feasible for reporting IFIs.

CONCLUSION, IMPLICATIONS AND RECOMMENDATIONS

The study highlights two significant limitations of the IFAS-2: (i) the lack of overall comparability and (ii) not correctly capturing the substance IMBT. The reason for reporting financial information through financial statements is to improve the governance of corporations by promoting transparency. By ignoring the economic substance of the transaction (and not properly capturing the off-balance sheet items), the quality of the reporting of IFAS-2 is seen as inferior to IFRS-16 by the experts, which contradicts the earlier work of Atmeh & Serdaneh (2012) and Ibrahim & Ling (2016). IFRS-16 fills these gaps by providing a better opportunity for global consistency and properly capturing the economic substance of the transactions. Due to these reasons, the experts rated IFRS-16 higher than the IFAS-2. However, there was a general disagreement between the accountants and the Islamic bankers. Islamic bankers believed the presentation resulting from IFAS-2 to be more relevant. In contrast, the accountants believed that IFRS-16 enables more faithful and comparable results, which is consistent with the findings of the study conducted by Hussan & Sulaiman (2016). The quality score received from the experts suggests that separate accounting standards for IFIs might not be necessary, as the conventional financial reporting framework produces higher quality reporting for the IFIs, for the IMBT instrument. Although these conclusions are consistent with the work of Morshed (2022); Mohammed et al. (2019) and Ullah (2020), however, these findings diverge from the earlier work of Atmeh & Serdaneh (2012); Ibrahim & Ling (2016); Khan et al. (2018). The main reason for the divergence is that these earlier studies do not consider the updates in conventional reporting framework.

The conclusions drawn from the analysis performed in this study have direct global and local implications for the overall governance and regulatory environment of IFIs. The findings of this study can be used by the local and global regulatory and standard-setting bodies in identifying practical avenues for harmonization. It is also recommended that the regulatory bodies of Pakistan should focus on harmonization and adapt the IFRS framework, as done in Malaysia (Hijazi & Tayyebi, 2010). At a global level, these bodies should liaison with other international standard-setting bodies like IASB and FASB and work on standardizing the accounting treatments, enabling consistent and comparable reporting for IFIs. Identified shortcomings of the IFRS framework should be discussed on international platforms, improving the applicability of the conventional reporting framework for IFIs. Additionally, a financing mode-wise accounting manual should be prepared for IFIs, helping them apply the IFRSs on Islamic instruments.

However, this study only focuses on the accounting standard adopted by SECP in Pakistan. Thus, the scope is limited to IFAS-2. As IFIs trade in numerous Sharīáh-compliant products, further research can be conducted on other products and instruments to fully examine the IFRS framework's limitations for IFIs. Additionally, the study uses a convenience sampling technique due to Pakistan's scarcity of relevant experts. A broader sample and focus on other reporting aspects (measurement, classification, and recognition) not covered in the study would improve the overall scope of comparison. Finally, this study also ignored the disclosure requirements in the comparison performed. Future research can focus on these identified limitations of the current study.

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