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**THE DETERMINANTS AND THE CONSEQUENCES OF ADOPTING
ACCOUNTING STANDARDS IN ISLAMIC BANKS: A CROSS
COUNTRY STUDY**

By
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A thesis submitted to the University of Plymouth
in partial fulfilment for the degree of

DOCTOR OF PHILOSOPHY

Plymouth Business School

December 2017

Dedication

To Allah,

Whom I ask for his satisfaction and acceptance for my efforts in creating this thesis and my effort of managing everything else while doing it.

Acknowledgments

My utmost praise goes to Allah, most gracious and most merciful, who showed me this road and helped me to walk along it the best I can.

I am particularly thankful to my Director of Studies, Prof. Khaled Hussainey, who encouraged me to learn and test new avenues of research. He trusted me, which gave me the trust I needed to try and explore the research world. Many thanks to Dr. Basel Awartani and Prof. Salima Paul for all the support and help they provided. A special thanks to both of you for making this journey possible for me.

I am also grateful to my parents, who were the first to call me ‘doctor’ since I was young. I hope I can make their dream come true. To my lovely daughters Malik, Maryam and Aisha – thank you for accompanying me during this journey. I hope you loved being with me during this journey as much as I loved having you with me.

A special place in my heart is booked for my precious angel, Malik, who helped me the most throughout my PhD journey. I will leave your reward to Allah, as I cannot reward you enough.

All my love to my special gift from Allah, Abdulmalik, who first inspired me to start my PhD journey along with his treatment for autism. Starting these two important journeys together made me feel like I am special to Allah, who apprised me of the two journeys together.

I would like to extend my thanks **to all of my family and everybody who waited patiently for my success, and for them to know that nothing is impossible.**

I would like to extend my profound thanks to Shinas College of Technology and Ministry of Manpower management, as well as Plymouth University management, for all their support and cooperation during the study period.

Author's declaration

At no time during the registration for the degree of Doctor of Philosophy has the author been registered for any other University award without prior agreement of the Doctoral College Quality Sub-Committee.

Work submitted for this research degree at the University of Plymouth has not formed part of any other degree either at the University of Plymouth or at another establishment.

This study was financed with the aid of a studentship from the Ministry of Manpower, Sultanate of Oman.

Presentations at conferences:

Local Conferences in UK

- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', Plymouth University postgraduate symposium, 2nd of July 2014.
- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', Oral presentation on postgraduate conference in Plymouth University, 4th of June, 2015.
- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', Plymouth Doctoral Colloquium UKPDC, Plymouth University, 16th - 17th June. **Winning the award of the Best Oral Presentation.**
- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', 15th Workshop on Accounting and Finance in Emerging Economies, University of Bristol, Friday, 24th June 2016.
- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', Portsmouth - Fordham Conference (24-25th September 2016), UK.

International Conferences

- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic Saudi Arabia, Mekkah, March 2016.

- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', Morocco, Casablanca, May 2016.
- Al Qamashoui, A. and Hussainey, K. (2016) 'The Determinants of Adopting Accounting Standards in Islamic Banks Cross Country Study Using Multinomial Logistic', Ireland, Dublin, June 2016.

Word count of main body of thesis: 70,215

AZIZA ABDALLAH HUMAID AL QAMASHOUI

THE DETERMINANTS AND THE CONSEQUENCES OF ADOPTING ACCOUNTING STANDARDS IN ISLAMIC BANKS: A CROSS COUNTRY STUDY

Abstract

This study investigates the determinants of adopting accounting standards (AAOIFI, IFRS or local standards) in thirty different countries with an Islamic banking industry. This study also examines the link between corporate governance disclosure, corporate social responsibility disclosure, and the adoption of accounting standards in the Islamic banking industry (IBI) as consequences for the adoption process. To the best of my knowledge, this is the only study that empirically investigates this topic. Environmental determinism theory is used as a framework to develop and test for explanations of the accounting standards used in countries where Islamic banks operate. Using multinomial logistic analysis to investigate the determinants of adopting any of the accounting standards sets (AAOIFI, IFRS, LOCAL), I find that both internal environmental factors, such as the level of education and the sophistication of the financial press, as well as enforcement factors, such as the existence of a centralised Sharia committee, are likely to have an impact on the accounting standards adopted by the Islamic banking industry.

In regard to the second objective of examining the link between corporate governance disclosure, corporate social responsibility disclosure, and the adoption of accounting standards in the Islamic banking industry (IBI), multivariate regression was used to analyse the data. The results present that: there is an association between corporate governance disclosure and social responsibility disclosure with the accounting standard adopted in the country. The analysis also presents that both types of disclosure within the IBI is associated with the other non-accounting institutions in the country as openness to economy, political stability, and enforcement mechanisms such as a centralised Sharia committee in the country.

This result implies that the specific accounting standards adopted by the Islamic banking industry are subject to the internal environment of, and the enforcement mechanisms imposed by, the country. This result further suggests that accounting institutions such as accounting standards adoption and non-accounting institutions are associated with disclosure practices in

IBI. Therefore, a conclusion can be drawn that adoption of accounting standards within the Islamic banking industry is an important accounting institution which can be determined by other institutions, as well as affecting disclosure practices in the industry.

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List of Abbreviations

<u>Abbreviation</u>	<u>Full term</u>
AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
AOSSG	Asian Oceanian Standard Setters Group
CG D	Corporate Governance Disclosure
CSR D	Corporate Social Responsibility Disclosure
EDT	Environmental Determinism Theory
GCC	Gulf Co-operation Council
IACPA	Iranian Association of Certified Public Accountants
IACPA	Iranian Association of Certified Public Accountants
IAO	Iran Audit Organization
IAS	International Accounting Standards
IBD	Islamic Development Bank
IBI	Islamic Banking Industry
IFIs	Islamic Financial Institutions
IFRSs	International Financial Reporting Standards
IFWG	Islamic Finance Working Group
MASB	Malaysian Accounting Standards Board
MIFC	Malaysian International Islamic Financial Centre
MNL	Multinomial logistic
TSE	Tehran Stock Exchange
Sharia	Islamic Law

CHAPTER ONE: INTRODUCTION

1.1 Overview

The importance of financial reporting is not something anyone can deny, particularly since the financial crisis and other global scandals. Financial specialists realise that weak financial reporting practices across the world weaken the economy further. Considering the history of global financial crises, many changes to financial reporting and enforcement regulations followed, for example Sarbanes-Oxley (Zhang, 2007). It is true that financial reporting is a core economic issue. Another factor highlighting the importance of financial reporting is the economic consequences associated with financial reporting practices, not only at the economy level, but also at firm value. This makes the decision of which financial reporting standards to adopt a core issue for the country's economy. It is important to realise that financial reporting leads to favourable economic consequences, as it not only considers the preparation of financial statements, but also the disclosure of all necessary information to all parties. Thus, it is critical that the accounting system adopted in the country is advanced and emphasises the concept of information production through disclosing both financial and non-financial information.

1.2 Research Background

The background of financial reporting in the IBI (Islamic banking industry) can be read from the practices of countries leading this industry, such as Malaysia, Iran, and the Gulf Cooperation Council (GCC) countries. These countries' practices can be used as a model by almost all other countries in regards to the adoption of accounting standards in IBI.

The Islamic finance industry was established in Malaysia, with the first Islamic bank opening in 1983. In addition to being one of the pioneering countries, the Malaysian government also had a mission to become a global centre for Islamic finance (GIFR, 2013). To this end, the Malaysian International Islamic Financial Centre (MIFC) was opened in 2006 to fulfil the many objectives defined by all the Islamic financial industry's stakeholders. In addition, and to meet the requirements following the increase in Islamic financial products, the Asian Oceanian Standard Setters Group (AOSSG) introduced a working group for Islamic financial

reporting. The main objective of the AOSSG is to promote the adoption of and convergence to IFRS and ensure consistency in the financial reporting practices of the Asian region (AOSSG, 2015). AOSSG has many working groups, and appointed the Malaysian Accounting Standards Board (MASB) as a leader for the Islamic Finance Working Group (IFWG). “The objective of the IFWG is to facilitate AOSSG members providing input and feedback to the IASB on the adequacy and appropriateness of proposed and existing International Financial Reporting Standards (IFRSs) to Islamic financial transactions and events” (AOSSG, 2015, p.7).

According to AOSSG (2016, p.1), some countries in the Asian region are converging to and permitting IFRS, such as India, Indonesia, Japan, Vietnam, Thailand, China, Brunei, Saudi Arabia and Uzbekistan. Thirteen countries have adopted IFRS fully, making the accounting standard a requirement. These countries are Australia, Cambodia, Iraq, Kazakhstan, Korea, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Singapore, and Sri Lanka, and additionally the financial centres in Dubai and Hong Kong. For the countries where IFRS is required for all entities, such as Kuwait and UAE, IFRS is also used to record all Islamic financial transactions. Most countries which are currently converging to IFRS either use local standards to report Islamic financial transactions, such as Indonesia, or they use IFRS, like Saudi Arabia.

Another leading example is Iran. The Iranian revolution in 1979 was the cornerstone in Iranian economics as well as cultural aspects and personal life. In the accounting field before the revolution, according to Mirshekary and Saudagaran (2005), Western practices dominated financial reporting practices in Iran. For example, the Big Eight international accounting firms were domiciled in Iran alongside the local Iranian firms. However, following the revolution, there was a vision toward nationalisation which led to the establishment of the Iran Audit Organization (IAO), which played a key role in the development of accounting standards in Iran (Mohammadrezaei et al., 2013). Before the IAO was established, Iranian companies predominantly used US GAAP, in addition to the UK, Australian, and Canadian standards (Mirshekary & Saudagaran, 2005; Roudaki, 2008). However, the IAO was pivotal in forming the National Accounting Standards (NAS) based on the International Accounting Standards (IAS), and not based on IFRS (Mohammadrezaei et al., 2013), and became compulsory in 2001 (Mashayekhi & Mashayekh, 2008). Also in 2001, the Iranian Association of Certified Public Accountants (IACPA) was established to provide guidance for the proper accounting practices in Iran (Mohammadrezaei et al., 2013). In 2004, the Code

of Corporate Governance of Iran was prepared; even though it was not mandated in the country, it has been adopted in the Tehran Stock Exchange (TSE) (Mashayekhi & Mashayekh, 2008). In Iran, some Islamic banks use IAS, such as Saman Bank and the Export Development Bank of Iran. While other banks may not specify the particular accounting standards they have adopted, they prepare their financial statements based on historical costs and use FV where appropriate (AOSSG, 2015).

On the other hand, Gulf Cooperation Council (GCC) member states – Oman, Bahrain, Kuwait, Qatar, Saudi Arabia and the United Arab Emirates – own the most developed Islamic financial system in the world and enjoy a very well developed Islamic interbank money market (Grassa & Gazdar, 2014a). GCC countries have 54 Islamic banks, in addition to the Islamic windows in conventional banks (Zawya, 2015). Most of the Islamic banks are branches from the well-established Islamic holding companies, such as Al Baraka Co., Abu Dhabi Islamic Bank, and Dubai Islamic Bank. The Accounting and Auditing Organisation for Islamic Institutions (AAOIFI) is a non-profit organisation based in Kingdom of Bahrain. Following the recommendation from the IDB workshop in 1987, it was developed in 1991 as an industry-led initiative (AAOIFI, 2010). The AAOIFI has developed 88 standards across multiple disciplines, which consist of: 48 in Sharia, 26 in accounting, five in auditing, seven in governance, and two in ethics (AAOIFI, 2015). The strategy used by the AAOIFI in developing those standards was to review the existing international standards, test them against Sharia principles, accept what is consistent with Sharia, and reject what is not (AOSSG, 2010, 2011, 2013; AAOIFI, 2010). Three of the six GCC countries utilise AAOIFI Financial Accounting Standards (FAS), while the other three use IFRS. In addition to the three GCC countries who lead the Islamic finance industry, Jordan, Lebanon, Sudan, and Mauritius have also adopted AAOIFI FAS in their domestic Islamic banking industry.

1.3 Motivations

Analysing the real-world pragmatics of accounting standards in IFIs generated the motivation to consider investigating the determinants of adopting one standard over another in IBI. Understanding the motivations for the adoption selection at the macro level can lead to a greater understanding at the micro level. Therefore, this research aims to investigate the determinants of adopting all of the accounting standards into the Islamic banking industry.

In addition to being able to bridge the gaps in the existing AAOIFI literature, the motivation of this research comes from the results of two main debates. Firstly, the debate within the industry between the accounting standards bodies, such as AAOIFI and Islamic Financial Standards Board (IFSB), with regards to the validity of the individual accounting standards to record Islamic financial transactions. Secondly, the debate within academia as to whether one accounting standard should be used across countries universally, or whether the use of two or more standards where each country adopts the most appropriate standard considering that individual country's environment is preferable. These two key debates will be discussed in turn.

There is debate between the accounting standards bodies, supported by Sharia scholars, as to whether conventional financial reporting practices such as IAS and IFRS are appropriate for reporting Islamic financial transactions. Hence, Sharia-compliant transactions should be recorded in different ways than the conventional comparative. The key difference in views of reporting Sharia-compliant transactions can be attributed to two main factors. One is the acceptability of reflecting the time value of money concept; the other is recognition, measurements, and reporting of the economic substance of transactions, but not the legal form (AOSSG, 2010).

In regards to the time value of money, the Malaysian Accounting Standard Board (MASB) has come to the conclusion that the IFRS does not conflict with Sharia, and issued a Statement of Principles, SOP i-1, which explains that financial reporting from an Islamic perspective does not conflict with the IFRS principles (MASB, 2009). Thus, SOP i-1 gives the green light for IFIs to use the IFRS to record Islamic financial transactions, under the condition that there is no conflict with Sharia. This step was approved by Bank Negara Malaysia (BNM) (GIFR, 2013). The Malaysian Accounting Standards Board states clearly that "Sharia-compliant transactions and events shall be accounted for in accordance with MASB approved accounting standards which are based in IFRS, unless there is a Sharia prohibition" (MASB, 2009 p.7). In the case of conflict between the IFRS and Sharia, then "management shall use its judgment". AAOIFI does not agree with the concept of time value of money, and considers it to be conflicting with Sharia principles. Considering that the IAS and IFRS are based on the time value of money concept, and given that their view of the time value of money concept does not comply with Sharia, the AAOIFI does not accept it in its FAS.

The recognition, measurements, and reporting of the economic substance of transactions articulates the substance over form concept. In Malaysia, it is viewed as a recording process of economic effect which will not affect the Sharia validity transaction, which was also approved by BNM (AOSSG, 2010). However, the AAOIFI emphasises that financial reporting should involve the substance of the economic activity as well as its legal form to be considered compliant with Sharia (AAOIFI, 2010). This debate stipulating which are the right standards to record Islamic financial transactions will continue until the AAOIFI or the IASB adjust their views on which standards are in compliance of Sharia principles. Additional points on the differences between AAOIFI FAS and IFRS is discussed in the research rational section.

The second debate, which discusses whether a universal accounting standard should be used across all countries or whether accounting standards should be adopted on a country by country basis, is dependent on the extent to which accounting is affected by its domestic and international environment (Cooke & Wallace, 1990; Rodrigues & Craig, 2007). If accounting is the product of its environment, as discussed by Ahmed et al. (2013) and Gernon and Wallace (1995), then it is implied that each country should apply the accounting standard which is deemed most appropriate. In contrast, if accounting is not affected by the environment, then it is universal. This would suggest that using one international accounting standard is recommended, since accounting is a universal product. As a result, this debate spurred motivation to empirically investigate the determinants of accounting standard adoption within the Islamic banking industry.

In addition, this research is not purely motivated by the subject's increasingly important role in a globalised and interconnected financial services industry, but also for the following reasons. Firstly, there is currently an absence of literature for AAOIFI adoption determinants, even though AAOIFI standards have been mandated in 10 countries and are used on a voluntary basis in many other countries (Baker, 2015). Additionally, they are used as a basis for local standards developed for the IBI (AAOIFI, 2015). Secondly, there is a significant paucity of research regarding the adoption of IFRS in developing countries, as well as economies in transition (Carmona & Trombetta, 2008). The factors which can influence adoption can differ significantly when comparing developed and developing economies, and therefore conclusions based on empirical research of developed economies may not be upheld for developing economies. For example, Mohammadrezaei et al. (2013) put forward that

institutional settings and capital markets are weak in developing countries, which implies that IFRS adoption cannot take place due to other forces.

1.4 Research Rational

Another motivation for the research is how different reporting practices are there in IBI. Different accounting practices can lead to different disclosure and as result different economic consequences see. Watts & Zimmerman, (1978); Zeff, (1978) Mueller, (1983); Pope and Mcleay (2011); Scott, (2012). From studying the different reporting practices for some of the common transaction in Islamic finance such as:

- Lessor accounting for ijarah with an arrangement to transfer ownership.
- Classification of customer investment accounts.
- Recognition and measurement of finance income.

It was clear how this can lead in different financial statements figures and this will be reflected in different consequences.

Lessor accounting for ijarah

There are different types of Ijarah according in IBI A) the lessor accounting practices for Ijarah that transferred ownership by or at end of the contract *ijarah muntahia bittamleek* or (IMB) as there are significant differences between IFRS & AAOIFI accounting practices. B) Another form of Ijarah is *al ijarah thumma al bai* ('ijarah followed by a sale' or AITAB). C) The ijarah arrangement in *musharakah mutanaqisah*.

There are different accounting practices between IFRS and AAOIFI for each type of *ijarah*. The accounting practices under IFRS and AAOIFI will be discussed separately as in (AOSSG, 2015).

- Under IAS 17 Leases: lease and lease end with transferred ownership as in *ijarah muntahia bittamleek* is consider finance lease.
- Another accounting practice for some forms of *ijarah muntahia bittamleek* can be reported under IAS 39: Financial Instruments: Measurements and Reconnections or IFRS 9, this can happen when the asset is recognised as substance of loan, then to

comply with Sharia substance has to be taken over form and therefore, asset recognised as loan.

- AAOIFI requirements for ijarah and ijarah muntahia bittamleek according to AAOIFI FAS No.8, require that the asset is recognised as lease investment the whole leasing period. Which should be amortised according to the institution depreciation policy. At the end of the leasing period the asset is derecognised after the final transfer.

Classification of customer investment accounts.

The customer in the Islamic bank can place their funds for investment based in musharakah (profit and loss sharing) or, mudarabah (profit-sharing), or wakalah (agency) (Ayub, 2007) IFI mainly use these funds for its banking activities or to invest in other assets. “An IFI generally does not guarantee the principal, and any loss would be borne by the investment accountholder unless there is negligence on the part of the IFI. This feature distinguishes an investment account from a deposit.” (AOSSG, 2015)

There are two types of investments accounts in the IFIs. First, an unrestricted investment account (URIA), where the IFI has the authority to determine how the fund is invested. Second, a restricted investment account (RIA), where the customer has some conditions for how the IFI may invest the fund.

There are three possible classifications for an investment account:

1. As a financial liability

Under IFRS, if there is a contractual obligation to deliver cash or another financial asset to the investment account holder. Then, an entity would recognise a financial liability for URIA or RIA.

AAOIFI does not recognise either URIA or RIA as financial liabilities.

2. As an intermediary element between liability and equity

Paragraph 16 of AAOIFI FAS No. 6, Equity of Investment Account Holders and Their Equivalents, requires URIA to be “presented as an independent category in the statement of

financial position of the Islamic bank between liabilities and owners' equity" (AAOIFI, 2010, paragraph 6.3, page 16)

3. As an off-balance sheet item

Previously AAOIFI's conceptual framework imposed prohibition on recognising RIA in the statement of financial position:

AAOIFI (2003) Statement of Financial Accounting No. 2, illustrate that "restricted investments are not assets of the Islamic bank and should not be reflected on the bank's statement of financial position since the bank does not have the right to use or dispose of those investments except with the conditions of the contract between the Islamic bank and holders of restricted investment accounts and their equivalent". (AAOIFI, 2003, paragraph 51, page 36)

Under both AAOIFI and IFRS, an investment account would not be recognised on the financial statements if it does not give rise to an element of the financial statements (AOSSG, 2015).

Recognition and measurement of finance income

Looking at the recognition and measurement of finance income which arising from ijara, murabahah and deferred payment sale. Because, they are the most used contracts for Islamic bank financing, and the relevant requirements under IFRS and AAOIFI FAS are different. Below an illustration how the requirements are differ under AAOIFI FAS and IFRS.

IFRS requirements for recognition and measurement of finance income

- IFRS 9 requires finance income (interest) to be recognised using an effective profit (interest) method which is "The method that is used in the calculation of the amortised cost of a financial asset or a financial liability and in the allocation and recognition of the interest revenue or interest expense in profit or loss over the relevant period" (AOSSG, 2015, p: 11).

AAOIFI FAS requirements for recognition and measurement of finance income

AAOIFI recognise and measure finance income, depending on the Islamic finance tool used, i.e. murabahah, mudarabah, musharakah, salam, ijarah, istisna' and deferred payment sale.

Proportionate allocation is the general method used in AAOIFI, which many interpret to mean straight-line allocation as explained by (AOSSG, 2015).

- Ijarah – AAOIFI FAS No. 8, paragraph 9 states: Ijarah revenue shall be allocated proportionately to the financial periods in the lease term.

- Murabahah – AAOIFI FAS No. 2, paragraph 8 states:

For cash or on credit not exceeding the current financial period sale, profits of Murabaha or Murabaha to the purchase orders are recognized at the time of contracting.

- Deferred payment sale – AAOIFI FAS No. 20, paragraphs 9 and 10 state:

Revenue from deferred payment sale transactions shall be recognised at the point of contracting. While Profit from deferred payment sale shall be recognised on an accrual basis and proportionally allocated over the period of the contract, whereby each financial period shall carry its portion of the profits.

In the literature the arguments for using which set of accounting in IBI is old, some argue that IFIs in general should follow an accounting standards which are based on Sharia. Some literature recommends AAOIFI FAS hence they are based in Sharia standards issued by AAOIFI also. This same literature argues to exclude IFRS due to problems in comparability, reliability and compliance (karim, 2001; White, 2004; Sarea and Hanefah, 2013). While many other researchers and practitioner supporting the use of IFRS for IFIs. It is very critical not to assume that the any of the financial reporting standards are not according to the Sharia. According to Mukhlisin, (2016) Sharia itself is defined very broadly which actually did not help in the standards setters to prepare the ideal set of the financial reporting standards. Therefore in this research we take all the financial accounting standards comply with Sharia even though there are differences in the way they are reporting IFIs transactions.

1.5 Objectives

The first objective of this thesis is to enhance the understanding of the determinants for adopting Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), International Financial Reporting Standards (IFRS), and local standards in the Islamic banking industry. AAOIFI is a non-profit organisation based in Kingdom of Bahrain. This industry-led organisation was established in 1991 based on recommendations from an Islamic Development Bank (IBD) workshop in 1987 (AAOIFI, 2010). The main purpose of establishing the AAOIFI was to provide full guidance on how to conduct business in the financial services industry so that compliance with Sharia (Islamic law) could be ensured (AAOIFI, 2015). Sharia covers the Islamic principles not only in a financial sense, but also in all aspects of a Muslim's life. The AAOIFI has developed 88 standards covering multiple different areas: 48 in Sharia, 26 in accounting, five in auditing, seven in governance, and two in ethics (AAOIFI, 2015). The strategy used by the AAOIFI in developing these standards (excluding the 48 Sharia standards) were to: review the existing international standards; test them against the Sharia principles; and then to accept the components that are consistent with Sharia and reject those which are not (AOSSG, 2010, 2011; AAOIFI, 2010). All standards issued by the AAOIFI should not contradict each other in order to ensure that financial services industry products are fully compliant with Sharia.

The second objective is to examine whether the adoption of certain accounting standards (AAOIFI/IFRS/local) in IBI can affect both the corporate governance disclosure and the social responsibility disclosure in the country. For the international field, the main aim of the information production is to protect the investors and other stakeholders in the business cycle. However, considering the characteristics of the Islamic financial sector, the main aim in producing this information is to fulfil the obligation of being a Sharia compliant business. Sharia compliance is the primary objective, so that stakeholders and investors can fully trust the business and its principles and are less likely to abandon it. Further, the point of Islamic accounting (Islamic reporting practices) is that it is inextricably linked to the Islamic religion, and thus cannot be separated from Islamic Law (Sharia). Therefore, Islamic financial transactions must have the characteristics of being Sharia compliant, otherwise the transactions are invalid. In Addition as discussed by (Asutay, 2016) the main objective of Islamic finance is to be ethical business more than being financial business only. Therefore, it is expected that Islamic reporting practices are promoting this objective as well.

1.6 Importance

The importance of this study can be seen from several stakeholder perspectives. Firstly, investigating the determinants of accounting standards adopted in the Islamic banking industry is important analytical research for the accounting standards bodies, such as AAOIFI, as well as scholars. Accounting standards bodies are able to develop an insight as to where to position their standards. Secondly, as this study also highlights which environmental factors influence the adoption of accounting standards, it is possible to apply these factors on a case study basis to assess the positioning of the AAOIFI or IFRS standards. Thirdly, governments and regulators which are considering changing their financial reporting regime to accommodate Islamic financial institutions (IFIs) can also benefit from this research. Hence, this study highlights the institutions most likely to affect accounting quality in general in the country. Fourthly, countries considering improving their accounting and financial reporting practices will be able to identify which of the possible forces affect the adoption process. This could be through the internal environment, such as education; institutional settings, such as enforcement mechanisms; or the external environment, such as international trade agreements. Finally, scholars are also able to further their knowledge and understanding from this research to gain insights into the validity of Environmental Determinism Theory (EDT) and institutional theory in the Islamic banking literature spectrum.

1.7 Contributions

This research will contribute to the existing literature in seven ways. **First**, due to the absence of extant literature, this research is the first to investigate the determinants in adopting AAOIFI at country level. **Second**, the existing literature predominantly uses comparative analysis between adopting and not adopting one particular accounting standard; this study, however, conducts comparative analysis between determinants of AAOIFI adoption and the adoption of both local and IFRS standards. **Third**, this research also contributes towards the enrichment of discussions surrounding the enforcement mechanisms, external environmental factors, and internal environmental factors that influence the determinants of standards adoption. **Fourth**, this research's novel contribution is that, for the first time, the financial press is used as one possible factor influencing the adoption process, as suggested by EDT theory. **Fifth**, the researcher considered the weaknesses of prior researchers as they used either unreliable data sources, unsuitable measures for the environmental variables. These

weaknesses are discussed in (Cooke and Wallace, 1990 and Gernon and Wallace, 1995) and they recommended that they need to be consider in International Accounting Research (IAR). Therefore, the measures used in this research for each variable at the country level further contribute to the field for two reasons. Firstly, previous research investigates the determinants of international accounting standards, not including AAOIFI, at the individual country level; however, the measurements used do not represent the variables intended to be measured,¹ whereas this study uses measures related to IBI. Secondly, the variables and their measurements used in this research use up to date data for developing countries, and are country specific as well as industry specific. **Sixth**, the existing literature applies logistic regression as a methodology; however, this study undertakes a new methodological approach within this field of research. Multinomial logistic (MNL) regression has been utilised in this study to conduct comparative analysis between the determinants of the three accounting standards within the same model. Using MNL appropriately reflects the reality that countries have three options of accounting standards to adopt in the IBI, and MNL allows comparisons between the determinants across all three standards simultaneously.

Seventh novel contribution for this study to the literature is its investigation of the relationship between disclosure in IBI and the accounting standard used in the industry. To the best knowledge of the researcher, this is the only study that attempts to examine such a relationship in IBI. The novel contribution for this study is the assessment of the relationship between Corporate Governance (CG) disclosure and Corporate Social Responsibility (CSR) disclosure with three different types of accounting standards used in IBI across thirty countries. This study also discusses the main differences between conventional financial institutions and IFIs in terms of characteristics and also the financial reporting practices for Islamic transactions. This gives an idea about how the two institutions are different, and therefore also justifies the need for different accounting systems, as recommended by some scholars. This study also highlights the importance of the comparative research as a whole, and indicates how the comparative research is important for the accounting field as a whole.

¹ For example, Zeghal and Mhedhbi (2006) and Zehri and Chouaibi (2013) both use the literacy rate for each country as a measurement for the educational level; however, the number of institutions offering training courses in Islamic finance is used. Using the literacy rate does not adequately nor appropriately reflect the number of professionals who have received educational training in accounting standards. Zehri and Chouaibi (2013) discuss the complexities of accounting standards, stating that they require pre-existing knowledge in other areas, such as maths and finance, to be able to understand those standards; they, however, use the literacy rate as measurement of the educational level, which is unable to adequately measure their premise regarding education.

1.8 Research Methodology and Findings

EDT is used to develop the hypotheses in this study, as this theory considers multiple environmental factors which could influence the accounting environment in each country. Using EDT, seven hypotheses examining variables around external, internal, and enforcement mechanisms are developed to analyse the determinants of accounting standards adoption across 30 countries.

This study covers 30 countries that have Islamic finance and IBI. This sample size is divided as follows: 10 countries' adoption of AAOIFI (Bahrain, Mauritius, Jordan, Lebanon, Oman, Qatar, Sudan, Syria, Palestine, Tunisia), 10 countries' adoption of IFRS (Albania, Bosnia and Herzegovina, Kenya, Kuwait, Malaysia, Nigeria, Saudi Arabia, South Africa, Thailand, United Arab Emirates), and a further 10 countries' adoption of local standards in their IBI (Bangladesh, Brunei Darussalam, Egypt, Indonesia, Iran, Iraq, Maldives, Yemen, Pakistan, Turkey). This study also takes into consideration the recommendation of a number of academics (Nobes, 1998; Nobes & Parker, 2012; Pope & McLeay, 2011; Wysocki, 2011) who state that investigation of the outcomes of accounting institutions, such as the adoption of accounting standards, cannot be separated from the other non-accounting institutions such as those factors outlined in Environmental Determinism Theory (EDT). Examples of these non-accounting institutions are: free trade, political stability, economic growth, level of education, financial press, and the enforcement mechanisms in the country. Therefore, this study takes into consideration all other possible factors when designing the regression models for analysis.

After testing the hypotheses of the first objective (determinants of the adoption), the analysis shows that some factors affect the adoption of more than one accounting standards. For example, the financial press and existence of a centralised Sharia committee is likely to influence the adoption of AAOIFI and IFRS. In contrast, other factors are significant in terms of only adopting one accounting standard, such as political stability and level of education in the country.

The result of the analysis of the second objective (consequences of the adoption) shows that there is a significant association between both Corporate Governance (CG) disclosure and Corporate Social Responsibility (CSR) disclosure in IBI and accounting institutions in the adoption of accounting standards (AAOIFI, IFRS, or local). The result also shows that there

are associations between both disclosure types (CG and CSR) and other non-accounting institutions such as political stability, level of education and enforcement mechanisms in the country. This result can help clarify how the adoption of certain accounting standards in IBI is possibly related (not alone, but with other non-accounting institutions) to improve transparency in adopting countries through improving their disclosure practices (Leuz & Wysocki, 2016). The findings also revealed that there is an association between the disclosure score and the adopted accounting standards in the country in IBI. Indeed the result shows that there is a strong association between both (CG and CSR) disclosure and the accounting standards adopted in the country. It is for the first time that the association between the disclosure and accounting standards adoption are proven for IBI at country level. This result can lead to many conclusions considering the link between disclosure and other economic consequences such as (transparency, liquidity, foreign direct investment, reducing asymmetry as discussed in Pope and McLeay, (2011). In Addition, in this thesis it is proven that there is a link between the adopted accounting standards in the country and the disclosure score in the country which is the bases for driving the other possible conclusions that may result from this link such as adopting accounting standards and improving the economic and society in many aspects (e.g. improving employment and investments).

1.9 The Structure of the Thesis

The rest of this thesis is structured as follows:

Chapter 2 discusses the conceptual framework of the thesis, where the importance of defining terms in accounting in international studies is highlighted as the same term can have different meanings in different countries or within different studies. The same chapter discusses most of the terms used in this thesis, and explains their meaning and history when necessary. For example, Chapter 2 discusses terms such as ‘economic consequences’, ‘information production’, and ‘Islamic banks’, as well as comparing accounting roles and principles in Islamic banks and conventional banks. The end of the chapter highlights the importance of the comparative research.

Chapter 3 of the thesis discusses the theoretical framework of the study. This chapter presents the different theories used in the literature to study the determinants of using accounting standards in previous studies. Examples of the theories discussed are: institutional

theory, isomorphism theory, EDT, globalisation theory, and culture-free theory, in addition to other possible future theories. The chapter also analyses the theories and highlights why EDT theory is used in this study to the exclusion of others.

Chapter 4 presents the discussion of the literature review of the determinants and the consequences of adopting the accounting standards. Although the literature on this topic is rich in terms of developed countries, very few studies discuss it in the context of developing countries. To the researcher's best knowledge, all relevant literature concerning developing countries is included in the thesis. Chapter 4 also presents the hypothesis development for both the determinants objective and the consequences objective.

Chapter 5 of the thesis discusses the research methodology. It presents the paradigm of enquiry for the study, a detailed discussion about the methodology, the type of the study, the approach of the study, the triangulation, and why this study is country level. In addition, Chapter 5 also presents all the required information about data collection and sources, along with data sampling and variables measurements.

Chapter 6 In this chapter, there is a detailed discussion about the different variables used in the analysis, including dependent, independent, and control variables. Moreover, this chapter includes all models used in the analysis for the determinants. It also discusses the findings of the analysis. It also includes a detailed discussion about the descriptive analysis, the assumptions of the models used, and the multivariate analysis for objective one: the determinants of adopting accounting standards at country level.

Chapter 7 In this chapter and as in chapter 6, there is a detailed discussion about the different variables used in the analysis, including dependent, independent, and control variables and models used in the analysis. It also discusses the findings of the analysis. The chapter includes a detailed discussion about the descriptive analysis, the assumptions of the models used, and the multivariate analysis for objective two: the consequences of adopting the accounting standards in the countries.

Chapter 8 concludes the thesis. It includes a summary of the findings, research implications, research limitations, and suggestions for the future research.

CHAPTER TWO: CONCEPTUAL FRAMEWORK

2.1 Overview

The current study contributes to the Islamic finance, financial reporting and disclosure literature by introducing new evidence of the link between financial standards adoption and disclosure in the countries of IBI. This current section aims to identify the main concepts and aspects related to the present study. Section 2.1 starts with the definition of accounting systems and financial reporting practices, and highlights the importance of these definitions in the accounting field, especially in the cross-country studies. Section 2.2 discusses issues related to the term ‘economic consequences’. These issues include the definition of economic consequences in the literature, and the importance of economic consequences. Section 2.3 presents the definitions of the information production and disclosure concept in the accounting field. The section also includes a comparison between the aim of information production in the international financial literature and the Islamic financial literature. Section 2.4 starts with the definition of Islamic financial institutions and Islamic banks, followed by the main characteristics of IFIs compared to non-Islamic financial institutions. Section 2.5 discusses the importance of comparative research in the accounting literature, identifying the main literature, and discussing the possible reasons for the differences in international accounting practices. Finally, the last section summarises the main issues discussed in the current chapter.

2.2 Importance of Identifying Definitions in Accounting

The importance of defining the terminologies in the accounting field is emphasised by Nobes (1998), Gernon and Wallace, (1995), who discusses that there are many misunderstandings regarding certain terminology in this field. This happens because there are no clear definitions of specific terminology in studies related to international accounting issues. He discusses further that what is being examined and/or classified are not clarified, which causes obstacles to the introduction of a theory. For example, Nobes (1998) criticises Douppnik and Salter (1995) for the framework they introduced as a possible theory for the differences in international accounting practices. Douppnik and Salter (1995) introduced a framework with

17 possible factors for international accounting differences, including nature of business ownership and financing system, colonial inheritance, invasions, taxation, inflation, level of education, age and size of accountancy profession, stage of economic development, legal systems, culture, history, geography, language, influence of theory, political systems and social climate, religion, and accidents.

Indeed, Nobes (1998) identifies some of the factors suggested by Doupnik and Salter (1995) as wholly unnecessary, including inflation and taxation, history & colonial inheritance, also culture, religion, language and geography, spotting that most of the institutional factors discussed by them actually cause each other. Therefore, Nobes (1998) concludes that Doupnik and Salter (1995) are in effect mixing theories rather than introducing a new theory to explain the differences in international accounting practices. Part of the reason Nobes comes to this conclusion is the misunderstanding caused by the lack of clear terminology definitions. Thus, Nobes (1998) recommends identifying specific terminologies – e.g. accounting practices, accounting system – before working to introduce any theory in the literature related to differences in international accounting practices.

Considering the importance of identifying terminologies as per the recommendation of Nobes (1998), sections 2.2 and 2.3 present definitions of terminologies used in the research. Specifically, when identifying the terms ‘accounting system’ or ‘financial reporting practices’; Nobes (1998) posits the need for each research paper to define the exact meaning of these terms. Hence, in this research, the exact definition of important terminology is set out below.

Accounting system: The term ‘accounting system’ refers to the principles/standards suggested by a country’s authorities to prepare the annual reports for particular sector (such as the Islamic finance sector). In this case, the term ‘accounting system’ is the same as ‘accounting standards adoption’ or ‘financial reporting standards’. This takes into consideration that each country can have more than one accounting system depending on the type of company, such as small or medium enterprise, corporation, or IFI. Hence, as this study examines the accounting system for IFI, the word ‘system’ refers to the system suggested by the authorities to be used in the IFI sector.

Financial reporting practices: This refers to the accounting standards implemented in the sector based on the recommended accounting system by the authorities in the country for that particular sector. Financial reporting practices include the measurements and disclosure

practices recommended by the accounting system implemented in the sector. In terms of whose financial practices are of concern in this research, this study looks in particular at the financial practices of the IFIs in the country.

2.3 Definition and History of the Term ‘Economic Consequences’

The economic consequences of accounting can be defined as the effects of financial reporting in the firm values and the wealth of those who use the accounting information, as well as those affected by others’ decisions based on the financial information (Holthausen & Leftwich, 1983; Zeff, 1978).

In his paper ‘The Rise of Economic Consequences’, Zeff (1978) highlights the history of the term, outlining when it started to rise and when it was accepted and included in the FASB framework. He writes that “The decade of the 1970s is clearly one in which American society is holding its institutions responsible for the social, environmental and economic consequences of their actions” (Zeff, 1978, p.61). This change in society put government bodies, including standard setters, to consider all consequences of any proposed accounting standards. Therefore, the FASB initially included the probable economic and social impact in the board conceptual framework. Second, the FASB held a conference in 1978 in the subject and commission papers to research the economic consequences of certain standards (Zeff, 1978). The IASB added the economic consequences to their objectives when highlighting the need for financial statements to be of high quality, transparent, and comparable. This was done mainly to help participants in capital markets throughout the world to use the financial information in their economic decision making (Article 2 of the IFRS Foundation Constitutions, 2010, cited in Pope & McLeay, 2011). Pope and McLeay (2011, p.236) write that “it is one of the objectives of the IASB that IFRS has role in the capital market participants’ and other users’ economic decisions”.

Scott (2012) defines four criteria for the introduction of any accounting standard. These are: be acceptable, decision usefulness, reduction of information asymmetry, and have favourable economic consequences. According to Scott (2012), having economic consequences for the accounting standard is a core criterion. Scott (2012, p.294) defines economic consequences as “a concept that asserts that, despite the implications of efficient securities market theory, accounting policy choice can affect firm value”.

Sunder (2002, p.222) explains that “Financial reporting standards serve as a template contract among agents who participate in a firm, especially between the investors and the top management”. This takes into consideration that corporation shareholders cannot negotiate the projects as they only can vote *yes* or *no*. Therefore, financial reporting standards are the template contract which act as the law “that govern[s] the corporate characters, issue of securities and rules for exchange listing of corporate shares” (Sunder, 2002, p.222).

2.4 Definition of Information Production and Disclosure

The environment of accounting is both very complex and very challenging. It is complex because the product of accounting is information (Scott, 2012, p.19). The biggest problem with financial accounting theory, according to (Scott (2012, p.460), is how to determine the “right” amount of accounting information to produce socially. The two sections below present the aims of information production in international accounting systems and the Islamic accounting system. Within the discussion, the question raised by Scott (2012) regarding how much information is socially enough is approached.

2.4.1 Information Production in Islamic Finance and International Finance

Scott (2012) categorises accounting information production into three categories. The first category is finer information, where more information is added to the existing financial statements; for example, expanded note disclosures, segment reporting, and additional items in the financial statements. The second is additional information, which means introducing new information systems to report on matters not currently included, for example expanded disclosures of firm risks and future-oriented financial information included in MD&A. The third information production category is credibility. Credibility means that the receiver of the information knows that the supplier has incentives to disclose truthfully (e.g. is the information disclosed by the ‘Big Four’).

As a result of the discussion above, it is very clear that the production of information is necessary to bridge the gap between the information producers through accounting systems and the information needs of the different users. Below, a discussion is presented of the main

points highlighting the aims of producing information for different accounting systems (International and Islamic) to allow comparison and contrast between them.

A) Information production in International Accounting

Internationally, the aims of information production are clearly discussed and summarised by Scott (2012) in his book 'The Financial Reporting Theory'. The aims discussed are:

- Better informed investment decisions.
- Lower cost of capital for firms producing the information.
- Better working markets due to greater investors' confidence resulting from adverse selection and moral hazards.
- Reduction of monopoly power due to improved ability of potential entrants to an industry to identify profitable investment opportunities.
- Timely identification of failing firms.
- Information released by one firm generates information about others.

B) Information Production in Islamic Finance

In Islam, there is no concept of separating state and religion. Thus, Islam dominates all aspects of life for followers, including business activities. There is evidence in literature from the early Islamic state government regarding accounting practice and the introduction of accounting books and procedures in order to comply with Islamic law (Sharia). Zaid (2004, p.153) argues that the early Islamic state encouraged accounting after the introduction of *Zakah* in 624 AD. *Zakah* plays an important role in the lives of individuals and society, being the fourth pillar of Islam. Therefore, proper calculation of *Zakah* is required to comply with Sharia by anyone conducting business. In addition to *Zakah*, the accounting field is encouraged to fulfil the Qur'an's request of recording debts in accordance with *Ayah* 282 and 283 of Surah al Baqarah. The term accounting *Muhasabah* was first introduced by Al-Khawarismy in 1984 (Zaid, 2004). Prior to this, many other terms were used during the early Islamic state to describe the person

responsible for the accounting function. Some of these terms or titles included *Al-Amel*, *Mubasher*, *Al-Kateb*, or *Kateb Al-Mal* (Zaid, 2004).

In his paper, Zaid (2004) discusses seven accounting systems in the early Islamic state along with their objectives. Those systems were introduced for the government during that period; however, according to Zaid (2004), those systems were also properly used by private businesses. The seven accounting systems were: stable, construction, rice farm, warehouse, mint (currency), and sheep grazing accounting. The main objectives of those accounting systems were to ensure accountability, help with decision making, and allow the evaluation of completed projects. Lewis (2001) wrote that the main objective of Islamic accounting is to “discharge those involved in firms from their accountability to the *umma*” or Islamic community. However, Maali and Napier (2008) discuss that the main objective of Islamic accounting is accountability towards God (Allah) and to show compliance with Sharia.

In the Islamic accounting field, the main purpose of information production is to fulfil the Islamic law requirements towards *Umma* (Lewis, 2001). The second reason is to help each Muslim practice their obligation of *Zakah* (religious levy). The information in Islamic accounting cannot be divided as finer, additional or credibility as the purpose of producing the information is an obligation to the party holding it. How much information each party should produce under Islamic law is guided by the principle of ‘do not harm you and do not harm others’. This principle is essentially asking every party to disclose all the required information for the benefit of all parties involved. Each company should disclose any information which may affect the decisions of other parties. The main aims of accounting information production according to the Islamic law (Sharia), as discussed earlier by Lewis (2001) and Zaid (2004), can be summarised as follows:

- It encourages individuals to invest their money, as if it is not it will be subject to reduction by *Zakah* (religious levy).
- It increases trust within the business environment by disclosing the activities of the business, and the fact that those activities are Sharia compliant.

- It helps Muslims to practice their obligation of *Zakah* payments, as the main objective of the information production process in Islamic institutions is to record and disclose all relevant information to ensure correct calculation of *Zakah*.
- Another main purpose of information production in Islam is to protect other people's money, e.g. investors, suppliers and customers, as well as exercising their right to enjoying it. Therefore, it is recommended by the Qur'an to record all debts, no matter how small.

From the AAOIFI point of view, the objectives of producing accounting information through financial accounting are (AAOIFI Accounting Standards 2007, p.19):

- To determine the rights and obligations of all parties involved in the business.
- To protect all parties' assets, including those for Islamic banks.
- To encourage efficiency and fulfilment of disciplines by the management teams of financial institutions, as well as encouraging the practice of Islamic law in all business activities.
- To provide useful information through financial reports.

When analysing the purpose of the information production between international accounting systems and Islamic accounting systems both old and new, it can be seen that both systems are in agreement with the following points: First, both systems support the protection of investors and third parties involved in business transactions. Second, they both increase investment and trust in the business by providing the necessary information to users. Third, they encourage efficiency among businesses' management teams.

On the other hand, Sharia law states that information production is an obligation which must be fulfilled by each person involved in the business. The production of information is a duty of *Umma*, which indicates that there is another motive for information production in the Islamic finance context in addition to the need of the users, which is the duty of the producer (*Wajib*). How much information should be produced by accounting systems following the Islamic rule of obligation and not harming others? The concept of information production in Islam in general and in the Islamic finance industry specifically is different, because the motive to disclose information is not only to fulfil the needs of financial statement users; it is

also a duty of the business to comply with Sharia and to guarantee practicing Sharia guidance within the Islamic finance industry. It is also to fulfil the objective of Islamic finance as an ethical system not only financial system (Asutay, 2016).

2.4.2 Disclosure

Disclosure is part of the information production concept through accounting systems. It can be defined, according to Gibbins et al. (1990), as any deliberate release of information – financial or non-financial, numerical or qualitative, required or voluntary – via formal or informal channels. The disclosure information can be found through different means, e.g. annual reports, conference calls, analysts’ presentations, websites, or interim reports. The most important official disclosure vehicle (document) is the corporate annual report (Hassan & Marston, 2010). Disclosure has two possible approaches. The first approach is based on examining the original direct vehicle, for example an annual report (or part of it). The other approach is to set proxy for the disclosure without the recourse of the original disclosure vehicle, for example using questionnaires and interviews as disclosure proxy as in the AIMR (Hassan & Marston, 2010). Usually, content analysis and disclosure index are used to implement the first disclosure approach of investigating the original vehicle

Two types of content analysis can be used when investigating the original vehicle: first, the conceptual content analysis used to determine the frequency or the existence of certain concepts or key words; and second, the relational content analysis which examines the relationships between concepts in the text. Disclosure indices are used in content analysis to identify certain items from the disclosure vehicle. Marston and Shriver (1991, cited in Hassan & Marston, 2010) define disclosure indices as “extensive lists of selected items, which may be disclosed in company report” Hassan and Marston (2010, p.19). The first to use the disclosure index was Cerf (1961). Hassan and Marston (2010) discuss that because of relaxed enforcement regulations, the trend in developing countries is to examine the compliance level with the mandatory disclosure unlike in developed countries. The disclosure index can be of any item number, and no theory exists in the literature regarding this (Hassan & Marston, 2010). The items in the disclosure index can be either mandatory or voluntary, have equal weight or different weight. The decision of constructing either type of disclosure indices depends on the purpose of the index itself.

This study will investigate how disclosure can change according to the accounting system adopted in any country. The existence of the link between the accounting system and disclosure has recently been examined in the literature for IFRS adoption (Cumming et al., 2011; Frost et al., 2006; Glaeser et al., 2001; Hail and Leuz, 2006; La Porta et al., 2006). However, it has not yet been examined in the context of IFIs. Therefore, this study intends to bridge the gap in the literature and to try to explore such a link between accounting standards adoption and disclosure.

2.4.3 Definition of Islamic Banks and Major Differences between Islamic IFIs and Other Conventional FIs

Jarhi and Munawar, (2001, p.1) define Islamic banks as

“...deposit-taking banking institutions whose scope of activities includes all currently known banking activities, excluding borrowing and lending on the basis of interest. On the liability side, it mobilizes funds on the bases of *Mudarabah* or *Wakalah* (agency) contract. It can also accept demand deposits, which are treated as interest-free loans from the clients to the bank and which are guaranteed. On the assets side, it advances funds on a profit-and-loss sharing or a debt creating basis, in accordance with the principles of the Shari’ah. It plays the role of an investment manager for the owners of time deposits, usually called investment deposits. In addition, equity holding as well as commodity and asset trading constitute an integral part of Islamic banking operation”.

This definition of Islamic banks actually highlights how the IFIs such as the Islamic banks differ to their conventional counterparts. A summary of the differences between IFIs and conventional FIs are summarised more precisely by Llias (2008) as follows:

- Risk Sharing: Islamic institution parties must share all risks of their business activities.
- Profit sharing: Islamic institution parties must share the profit of their business activities.
- Ethical investment: all business activities in Islamic Institutions should be compliant with Islamic law.

- *Riba* (interest) is banned in Islamic institutions according to Islamic law. All
- Levels of interest are disallowed.
- Asset-backing: money is not considered an asset because it is not tangible. All financial transactions should be tied up in tangible assets.

Table 1 Features of Islamic Finance Tools

- The ban of uncertainty: all terms of risks should be clear to all parties involved in the financial transactions

Table 1: Features of Islamic Finance Tools

Type of contract	Liquidity	Guarantee	Rate of return
Debt-Creating Modes			
Qard Al Hasan	—	Collateral	Nil
Credit Sales	Non-liquid	Collateral	Known
Salam	Non-liquid	Collateral	Unknown/known
Istisna'a	Non-liquid	Collateral	Unknown/known
Semi-Debt Modes			
Ijarah	Liquid	Collateral	Known
Sharing Modes			
Musharakah	Liquid	Penalty for misconduct	Unknown
Restricted Mudarabah	Liquid	Penalty for misconduct	Unknown
General Mudarabah	Liquid	Penalty for misconduct	Unknown

Source: Ayub (2007)

In the absence of interest in Islamic finance, Islamic banks introduced number of tools and techniques as an alternative for interest-based business. These tools are based on the principles of participating and sharing, as in *Musharakah* and *Mudharabah*, or based on the deferred principles applicable in respect of credit and forward sales, as in *Mu'ajjal* and *Salam*. Sometimes, a combination of techniques is employed such as *Shirkah* and *Ijarah*, or *Murabaha* and *Salam/Istisna'a*. In addition, return free loans are another facet of Islamic finance tools, as in *Qard al Hasan*. The tools and techniques of Islamic finance and their features are summarised in the table below, as presented by Ayub (2007).

The most common features of the above Islamic finance tools are that they do not deal with *riba* (interest), and all Islamic finance tools are based on the trade concept rather than the

loan concept, as is usual in conventional finance. Another feature is that there is no prefix rate of return in Islamic finance, except for in *Salam* contracts. This implies that the most important factors in Islamic business transactions are value, transparency, disclosure, and the free consent of each party to enter into contracts. A further feature of the Islamic finance tool is that, just as any other business institution, Islamic finance institutions must take pledge/collateral to a satisfactory level in order to collect their receivables back, as IFIs deal in goods and create receivables. Some scholars support the idea that IFIs have a greater need for collateral and documentation than conventional institutions, considering the instructions of the Qur'an and Sunnah for transparency and disclosure in all credit transactions (Ayub, 2007). However, in the sharing mode types of Islamic finance tools, such as *Musharakah*, restricted *Mudarabah* and general *Mudarabah*, the bank can ask for a guarantee against negligence. In terms of risk, understanding the situation in the conventional banks first can help to clarify the point of risk sharing within Islamic banks. Conventional banks give and take risk free return by giving loans and interest as a guaranteed transaction (Ayub, 2007) from the depositors. This is not the case in IFIs, as the institutions conduct business and take risks, therefore it can earn profit or incur losses; in this case, depositors share in the resulting profit or loss.

Taking into consideration the abovementioned differences between conventional FIs and IFIs in addition to the tools of Islamic finance, the following points clarify how financial reporting in IFIs consider these differences in business and reporting practices in order to be considered Sharia compliant. They also highlight the difference between conventional accounting and accounting for Islamic financial transactions (MASB, 2009) in more detail.

First, there is a need to utilise permissible contracts, such as trade, leasing or partnership, to comply with Sharia and avoid *haram*. If the transactions are not tied up to one of these contracts they are not Sharia compliant and, therefore, the purpose of the whole transaction cannot be certified as Sharia compliant. Such contracts can make the entity enjoy returns in the form of sales, rental or dividends. However, any sort of interest is not acceptable.

Second, prohibition of interest must be observed, as Sharia has a different view on loans compared to conventional banks. Conventional loans are a source of income, while in Sharia, a loan is a type of benevolence or charity. Hence, interest is not permitted in Islam. This does not mean profit is not encouraged in Islam; it is encouraged that profit be gained through trade rather than loans.

Third, sources of returns from Sharia compliant contracts such as trade, leasing or partnership should be reported separately as required by Sharia, while any other returns from other sources such as interest should be reported separately to ensure clarity between legitimate returns and interest. The entity can highlight that financing is conducted through Sharia compliant contracts, and not through interest-based borrowing or lending. In Malaysia, it is enough to show the difference using notes which further explain the nature of each transaction (MASB, 2009). In countries such as Bahrain and Oman, a separate line must be added to the statements to identify the amount of noncompliance return.

Fourth, the application of the generally accepted accounting principles to Sharia compliant transactions can result in different accounting treatment than is available in the conventional comparative.

Fifth, in Malaysia, the MASB advocate that not all Sharia compliant transactions need different accounting standards from those available in the conventional comparative. This is because the application of new accounting principles may lead to different economic effects or obscure the overall economic effect of the transactions. This indicates that different accounting practices can lead to different economic effects overall.

2.5 Importance of a Comparative Research

Comparative research is an attempt to identify and explain similarities and differences between phenomena in different locations or cultures (Carnegie & Napier, 2002). In a research context, comparative methods are considered to be the sole of sociology; this can be applied not only to one specific point in time, but also across time (Durkheim, 1982). This type of research is common in international and cross-cultural studies generally. Thus, comparative accounting studies mainly study the impact of culture in accounting. Examples of such studies are Ansari and Bell (1991) and Gray (1988).

Comparative studies in international accounting began during the early 1980s (Carnegie & Napier, 2002). Within the accounting field, comparative international research helped clarify many issues such as the diversity in national accounting systems, diversity in theories, and the influence of one nation's system on other nations' systems (Carnegie & Napier, 2002). However, the trend in comparative research has changed recently, as documented by Gernon

and Wallace (1995). They argue that previously, the trend mainly concentrated on identifying variables influencing accounting nationally and internationally, while recently the trend has changed towards studying the variables which accounting influences. In this study, both trends are investigated; the first trend will be covered by studying the variables that influence accounting standards adoption and compliance, and the more recent trend is investigated through studying the consequences of adopting certain accounting standards.

Carnegie and Napier (1996) propose Comparative International Accounting History (CIAH). The purpose of introducing this is for “examining and explaining cross-national differences in accounting development”. Later, in 2002, they introduced the CIAH framework, which suggests seven factors or dimensions that can be used as guidelines to explain the differences. Those factors are: period, places, people, practices, propagation, products, and profession. Particularly, this framework is used to compare the development of two accounting methods in different contexts.

Wallace and Gernon (1991) discuss the shortage of comparative international accounting theories. Literature such as Belkaoui (1995), Choi and Mueller (1992), Nobes and Parker (1995, 2012), and Radebaugh and Gray (1997) discuss many possible factors for international differences, including a number of theoretical models introduced to answer the question of international accounting system differences. Nobes & Parker (1995, 2012), in their book ‘Comparative International Accounting’, discussed accounting regimes across various countries and highlighted the differences between the regimes, but the comparison mainly focused on developed countries. Gray (1988) suggests a theoretical model based in culture, while Douppnik and Salter (1995) discuss 17 variables possibly causing the differences in accounting systems. Douppnik and Salter’s (1995) framework is used by many researchers as a base for investigating the factors affecting accounting quality, for example in the study by Schultz and Lopez (2001). However, this framework is criticised by Nobes (1998).

Instead, Nobes (1998) suggests a model with three main variables which, according to him, can influence international differences. These variables are financing systems, financial reporting systems, and colonial inheritance. For Nobes, all other variables are consequences of the main variables. For example, economic growth is a consequence of the market type of the country, thus cannot be an independent variable influencing the differences. However, Nobes (1998) admits that the variables identified by him are for developed countries. In the case of developing countries, he explains that other factors can be of high importance such as

religion, a view further supported by Gambling and Abdel-Karim (1991) and Hamid et al. (1993).

Puxty (1987) also asserts that there are four approaches which explain the international differences. The first is the legalistic approach, which emphasises that the government has more influence than professional accounting bodies on financial reporting regulations. The professional approach is opposite to legalistic, whereby it suggests that professional bodies in financial reporting have more influence on companies than government. The hybrid approach is when both the government and the private sector collaborate to form financial reporting regulations, while the market approach reflects the fact that firms are free to choose the most suitable reporting practices (Mohammadrezaei et al., 2013; Gernon and Wallace, 1995).

In recent literature, there are many suggestions for possible environmental factors which may cause differences in international financial reporting. Pope and McLeay (2011) introduce a comprehensive framework to discuss the possible factors causing the differences between accounting systems worldwide. This framework is presented in the figure below.

The Institutional Framework

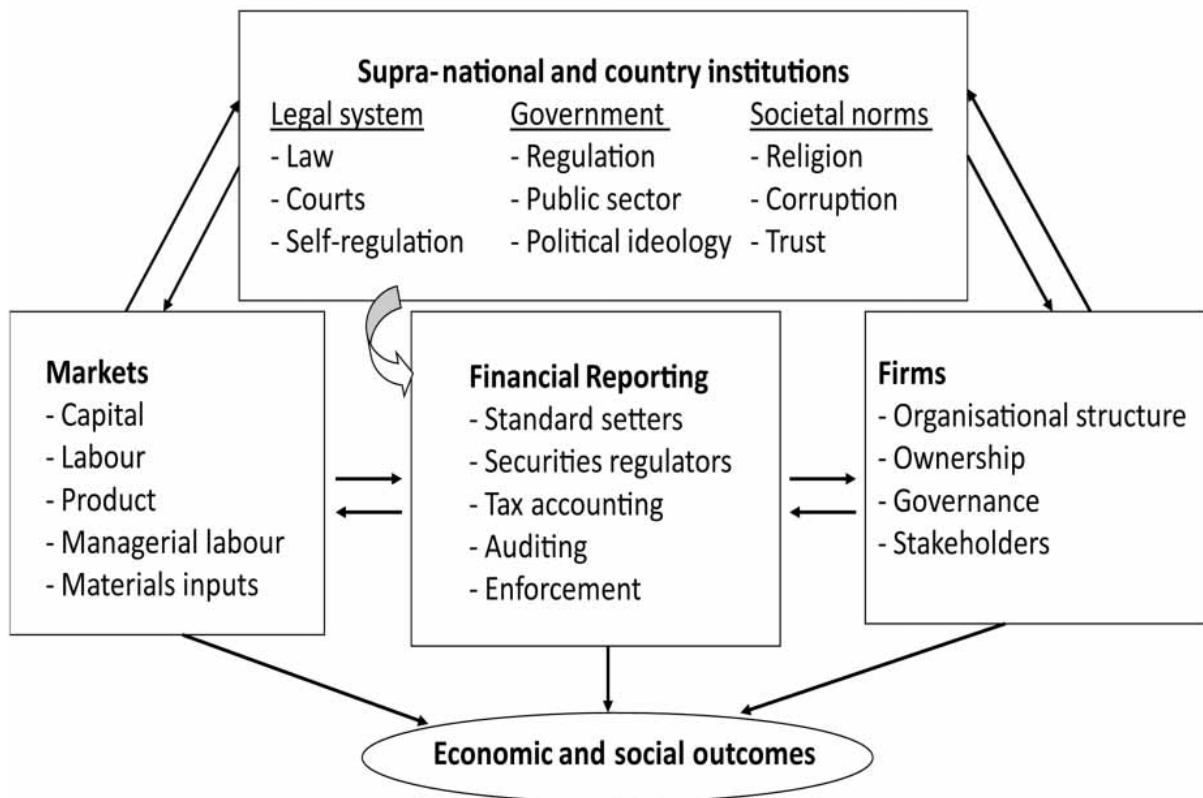


Figure 1: The institutional context of financial reporting (Pope & McLeay, 2011)

All of the abovementioned studies believe in one common fact – that international differences in financial accounting reflect different environmental influences. This study uses EDT theory to investigate possible differences in reporting practices in IBI across countries, where possible variables discussed by Nobes (1998), Douppnik and Salter (1995), and Pope and McLeay (2011) are examined through ED theory to investigate both determinants and consequences of adopting accounting standards in IBI.

2.6 Summary

This current chapter identified the main concepts and aspects related to the present study. It included the definitions of the concepts discussed in this thesis such as, Islamic banking, Islamic finance, information production, disclosure and economic consequences.

The importance of identifying the terms in international studies is highlighted by many key authors in the accounting field for example Nobes, (1998). Nobes, (1998) also discuss the important role of religion as a main factor for accounting differences in the developing countries. This chapter also discussed the importance of the comparative research in the accounting field as highlighted above by (Carnegie & Napier, 2002) and (Nobes & Parker, 1995 to 2012). In addition this chapter also summarised the main studies which highlight the possible factors for the international accounting differences across countries Pope and Mcleay, (2001) for example identified a framework for the possible factors causing the main differences in accounting practices across countries. Even though those factors are highlighted in this chapter however, the main theories emerged throughout the years trying to explain the accounting differences across countries are many and therefore the next chapter is completed to discuss those theories hence 1960s.

CHAPTER THREE: THEORETICAL FRAMEWORK

3.1 Overview

In Chapter 2, the discussion reveals that there are many attempts in the literature to identify the factors causing the differences in international accounting systems. The literature is still growing in this field, and suggestions for the possible factors are increasing. This chapter summarises the most important theories in the literature. Some theories used to explain the international accounting differences are borrowed from other literature such as social science, for example institutional theory and isomorphic theory, while others are suggested based on research within the accounting field, such as EDT and PAT.

3.2 Theories in International Accounting

The determinants of international accounting standards can be related to many theories. Theoretical insights, especially in international fields such as international accounting, can help the researcher to explain those developments in the literature. In particular, discussing and understanding the different theories in the study's field can guide research, help explain results and offer insights into the best forms of implications. Given these benefits, it is definitely worth considering the different theories in social science which has been used to explain the motives of accounting standards adoption in each country. The main theories are discussed in this section, including isomorphism theory, institutional theory, new-liberalism theory (Efficient Market Theory), environmental determinism theory, free culture theory, positive accounting theory and other possible future theories.

3.2.1 Institutional Theory

In general, this theory is the belief that gaining legitimacy in society is the main force for change. It explains that each country can adopt a set of accounting standards only because they are socially accepted, and are being adopted by other countries within the same area or in countries which have the same institutional environment regardless of the usefulness of the adoption decision. Advocators of this theory also believe that the reason behind a country's adoption is usually their reputation for being modern and legally compliant (Carruthers, 1995,

cited in Rodrigues & Craig, 2007). According to Meyer and Rowan (1977, p.340), institutional theory (IT) states that the function of an institution is to gain “legitimacy, resources, stability, and enhanced survival prospects”. The institutional rules, as explained by Starbuck 1976), can be either supported by public opinion or the force of law or simply taken for granted. Greenwood et al. (2002) explain that the institutional factors are social (e.g. culture, religion), technological (e.g. changing technology) or regulatory (e.g. new laws). This means that institutional theory indicates three main forces that can lead to the adoption of accounting standards, including: 1) the force of public such as being modern and gaining social prestige or gaining legitimacy through the educational system, 2) the force of law such as the tax law and audit law, and 3) the granted forces, like to gain resources from higher authorities or technology (Meyer & Rowan, 1977). Mohammadrezaei et al. (2013) state that, in Iran, full convergence to IAS is not possible because of the specific tax laws in the country. This could be one reason why different institutional settings of a country can lead to different decisions regarding accounting standards adoption.

One of the drawbacks of this theory is that it advocates that changes are happening mainly for the purpose of providing legitimacy rather than giving efficiency or improving performance. This theory is thus unable to reveal the consequences of the adoption of each set of standards. Moreover, when applying this theory, it also seems impossible to ascertain the correct measures for legitimacy or social prestige and how they can lead to adoption of accounting standards. It is also too broad for researchers to identify which forces lead to actual adoption of accounting standards.

3.2.2 Isomorphism Theory

Isomorphism theory is another theory that investigates the forces of the adoption decision. This theory says that there are two types of isomorphism: competitive or institutional. Competitive isomorphism is applicable only if there are free and open competitions in the field where change can happen. In institutional isomorphism, there are three different forces for organisations to consider: coercive, mimetic, and normative (DiMaggio & Powell, 1983). Each type of institutional isomorphism is driven from a different source.

- **Coercive** is the political influence, such as the formal and informal pressure of other organisations or the government, as well as pressure from the cultural expectations of society (legitimacy). According to DiMaggio and Powell (1983), usually change

occurs inside the governmental arena or outside of it. For example, the government can impose a law which forces the change, or social institutions can demand a change for public benefit. In addition, modelling to any organisation can occur due to its control of resources. For example, the European Union enforces IFRS otherwise companies cannot get loans with tax exemption.

- **Mimetic** is driven from responses to uncertainty, where organisations with weak systems and uncertain goals are more likely to copy or model the changes of other successful and legitimate organisations. Thus, change can happen not because of competition or improving performance, but rather as a result of uncertainty in the first place. Modelling also can happen indirectly through employee transfer or industry consultancy.
- **Normative** is driven by professionalism. DiMaggio and Powell (1983 p.152) followed Larson (1977) and Collins (1979) in defining professionalism as “the collective struggle of members of an occupation to define the conditions and methods of their work”. The main purpose of this effort is to have a cognitive base and gain legitimacy for their occupation as well as controlling the quality of products. There are two main forces in professionalism in order to force change. First are the educational specialists in each field who force legitimacy through cognitive base. Second is the effectiveness of the professional networks which spread best practices or new methods among each particular field.

One criticism of the abovementioned theories is that both institutional theories, as well as isomorphism theory, admits that different forces can lead to change in organisations. However, both theories link to the desire to be unified with other organisations in the field, and ignore other incentives to change such as external changes (Oliver, 1991). For the purpose of this research, parts of these theories such as the mimetic of isomorphism and the legitimacy of institutional theory are not appropriate to test the effects in the accounting standards adoption process. Since adoption is about introducing new rules to the countries, it is difficult to believe that such a decision can happen in the bases of habits or imitation (Oliver, 1991). According to DiMaggio and Powell (1983), two out of the three types of isomorphism theory relate more to managerial behaviour rather than strategic choices: mimetic and normative. However, professionals are also considering one important force which can drive change regarding accounting standards adoption in the IBI: **Sharia**

requirements in IBI. Sharia professions in this industry have political power represented in Sharia committees, Sharia audit departments, or Sharia advisory boards which can drive changes to guarantee compliance with Islamic law. To this end, Nobes (1998) advocates that the level of accounting professions is the result of different international accounting systems, but not the cause of them.

3.2.3 Environmental Determinism Theory (EDT)

EDT presents that accounting is the product of its environment (Ahmed, 2013; Cooke & Wallace, 1990). Country-specific characteristics such as culture, religion, financial press, economic growth, political and legal systems and enforcement mechanisms in countries play a major role in the adoption of appropriate accounting standards. In addition, EDT advocates the possibility of external environment impact in the adoption decision such as international trade and colonial history. EDT does not emphasise any one force as being superior over the others in terms of impacting the adoption, however it does posit that the forces impacting on the accounting quality of each country differ. The adoption decision in each country can either be driven by its internal environment, external environment or enforcement mechanisms. EDT is widely used in accounting literature; however, it has not yet been examined for AAOIFI adoption or in IBI.

The EDT theory summarises most of the forces discussed in the literature which are possibly driving changes at organisational level as well as country level regarding the acceptance, adaptation and implementation of accounting standards. In contrast, to institutional theory and isomorphic theory, EDT does not emphasise that gaining legitimacy or modelling are forces which drive change.

3.2.4 Globalisation (Neo-liberalism)

Globalisation indicates that the ideologies of competitive markets and privatisations supported by the neo-liberalism movement are important forces in the accounting standards adoption process, especially the internationalisation aspect (Graham & Neu, 2003). Therefore, neo-liberals do not believe in a dual system (harmonisation) as discussed in Rodrigues and Craig (2007). However, they do believe that accounting should present only one economic reality and therefore support convergence. The rationale of neo-liberalism is consistent with the ideology of internationalising accounting standards, as both consider market efficiency as a base (Graham & Neu, 2003). In contrast, Cooper et al. (2003) argue that a universal

accounting system such as IFRS leads to uneven distribution of wealth and sustains the power differences between countries. The globalisation process also does not enable countries to deal with their social and environmental problems (Cooper et al., 1998; Neu et al., 2002).

Globalisation theories such as the neo-liberal and efficient market theories argue the use of one accounting system in all countries, as it is designed to fit all. Those theories totally ignore the role of environment in the decision-making process, and believe that one global standard can solve most problems designed to do such as comparability, transparency and lack of efficiency. Unlike the above theories which believe in the power of internal environment in driving change, globalisation theories believe in only one source of power coming from outside, which is capitalism.

3.2.5 Culture Free Theory (CFT)

Culture free theory highlights that the needs of financial statements' users are the same worldwide, therefore one set of accounting standards can be used universally (Mora, 1995). Aitken and Islam (1984) advocate that accountants throughout the world face the same problems of measurements and recording; thus, it is justified that the same set of accounting standards can fit all countries. The obvious drawback of CFT seems to be that it ignores the particular situations of the context in which the accounting standards are applied, such as country laws, stage of economics, and culture. This might lead to the misunderstanding of the ease of adopting one standard, and it also ignores how external environment can possibly impact adoption.

3.2.6 Positive Accounting Theory (PAT)

Scott (2012, p.304) defines positive accounting theory (PAT) as being "...concerned with predicting such actions as the choices of accounting policies by firm managers and how managers will respond to proposed new accounting standards". Scott (2012) emphasises that PAT has a number of specific characteristics. Firstly, it aims to examine how firms can change for survival and efficiency. PAT attempts to predict managerial accounting policy choices in different environments, institutional settings and across different firms. Secondly, PAT is not designed to tell individuals what they should do or to predict, unlike normative theories which are designed to give guidance and have predictive ability. PAT predicts that managers' choice of accounting policies is driven by the bonus plan, debt covenant and political cost, which can result from increased earnings in one period leading to the possibility

of more taxes. An example of PAT is given by Watts and Zimmerman (1978) who studied how managers' remuneration can impact the accounting standards adoption decision. Much of PAT research is in discretionary accruals, for example as seen in Scott (2012). Unlike other aforementioned theories, PAT includes managerial behaviour, as the choice between standards can be mediated by managers' preferences and motives as stated in the theory hypothesis. Hence, PAT can be studied at the organisational level; however, it is difficult to test this theory in a country level study, as is the case in this research.

3.2.7 Possible Future Theories for Adoption

Other forces exist which can influence adoption in addition to the forces highlighted in the above theories. These new forces are mainly driven by certain organisations. These are not theories yet, however they could develop in the future. For example, multinational companies advocate the convergence to IFRS to save the dual preparation cost of financial statements, especially if the companies are cross listed in the foreign market capital (Chand, 2005). In addition to lowering cost, convergence also enhances comparability of financial statements as the IFRS, for example, help narrow the national differences of financial statements in comparison to international financial statements. This helps international companies located in different geographical areas to overcome this problem when consolidating financial statements (Flower, 1997; Nobes & Parker, 2012). Chand and White (2007) assert that the 'Big Four' audit firms, as well as multinational enterprises and international accounting bodies, are the main forces in globalising international accounting standards (convergence) to serve their own interests. In contrast, Street and Larson (2004) believe that the 'Big Four' audit firms are against harmonisation of accounting standards as it is not efficient in the long run.

Why EDT?

Analysing these theories reveals that different theories believe certain forces to be determinants of accounting standards adoption in each country. Environmental determinism theory indicates that environment is the main force for proper accounting standard adoption. On the other hand, both the culture free theory and the neo-liberalism theory highlight that other forces, like uniformity of the needs of the financial statements' users as well as market efficiency, lead to internationalised accounting standards and support convergence.

Institutional theory deals with the importance of being socially accepted by following other countries in the area or similar industries in their decision to adopt accounting standards. The researchers also test many institutions (variables) as possible determinants such as the variables in figure 1. Those variables are suggested by researchers such as Pope and McLeay (2011). However, these variables are tried by the researchers intrinsically or based in prior research which makes any suggested format as figure1 very broad to be used in one study. Therefore, institutional theory can be used as grand theory however, applying it in one study or using it as a substantive theory is not possible.

Isomorphism theory highlights the role of the state, professions, and the influence of successful companies in effecting change in a country (Dimaggio et al., 1983). Both institutional theory and isomorphism theory consider internal environment as the main force for change with no much focus to the external forces. In the other hand, Chand and White (2007) explain that adoption, and especially convergence to IFRS, is not driven by natural forces such as environmental or economic factors, but in instead driven by the interest of certain parties like MNCs and the Big Four audit companies. In other words, Chand and White (2007) consider the power of the external factors but neglect the power of the internal factors as possible determinants. Consequently, these theories within international accounting literature vary in terms of which forces determine the adoption of accounting standards. However, limited theories consider both internal and external possible forces for the determinants and consequences of accounting standards adoptions.

Since this is the first attempt to study accounting standards adoption in this context, the author looks to identify a comprehensive framework to study the forces that influence the adoption of accounting standards. To consider the context, the IBI context involves a number of features as it is mandated by Islamic law which requires consideration for not only the culture variable in each country, but also other enforcement mechanisms applied in the countries. It is also important to consider other characteristics of the countries in which Islamic banks operate, such as the level of development in the country and the strength of its infrastructure. For example, in developing countries and emerging economies such as where this study takes place, the influence of the capital market or multinational companies is weaker than political and cultural influences. Therefore, any theory used in this study should not neglect any possible aspect that can impact the accounting standard adoption in the IBI context.

The author decided to apply environmental determinism theory (EDT) for several reasons. The main reason is that this theory is more comprehensive and enables the researcher to address many possible variables (internal and external), a factor which was not provided by other theories to the same degree. Further, more specific reasons for choosing EDT are presented below.

First, EDT is considered a substantive theory of the institutional theory (Grand theory) in the field (see Howell, 2013) for more details in grand theories and substantive theories in business field. Unlike institutional theory which is very broad with tens of many possible variables that can be linked to the adoption's determinants and consequences. EDT is focusing in many possible powers (e.g. internal powers, external powers, enforcement powers and professional powers) which are possible environmental determinants for the adoption of accounting standards and their consequences.

In addition, EDT takes some very important factors into account when studying the adoption of accounting standards and their consequences, such as religion and Muslim culture. It is very important for Muslims to practice Islam in all aspects of their life, including finance. As a result, IBI emerged, closely followed by AAOIFI. This indicates that religion is a very important aspect in IBI, particularly where this study takes place. For this reason, this environmental factor cannot be ignored in a study of this type. Hence, EDT theory is considered as the standing point in this study.

Second, the specific features of the Islamic banking industry mean that a special set of accounting standards are necessary, according to scholars (Hannifa & Hudaib, 2002, 2007, 2010; Lewis, 2001). Examples of the unique features in Islamic finance which require the adoption of a special set of accounting standards are risk and profit sharing, which are considered to be the main ideas behind any business activities. Additionally, the framework of this industry only allows ethical business activities, and does not allow the charging of interest (Lewis, 2001; Llias, 2008) which requires a set of accounting standards that take into consideration these features. Hence, EDT advocates that there can be accounting standards as much as there are environmental and this agrees with the reality in IBI because there are many local standards in addition to AAOIFI and IFRS across countries. This makes EDT more close to the reality in IBI which will allow testing for more accurate variables as possible determinants and consequences.

Third reason is very much related to the drawbacks of other theories which make it not possible to be used in IBI context. As other theories have several drawbacks rendering them less useful for this study. For example, culture free theory and neo-liberalism theory advocate the use of a universal set of accounting standards, therefore neither theory can be considered as one set of standards is not practicable in IBI. As discussed before and in practice, there are three different types of accounting standards used by countries adopting Islamic finance (AAOIFI, IFRS, and local). This also implies that it is unrealistic to test the validity of any theory which supports the convergence to one set of accounting standards or supports the use of only one in this particular industry.

Another theory which is used to test for the determinants in the accounting field is the

3.3 Summary

In summary, social science literature is rich in many theories which other researchers have used to address their research. In terms of accounting standards adoption, various theories available suggesting different forces to consider. However, none have been used to investigate the forces of accounting standards adoption in IBI, which makes the author wary about eliminating any possible variable which can affect adoption in this growing industry. Thus, EDT was chosen as the most appropriate theory to adopt in the current study.

CHAPTER FOUR: LITERATURE REVIEW

4.1 Overview

This chapter presents a discussion of the literature relevant to this study. Section 4.2 focuses on literature related to the determinants of accounting standards adoption; section 4.3 discusses literature related to the consequences of the adoption, as those consequences can be observed at the macroeconomic as well as the microeconomic level; section 4.4 presents a discussion leading into the development of the hypothesis for the determinants; and section 4.5 presents a discussion leading into the development of the hypothesis for the consequences.

4.2 Determinants

There is extensive literature in existence concerning the role of the environment on accounting quality and regulation (e.g. Lev, 1988; Puxty et al., 1987; Solomons, 1978; Taylor et al., 1986; Watts, 1979; Watts & Zimmerman, 1978; Zeff, 1978). Initial research exploring this relationship dates back to 1979 (Frank, 1979), and was later confirmed by Cooke and Wallace (1990). This paper will prioritise its focus on the existing literature where its scope encompasses developing countries and emerging markets, as this will ensure consistency with the scope of this research.

Ahmed et al. (2013) claim that “accounting is the product of its environment” (p.182), indicating that the accounting quality and regulation in each country cannot be studied separately from the surrounding environment. Environmental determinism theory (EDT), introduced by Cooke and Wallace (1990), discusses environmental factors and enforcement mechanisms which can influence the accounting quality in each. Environmental factors are split between external environmental factors, such as colonial history, regional economic trade, and international trade, and internal environmental factors, such as the stage of economic development, the goals of society, legal rules, and political system structure, level of education, financial press, and culture. In addition to the internal and external environment, the enforcement mechanisms present in the country also contribute to the guidance of accounting practices, such as the stock exchange, professional accounting bodies, and

judiciary authorities. Rodrigues and Craig (2007) summarise that EDT explains the different factors which can influence the different accounting standards of each country, such as religion, history, culture, and the sophistication of its established institutions. Enhancing Cooke and Wallace's (1990) research on environmental factors affecting accounting quality, two other environmental factors were later introduced by Haniffa and Cooke (2002): namely, human and non-human factors. The typography of human and non-human factors, as introduced by Haniffa and Cooke (2002), represent the corporate characteristics of the firm as well as its management attitude. EDT in its earlier form suggests “that accounting should be a product of the unique environment in which it operates” (Gernon & Wallace, 1995, p.54). EDT also suggests that it is plausible that there can be as many accounting systems as there are countries, since different countries exhibit different environments and accounting practices should reflect those differences. Investigating the environmental factors in different countries that use different accounting standards in the same industry, such as the IBI, presents an opportunity to firstly verify the validity of the theory from different perspectives and contexts, i.e. countries adopting AAOIFI, countries adopting IFRS, and countries adopting local standards. Secondly, investigation of environmental factors can give an opportunity to verify the theory in different contexts, acting as a testing mechanism (Howell, 2013). Testing a theory enables the researcher to confirm or reject the theory based on the results of the verification tests (Popper, 1994, 2002).

The discussions surrounding environmental determinants of accounting standards adoption in the existing literature separate them into two categories. Some articles only consider firms' characteristics as determinants for adoption selection, for example Leuz and Verrecchia (2001) and Trembley (1989). These studies show mixed results; Trembley (1989) studied 53 specialised software firms in the US and found that the adoption choices of US GAAP are usually determined by auditor's opinion and company size, whereas Dumontier and Raffournier (1998) studied 133 non-financial firms in Switzerland and the result shows no significant relationship between voluntary adoption of IAS, debt ratio, and firm performance.

Other articles adopt a broader scope and consider country level determinants, such as capital markets, culture, economic development, educational level, legal system, open to exterior, political system, and language (Abd-Elsalam & Weetman, 2003; Al-Akra, et al., 2009; Tarca, 2004; Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). Dumontier and Raffournier (1998) and Tarca (2004) investigated both firm level and country level determinants for adopting

IFRS and US GAAP. The results of these studies revealed that some country level determinants are of great significance for determining international accounting standards, such as educational level, existence of capital markets (Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013), and language (Abd-Elsalam & Weetman, 2003). Other key determinants, such as culture and economic growth, have also been found to be significant in the adoption of international accounting standards (Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). The majority of studies which investigate country level determinants exclude financial institutions from their samples (e.g. Abd-Elsalam & Weetman, 2003; Dumontier & Raffournier, 1998).

Zehri and Abdelbaki (2013) investigated to what extent country level determinants, such as growth, education, political stability, culture, and the legal system, can influence the selection of accounting standards adoption in a sample of 74 developing countries. They concluded that high levels of economic growth and education, as well as a common law legal system, would result in a developing country being more likely to adopt IAS/IFRS. Delcours and Huff (2015) broadened the scope further and investigated how the influence of country level determinants in developing countries compared to those in developed countries. This study introduced two new variables as possible determinants for the IAS/IFRS voluntary adoption; the governance system, and the strength of investor protection in the country. This study used a sample of 36 countries, with 17 developed and 19 developing countries. Their results suggest that capital markets, the quality of the governance system, and strength of investors protection significantly influence both developing and developed countries' voluntary adoption of IFRS.

Following an extensive review of the existing literature surrounding the determinants of adopting international accounting standards, there was a clear absence of studies empirically investigating the financial services sector. This is a clear gap within the literature which requires further research, especially as the financial services sector is considered to be one of the key industries which drives growth in the economy (Grassa & Gazdar, 2014a, 2014b).

In Islamic accounting literature, continued research is required to better understand the growth of the Islamic finance industry and its newly developed financial products (Haniffa & Hudaib, 2010). Lewis (2001) states that the principles of Islamic finance cannot be met by current conventional accounting, which supports the notion that environmental factors such as religion and culture, have to be taken in consideration when adopting accounting standards.

Vinnicombe (2012) states that in the last twenty years there have been very few studies on how the AAOIFI have empirically tested international accounting standards against the level of compliance that the organisation has stipulated. However, none of these articles investigated the determinants of adopting accounting standards in the Islamic banking industry. Sarea (2012) argues that most studies concerning AAOIFI discuss either understanding or acceptability of AAOIFI standards. Through investigating the determinants of adopting AAOIFI, IFRS, and local standards in the Islamic banking industry, this paper will contribute to the literature.

There is only one theoretical study which considers investigating the determinants of adopting accounting standards in IFIs since the emergence of IBI. Antonio and Mukhlisin (2013) studied the determinants of IFIs in the UK and Indonesia. Following an extensive review of the existing literature, theirs is the only study which discusses the determinants of accounting standards adoption for IFIs. The study adopted Khaldun's model of civilization, where a variety of factors are examined to identify the degree of civilization in a society. These factors are government, Sharia, people, wealth, development, and justice. Their result indicated that the adoption of accounting standards for IFIs in the UK is determined by institutional settings, while in Indonesia it is determined by accounting needs. This highlights the research gap in the literature, thus leading to this research being developed to investigate the determinants of adopting accounting standards in IBI. The determinants literature discussed above is listed in more detail in Appendix A and B.

4.3 Economic Consequences

This section presents how accounting standards adoption can be such an important policy in a country. Section 4.3.1 discusses the macroeconomic and microeconomic effects on countries through changes in accounting polices applied there. Section 4.3.2 discusses studies highlighting the impact of accounting standards on disclosure, and how disclosure can lead to different micro and macroeconomic consequences.

Applying one set of accounting standards can have consequences at the micro level in companies and markets as well as at the macro level in countries. Mueller (1983) discusses in detail how accounting can be used to gain microeconomic as well as macroeconomic benefits. Other research papers go into detail about how financial reporting using IFRS and local

accounting standards can have consequences at firm level, market level and country level. The discussion below highlights the different types of possible consequences of accounting policies and consequences of accounting standards adoption (IFRS/local) at all levels.

4.3.1 Macroeconomic Effect of Accounting Standards Adoption

According to Mueller (1983), accounting can be used directly as a tool to achieve certain economic results. He states that “Close coordination of various business and government efforts is possible when accounting serves directly as an instrument of national economic policies” (Mueller, 1983, p.8). Mueller discusses many possible instances where this can be true; for example, in the area of corporate income tax, accounting policies were used in order to avoid tax-shield so governments could gain more income. In contrast, when the government wants to encourage investment and stability, it will issue policies that encourage investment as a tax-shield. This is exemplified in the use of accounting policies as motives for economic stability in Sweden, where accounting policies such as depreciation are free and companies can tax-shield their earnings under any capital investment. All this, according to Mueller, played major roles in pulling Sweden from the worldwide economic recession of 1957-58.

Financial reporting is also important at the macro level. Mueller (1983 p.17) contends that “reporting does not mean a one directional flow of large volume of all kinds of bookkeeping data. It means the effective communication of accounting information”. In order for accounting to be the instrument to achieve all the nations’ macroeconomic objectives, accounting information should be communicated effectively through reporting. Mueller (1983) also points out that accounting is useful as long as it is a tool to communicate effectively between firms and interested public parties such as shareholders, investors and government. In addition, he also argues that measurements for the sole purpose of keeping records do not justify the cost of doing them. Therefore, accounting, according to Mueller, is one of the instruments to achieve national public policies in countries. Mueller (1983) sets out several important accounting reporting policies that can be very helpful in serving the macroeconomic goals of any nation:

- Income determinations can be one policy nations use to encourage economic stability, where income normalisation is required along with full disclosure of income reserves to serve the purpose of the policy at macro level in the long term.
- Free depreciation: In Sweden, businesses are allowed to expense all of their depreciation regardless of the rate or method used. This encourages businesses to invest more during this period and helps them to grow. Similarly, government projects designed to serve the state (such as defence projects) can have their expenditure amortized. This consequently encourages investment across the entire country, leading to an improved economy.
- Taxation policies: the taxation policy in a country can also be a reason to encourage investments and attract foreign direct investment to any country.

After Mueller (1983) initiated the discussion of international accounting, there has been much research attempting to determine how well the accounting standards boards have managed to meet their objectives so far. However, there is debate in the literature about the objectives of standard setting. Investigation of the accounting standards takes two approaches, with some researchers investigating consequences using the objectives announced by the body as a base for the investigation, e.g. the objectives of the European Commission (EC), and the second approach being to consider the objectives of the accounting standards themselves, such as IFRS, as a base for investigating the consequences. The main objectives of the above bodies are compared and contrasted in Pope and McLeay (2011). Many papers use these objectives to compare IFRS adoption consequences; some researchers consider financial statements objectives to be of increased comparability and transparency (Brüggemann et al., 2013; Cascino & Gassen, 2011; Lang et al., 2010; Liao et al., 2011; Yip & Young, 2012). Others consider the objective of having efficient capital markets and how it will lead to more favourable economic consequences, with several researchers investigating market liquidity (Brown & Tarca, 2012; Brüggemann et al., 2013; Daske et al., 2008; Scott, 2012) and one looking into crash risk (Defond et al., 2011).

On the other hand, some researchers investigate the consequences of IFRS adoption in comparison with certain criteria suggested in the literature. For example, Scott (2012) suggests several criteria and Zeff (2007) determines the obstacles which need to be overcome in the standard setting process. Some researchers prefer to use these criteria instead of the

regulatory objectives to examine the consequences of IFRS adoption. Scott (2012) argues that accounting standards should fulfil the following four criteria:

- improve the decision usefulness of financial reporting;
- reduce the information asymmetry between investors and managers;
- result in positive economic consequences;
- standard setting to be free from lobbying and political influence.

Meanwhile, Zeff (2007) posits that to reach genuine international comparability and convergence of IFRS there are many obstacles which must be overcome. Overcoming these obstacles is seen as criteria for standards setting (Mohammadrezaei et al., 2013). These obstacles can be divided into two groups, according to Zeff (2007). The first group of obstacles relates to culture differences, which consists of four cultural categories: business and financial culture, accounting culture, auditing culture, and regulatory culture. The second group of obstacles relates to the process of setting and applying the standards, e.g. problems of standards interpretation, language translation, understanding common terminologies like 'probability', adjusted earnings measures, and the role of market securities and politics while setting or applying the standards.

Other research papers discuss the consequences of IFRS adoption in terms of whether the IFRS adoption is mandatory or voluntary. For example, literature concerning voluntary adoption is summarised by Soderstrom and Sun (2007). Daske et al. (2007a) study the purpose of voluntary adoption of IFRS and the effect of this adoption. They categorise the firms which adopted IFRS voluntarily as 'serious' and 'label', where 'serious' refers to the adopters who seriously change/update their financial reporting practices according to IFRS standards, and 'label' refers to those companies who adopt IFRS for the sake of labelling their firms as international but very few changes or updates happen in accounting practices post-adoption. The results show that the serious adopters enjoy more positive effects from IFRS adoption than label firms do. Several studies compare mandatory and voluntary adoption of IFRS. Research by Christensen et al. (2008) is an example of a study comparing the effects of voluntary and mandatory adoption of IFRS. The results of this comparison study highlight that mandatory IFRS adoption may not lead to improvements in accounting quality; hence, the economic effects for mandatory adoption were not significant, but were

significant for voluntary adoption. Mohammadrezaei et al. (2013) recommend making conclusions about the consequences of IFRS implementation from review papers instead of considering each empirical paper individually. This because it is easier to see the impact of the adoption from a wider, international perspective instead of only considering it from a local point of view. Taking this into account when reviewing accounting standards adoption literature, the literature review in this section will consider making conclusions from review papers.

However, very few review papers discuss the consequences of implementing IFRS. To the best knowledge of the researcher, those papers are Soderstrom and Sun (2007), Pope and McLeay (2011), Brüggemann et al. (2013), and Mohammadrezaei et al. (2013). Review papers have the feature of discussing some of the determinants of IFRS adoption, the type of adoption (i.e. mandatory or voluntary) and a summary of results from all studies examining different effects. Nevertheless, they do not discuss the appropriateness of the measurements used and the factors which affect the quality of financial reporting associated with each study. These two points are mainly discussed in meta-analysis type research papers. The section below presents research papers that discuss IFRS adoption consequences in general (e.g. Ahmed et al., 2013; Brüggemann et al., 2013; Mohammadrezaei et al., 2013; Soderstrom & Sun, 2007; Pope & McLeay, 2011). Details of the aforementioned papers that discuss IFRS adoption effects are outlined in the following section.

Pope and McLeay (2011) started their research by comparing and contrasting the objectives of the regulatory bodies (IASB, IASB and IFRS) through the years. According to them, the IASB and the IASB based their accounting standards on the 'investor' which is the main assumed user for the accounting information. The authors structure their review paper to evaluate if the IFRS enhanced the decision usefulness objective by meeting its characteristics of comparability, verifiability, timelessness, and understandability. The scope of their review focuses on the archival analysis papers only, as they consider the relation between markets, accounting and financial reporting regime very complex. Thus, only studies which use multivariate econometric analysis to uncover this relationship are considered. Considering the many business activity areas where economic consequences can be affected after IFRS adoption, Pope and McLeay (2011) grouped their 38 review papers in two categories. The first category discusses the research papers that examine the properties of accounting numbers, including increase in disclosure, as economic consequences for IFRS adoption.

Most papers that examine properties of accounting numbers as economic consequences are those conducted via INTACCT researchers. INTACCT research covers many accounting properties as a measure of economic consequences. One is earning management (Ali et al. 2010; Capkun et al., 2010; Garcia-Osma & Pope, 2010). Others are forecast accuracy (Beuselinck et al., 2010a; Choi et al., 2010), accounting choice (Bischof et al., 2010), and disclosure quality (Atanassova, 2008).

The second category involves research papers that examine market outcomes as consequences of IFRS adoption. Daske et al. (2008) and Daske et al. (2009) are two examples of research papers investigating the economic consequences of IFRS adoption in this context. Daske et al. (2008) examine the mandatory and voluntary adoption of IFRS by global firms, testing the market outcomes (liquidity, valuation, and cost of equity) after adoption. Their results show that IFRS adoption affects market outcomes; market liquidity was measured by the bid-ask spreads and trading volume as well as the valuation ratios, which improved after mandatory adoption. This result is significant only for countries where enforcement regime for IFRS adoption is high, and where reporting incentives are also high. Many researchers in their investigation of the economic consequences of IFRS adoption adopt Daske et al.'s (2008) approach of examining market outcomes associated with IFRS adoption (Pope & McLeay, 2011). Examples of studies adopting the same approach include Jeanjean et al. (2010) and Floura and Kosi, (2010). Daske et al. (2009) investigated the market outcomes for the voluntary adoption of IFRS only, and the results were found to be the same as in Daske et al. (2008) discussed above. The findings of Pope and McLeay (2011) show that the consequences of IFRS adoption across Europe are far from uniform and depend on the enforcement regime and the incentives of the preparers.

Brüggemann et al. (2013) produced another review paper; in this, the evidence of IFRS implementations' consequences are measured in light of the European Commission (EC) objectives. They included a table of 29 empirical studies discussing the consequences of the IFRS adoption. His review mainly discusses the intended and unintended consequences of mandatory IFRS adoption, where the intended consequences mean all consequences of IFRS adoption which can be reconciled with the IAS's stated objective; if not, then it will be unintended. Brüggemann et al. (2013) advocate the use of the term 'unintended consequences' and state that the choice of this term is to simply refer to the absence of consequences from

the IAS regulation's stated objectives, and no negative connotation is attached to the role of IAS regulations which are the same as IASB objectives.

The main objectives studied by Brüggemann et al. (2013) are those resulting from enhanced reporting transparency and comparability across countries as a result of adopting the IFRS. The authors divide the objectives of IAS/IASB into three levels, with a chain effect as they describe it. They explain that Level One objectives of transparency and cross-country comparability should lead to Level Two objectives of efficient functioning capital (equity/debt) market, e.g. lower cost of capital, improved capital allocation and increased direct foreign investment. This should result in the Level Three macroeconomics objectives of growth and employment. All effects (consequences) related to the objectives stated in all three levels are labelled as 'intended consequences', with other consequences labelled as 'unintended'. Further to the three-level classification of the IAS/IASB objectives, the authors also highlight that there are two roles for financial reporting that can trigger economic consequences. The first is through its information role, where current and potential investors can use them in the decision usefulness process. The second is through its contracting role, where the stakeholders of the firm can hold management accountable for the resources under their control. The result of this review reveals that no increase in transparency or comparability of financial statements as consequences of IFRS adoption. However, at the macroeconomic level, there is evidence of increased positive effects in the capital markets. The justification given in Brüggemann et al. (2013) for these contradicting results related to the research design of the papers included in his study.

Another recent review paper comes from Mohammadrezaei et al. (2013), who reviewed whether the IFRS have achieved their objectives based on the standard setting criteria suggested by Scott (2012). They explain that considering Scott's criteria and not the stated objectives of the European Commission (EC) can provide useful insights for all users, including the EC. They study 120 empirical research papers concerning the consequences of mandatory IFRS adoption. They managed to map the consequences of IFRS adoption examined in the literature with their corresponding criteria of standard setting suggested by Scott (2012). For example, a conclusion about the decision usefulness criteria of the IFRS can be drawn after summarising the results of the studies which examine certain aspects which lead to a result of decision usefulness. These aspects are the value relevance of accounting numbers, earning managements, timely loss recognition, and the comparability of

financial reporting. To conclude whether IFRS meet the criteria for reducing information asymmetry, the authors considered research papers examining analysts' forecasted accuracy and consensus, and any aspects concerning accounting quality such as disclosure quality, segment disclosure, and earning smoothing. The third criterion is whether or not IFRS lead to favourable economic consequences; the effects of IFRS adoption were investigated by considering the following factors from the research papers: cost of equity, foreign investment, market liquidity, change in the audit fees, and the crash risk. The fourth criterion, that IFRS should not be influenced by any political forces, was considered through research papers with a focus on the cultural and educational background of the IFRS board members and the effect of major industries in forming or suspending a certain standard. However, the authors did not map the consequences with the stated objectives of the IAS/IFRS, which can give good benchmarking feedback about how far those objectives are met to the EC/IASB. Instead, they suggested that the IASB should develop the IFRS based on the accounting criteria suggested by Scott (2012). The results of this review paper show

- a mixture of evidence about the effect of IFRS adoption on decision usefulness;
- that IFRS adoption results in increased foreign direct investment, decreased cost of equity, and mixed evidence about the other economic consequences;
- that IFRS adoption is effective in reducing information asymmetry; and
- The majority of IASB members are from Anglo-Saxon accounting culture, and lobbying is clear when developing certain standards.

Another attempt to clarify the results of some of the research papers investigating the IFRS adoption consequences is to conduct meta-analyses. Only one meta-analysis has been carried out to group the effects of IFRS adoption (Ahmed et al., 2013). Using the meta-analysis technique, the research results are reconciled so a stronger conclusion can be drawn from them. Ahmed et al.'s meta-analysis (2013) reconciles the finding of the studies that investigated a) the value relevance of reported book value of equity and earnings, b) discretionary accruals, and c) analysts' earnings forecast accuracy. The results of 57 research papers are examined in this analysis, and the findings show that the value relevance of earnings has increased, the discretionary accruals are not associated with IFRS adoption, and the analysts' forecast accuracy has increased post-adoption. The results concluded by this

meta-analysis cover only part of the literature, as it is based on 57 research papers concerned primarily with the economic consequences of adopting accounting standards.

The main conclusion to be drawn from the discussion above is that the review papers highlight many interesting aspects from the extant literature, with the first being the inconsistency of IFRS adoption results among studies. Secondly, because the economic consequences of IFRS adoption is now an international study field as IFRS is globally accepted, the amount of literature in this area is vast. Thirdly, the feasibility of investigating the economic consequences of IFRS adoption from many aspects at firm level or country level has been highlighted – for example, changes in these areas after the adoption of IFRS, as discussed in the aforementioned review papers and listed in Pope and McLeay (2011), are considered economic consequences. Examples of these areas include the relevance of accounting numbers, the cost of debt and equity capital, the corporate finance patterns, the investment analysts using IFRS in the decision-making process, accounting practices or policy choice (such as financial risk hedging, benefit pension plan, asset leases and share-option based compensation), business structure (such as mergers, acquisition, joint venture and business segment), and government tax accounting. These papers also indicate the importance of the adoption impact on disclosure as a possible factor which can lead to many other economic consequences.

4.4 Hypotheses Development for Determinants of Accounting Standards

According to Damant (2006), “financial reporting is a chain and the accounting standards are one element only in this chain” (p.30). The framework of country level determinants which influence the adoption of accounting standards was not succinct in the literature (Zeghal & Mhedhbi, 2006). Therefore, many variables used in the literature as environmental determinants for accounting quality and regulations were based mainly on data availability. For the purpose of this research, EDT was chosen as a framework to investigate the determinants of AAOIFI, IFRS, and local standards in the Islamic banking industry. As a result, new variables such as financial press and enforcement mechanisms have been investigated as possible determinants for accounting standards adoption.

However, some of the environmental factors discussed by EDT are very difficult to be introduced, either because of difficulties in measuring them or because multicollinearity

appeared in the analysis, such as culture and colonial history. Based on EDT, this study focuses on formulating its hypotheses using variables in each type of environment within the theory.

4.4.1 External Environment

The external environmental factors and their effects in accounting dimensions are discussed widely in the literature, including colonial history (Nobes, 1998) and free trade and globalization (Cooke and Wallace, 1990). Recently, the literature began to explore the association between external environmental factors and the accounting environment in the IBI (Grassa and Gazdar, 2014a; and Said and Grassa, 2013).

External Economic Openness

Globalisation is one of many factors which can affect accounting. For example, Graham and Neu (2003) posit that accounting as a technology and social activity can serve global institutions. Another variable used in the literature is openness of the economy, which is used by Cooke and Wallace (1990) and Rajan and Zingales (1995) to indicate the volume of international trade in the country. This study measures openness of an economy by using ratio of imports plus exports to GDP, which has been utilised in many previous studies (Grassa & Gazdar, 2014a; Said & Grassa, 2013; Zeghal & Mhedhbi, 2006). As the openness of an economy increases, exports and imports are likely to also increase; this reflects that the business is developed and sophisticated as it is increasing its trade internationally.

In addition, it also reflects the need for unifying the use of the same accounting standards across countries where the same businesses operate to improve comparability and consolidation of accounts. This usually results in countries with international pressures adopting international accounting standards, such as IFRS, to satisfy these needs. Therefore, it is expected that more developed countries where Islamic banks operate will adopt international standards such as IFRS (Zeghal & Mhedhbi, 2006). However, this study takes place in IBI, where the priorities in this particular industry are different than that of other industries. In IBI, the primary objective which needs to be emphasised is that the whole business is required to be compliant with Sharia in order to guarantee continuity. Furthermore, there is no literature to support the argument that countries adopting IFRS in their IBI are linked to the openness of the countries' economy. Thus, the following hypothesis was developed based on the discussed literature above and EDT:

H1: External economic openness in the country is more likely to be related to accounting standard adoption in IBI.

4.4.2 Internal Environment

There is a general agreement in the literature that the internal environmental factors of a country which can affect accounting practices and/or development are: economic development, political systems, capital markets, culture, legal systems, level of education, and tax laws (Arpan & Radebaugh, 1985; Douppnik & Salter, 1995; Gray, 1988; Meek & Saudagaran, 1990; Mueller, 1968). The effects of these factors are investigated in two different ways. Some articles investigate the possible association of these factors with accounting practices, development, or adoption (Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). Other articles use these factors to explain the differences and the similarities in accounting across countries (Brown, et al., 2014; Tarca, 2004). In this study, four internal factors have been considered – economic growth, political stability, level of education, and financial press – to investigate their roles in determining the adoption of accounting standards in IBI across countries.

Economic Growth

The influence of economic factors on accounting is widely discussed in accounting literature (i.e. Arpan & Radebaugh, 1985; Belkaoui, 1983; Mueller, 1963). Adhikari and Tondkar (1992) highlight the importance of economic growth as a cause for financial development. Solomons (1978) emphasises that accounting is strongly associated with economic development since “corporate reporting standards should result in data that are useful for economic provided that the standard is consistent with the national macro-economic objectives and the economic programs designed to reach these goals” (p.67). Mueller (1963) explains that economic development pressures accounting bodies to set accounting standards which will not hinder growth. This implies that “if present-day management in the more developed countries relies heavily on accounting information, then some relationship between accounting and economic development becomes a factor of both economic planning and growth” (Mueller, 1963, p.145). The relationship between economic development and growth has been investigated before as determinants for the IAS adoption (Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). Arpan and Radebaugh (1985) support the argument put forward by Mueller (1963) that economic growth is fundamental for accounting

development in a country. The causality of this relationship is interchangeable, as accounting standards can also promote economic development (Meeks & Swann, 2009; Scott, 2012; Zeff, 1978). Economic development is also used to investigate its association with accounting aspects in IBI (Abdullah et al., 2015; Gheeraert, 2014; Grassa & Gazdar, 2014a; Said & Grassa, 2013). As a result of the discussion above and following the structure of EDT, the following hypothesis has been developed:

H2: Economic growth in the country is more likely to be related to accounting standard adoption in IBI.

Political Stability

The political condition of a country is a particularly good indicator of the stability and development of its financial services sector (Laeven & Levine, 2009; Uhde & Heimeshoff, 2009). Belkaoui (1983, 1985) contends that the political atmosphere has the potential to significantly affect accounting quality and development in a country, as democracy in the political spectrum has encouraged democracy in accounting policies as well. Solomons (1978) argues that “accounting can no longer be thought as non-political” (p.65) considering the standard setting process of the IFSB. If the accounting standard setting process is a political process, it can be assumed that accounting standards adoption is also a political process. This implies that political condition, especially the stability of the political system, is imperative to be able to assess how accounting standards support the general national economic goals of the country.

It is expected, then, that political stability in any country could impact choosing the accounting standards. Hence, it is part of the overall institutions affecting a country’s development. It can also lead to a standard setting process or standard adoption process which considers political aspects as national goals, despite other external and internal factors. Other than the political rights, civil liberty, and political stability of the country, revolutions also can change accounting systems, as seen in Iran. Purjalali and Meek (1995) discovered that the Iranian revolution in 1979 was followed by changes in the financial system, as well as the accounting system. This strongly supports the discussion above that the political condition of a country can affect its accounting system. As a result of this discussion, and following the structure of EDT, the following hypothesis has been developed:

H3: Political stability in the country is more likely to be related to accounting standard adoption in IBI.

Level of Education

Accounting standards are typically complex, and workers require advanced levels of education in order to understand and apply these standards. Gernon et al. (1987) were the first to establish the relationship between level of education and a professional accountant's competence. Douppnik and Salter (1995) and Street (2002) explain that qualified accountants are well trained, and are able to make judgements and deal with complex information. In particular, Islamic finance requires additional qualifications and training to understand the accounting principles related to Sharia in addition to conventional accounting knowledge before recording any financial transaction (Lewis, 2001). Haniffa and Hudaib (2010) argue that the principles of Islamic finance cannot be met by current conventional accounting. Thus, leading countries in Islamic finance, such as Bahrain and Qatar, are using AAOIFI standards which have been designed specifically for this Sharia-based industry. Bank Negara Malaysia, with assistance from the Islamic Financial Standard Board (IFSB), took a different approach and approved the use of IFRS in Islamic banks under the condition that the additional guidance on how to apply IFRS in IFIs was followed.

To be able to determine the most appropriate accounting standards for the Islamic financial services industry, the differences between Islamic and non-Islamic finance must be properly understood. Countries with a sophisticated financial services sector are usually able to provide appropriate education and training. Countries that satisfy this criterion are considered to be part of the Islamic hub, such as Malaysia. Therefore, the availability of advanced financial services education in a country increases the likelihood that the decision to adopt a particular set of accounting standards for Islamic finance transactions is well informed. As a result of the discussion above, and following the structure of EDT, the following hypothesis has been developed:

H4: Level of education in the country is more likely to be related to accounting standard adoption in IBI.

Financial Press

Cooke and Wallace (1990) listed financial press as one of the internal environmental factors that can affect accounting quality and regulations in any country. Prior academic studies on financial press predominantly discuss abnormal stock returns (Francis et al., 2002; Mitchell & Mulherin, 1994), stock prices (Dyck & Zingales, 2003; Palmon & Schneller, 1980), or information asymmetry (Bushee et al., 2010; Frankel & Li 2004). Previous literature surrounding the effects of financial press also report that news plays an important role in corporate governance as well as in capital markets (Bushee et al., 2010; Dyck & Zingales, 2002, 2003; Dyck et al., 2007; Frankel & Li, 2004; Miller, 2006). In addition, Zeff (2007) and Ball (2006) point out that a company's financial performance is discussed in the financial newspapers and magazines in developed countries. However, in developing countries, the role of newspapers and the financial press should not be expected to be as advanced, especially considering that they depend on the government for their funding. In the aforementioned studies, the financial press is considered as a watchdog which reports on companies' violations of accounting practices. However, this study considers it to be an intermediary to raise awareness within the industry; therefore, this study is the first to consider the financial press as a determinant of accounting standards adoption.

Awareness and a well-informed industry is an important aspect influencing many decisions regarding Islamic finance in a country. The AAOIFI is a good example of how awareness is important in many strategic decisions. AAOIFI, as an organisation, is established by the recommendation of the Islamic finance conference (AAOIFI, 10). Workshops, conferences, seminars, articles, and news all contribute in creating awareness, which can be utilised by professionals within the industry to be fully informed on the relevant aspects of accounting standards in their domestic market. As a result of the discussion above, and following the structure of EDT, the following hypothesis has been developed:

H5: Financial press in the country is more likely to be related to accounting standards adoption.

Enforcement Mechanism for Sharia

A healthy financial reporting environment in each country is one way of building trust with investors. How much each country would like to build the trust of investors in the financial

sector depends on how many regulations are available to protect investors and other stakeholders. The regulations in each country have to deal with problems such as information asymmetry, an agency problem to protect its investors including financial reporting regulations (Matoussi & Jardak, 2012; Scott, 2012). Examples of this include issuing different rules to ensure compliance in financial reporting in areas such as disclosure, corporate governance, and contracting (Matoussi & Jardak, 2012).

In this research, the enforcement mechanisms are not investigated as environmental factors which affect the quality of financial reporting practices in the country, but also as factors which can determine the accounting standard adoption in the country for the IBI industry. The reason this is possible is that in IBI there are certain mechanisms to guarantee Sharia compliance in the IBI industry which can affect the decision of accounting standards adoption in the country. For example, the central Sharia committee/Sharia advisory board in Bahrain has issued a regulation to adopt AAOIFI accounting standards in the IBI industry. This implies that the Sharia enforcement mechanism in the country also has an effect on the accounting standards adoption in the country. In addition to being determinants for accounting standards adoption, the quality of the enforcement mechanisms in the country affect the quality of financial reporting practices as well.

The role of enforcement mechanisms in each country is to ensure that the rules, standards and guidelines are fully adopted by all parties concerned. In IBI, it is very obvious that the adoption of accounting standards does not guarantee full compliance. In particular, accounting standards bodies do not have any enforcement power in terms of their developed standards. Therefore, in order to enforce full adoption of the accounting standards, it is very important to consider studying the type of enforcement mechanisms available in the country for IBI. In fact, studying the effect of the adoption of each accounting standard is not possible without first considering the available enforcement mechanisms in each country for IBI along with their effectiveness.

It is very important to initially emphasise that the ‘rule-enforce’ is different to the ‘rule-make’. According to Brown and Tarca (2005), this can be separated or combined depending on the institutional settings. According to Nobes and Parker (2012), the accounting standards body issues the rules and leaves it to other bodies to enforce them. Examples of these bodies are: stock exchanges and their regulators, governments departments and agencies, and private-sector bodies. Nobes and Parker (2012) further explain that there is no superior model

of enforcement which can be applied to all countries; usually it is decided within each country which body will be used and what authority it is given. Indeed, it is the general culture of the country, as well as political and legal environments, that influence its decisions regarding the creation of enforcement bodies. This makes it subject to change as per the environmental changes of the country.

The enforcement mechanisms of different countries can have the same names; however we cannot conclude that they also share the same functions. Brown and Tarca (2007) compared UK and Australian bodies and were unable to ascertain which was the most effective because of the different functions for which they are responsible. The only common mechanism which countries agree on as an important enforcement mechanism is auditing. Nobes and Parker (2012) argue that although auditing is a very important component of enforcement mechanisms, it is not sufficient – especially after the recent audit scandals. This subsequently led to the introduction of the Sarbanes-Oxley Act which controls non-audit services to audit clients, review audit partners, and requires the report of audits to an external committee rather than the client. Therefore, the audit function alone cannot be enough, and both audit and enforcement can benefit from each other as the existence of enforcement can make the audit function easier.

Roles of Enforcement Bodies

Monitor & Action

The main roles of the enforcement bodies, as explained by Nobes and Parker (2012 p.478), are “both to monitor compliance and to take appropriate actions in case of non-compliance”. In other words, enforcement bodies should proactively monitor compliance as well as reacting to it. Enforcement bodies are responsible for testing the financial reports, and in case any mistakes are uncovered, should take appropriate action (Pope & McLeay, 2011a). However, we have to take into consideration that monitoring actions can be restricted to the resources available to the body, hence different countries allocate different resources to such bodies. On the other hand, enforcement actions vary according to the powers given to the body by the regulatory authorities. Appropriate enforcement action can vary widely according to the law of each specific country (Pope & McLeay, 2011a).

Regarding monitoring actions, governments (or whoever is responsible for setting enforcement bodies) face the same difficulties when it comes to deciding what to monitor and

how. Some of these difficulties are discussed by Nobes and Parker (2012); for example, what companies to monitor, the process of monitoring – is it proactive or reactive? – and the type of action to take against non-compliance (administrative or legal?). Nobes and Parker (2012) and Gwilliam et al. (2005) agree that it is difficult to quantify the benefits and costs of the regulatory bodies, as according to them, there are both social and private costs and benefits concerning all types of stakeholder. Some researchers recognise the benefits of involving enforcement bodies to achieve the required goals from the adoption of new accounting standards.

Pope and McLeay (2011) argue that IASB has changed their objectives over time to set them as mainly high quality, understandable, enforceable and globally accepted standards. However, IASB was not exactly clear how to make the IAS enforceable and left this to each country to decide. This leaves the door open, according to Pope and McLeay (2011), for poor financial reporting practices and thus a danger of low quality adoption is very possible. This indicates that, in the presence of weak enforcement mechanisms, this can result in letting the managers' motivations lead the quality of accounting standards adoption. It also indicates that the inconsistency of enforcement mechanisms among the countries can definitely lead to inconsistent adoption of accounting standards. Furthermore, the benefits of applying one standard but not the other are not achieved. These difficulties, as explained by Pope and McLeay (2011), result in the assumption that the countries' enforcement mechanisms are predicted through different suggested proxies to indicate the variation between countries in regard of enforcement practices. In the literature, various proxies are used to indicate the enforcement quality in the countries. For example, control of corruption (Florou & Pope, 2010); rule of law (Daske et al., 2008); and the aggregate earning management index (Leuz et al., 2003). Other proxies can be used in the countries, such as investor protection and the legal system, to indicate enforcement quality (Pope and McLeay, 2011). Some researchers indicate that high quality corporate governance at firm level can effectively replace the weak enforcement environment at the country level. However, other researchers (e.g. Raonic et al., 2004) argue that more regulatory enforcement at country level can enhance the quality of accounting.

The role of strong enforcement at country level to improve the quality of financial reporting practices is recognised in the literature. Therefore, many suggestions are given for improvement of enforcement quality so that financial reporting can be enhanced. For

example, Schipper (2005) highlights the need for the enforcement bodies across the whole of Europe, instead of merely at national level, even though he acknowledges the difficulties of doing so. Leuz (2010) suggests the establishment of the global player segment, in which their main role is to form the corporate governance quality and the ownership structure of companies to reduce the risk of companies being recognised as low quality. Leuz (2010) discusses that this can be the solution for improving the regulatory environment for firms; however, he also admits that this can be a costly solution. Besides being a costly option, it is very critical to assume that this would be easily implemented in the EU. Another suggestion from Pope and McLeay (2011) is that companies could adopt a similar scheme to the health care check in Europe; they name it the ‘financial reporting health check’. The authors further explain this to mean that if any firm in State A wants to benefit by opting under State B (hence it has a credible reporting environment), it should be allowed with the cost tolerated by State A. According to the authors, this system has the advantage of creating competition between different enforcement agencies in offering more efficient enforcement, while also avoiding paying the expenses of states with weak enforcement agencies.

Two enforcement mechanisms are included in this research: the existence of Sharia governance regulation in the country, and the existence of a centralised Sharia committee. These enforcement mechanisms play a significant role, as noncompliance with Sharia in Islamic banking transactions is the biggest risk for the industry. Hence, this would reduce the credibility of banks and may result in discontinuity of the non-compliant ones.

A healthy financial reporting environment in each country is imperative to establishing and building trust with investors. The level of desired trust from investors in the financial services sector is dependent on the strength of regulations enforced which protect investors, especially, and all other stakeholders in general. The purpose of these regulations is to mitigate market failures, such as information asymmetry (Matoussi & Jardak, 2012; Scott, 2012). Different regulations address separate issues, and ensure a level playing field amongst all businesses within each industry – or across industries – in areas such as disclosure, corporate governance, and contracting (Matoussi & Jardak, 2012). Matoussi and Jardak (2012) demonstrate the importance of the two enforcement mechanisms mentioned above, namely Sharia governance regulation and a centralised Sharia committee. The biggest risk within the IBI is noncompliance with Sharia law, since failure to meet this crucial regulation affects the

credibility of the bank and may lead to closure of the organisation if noncompliance continues.

Centralised Sharia Committee

Pope and McLeay (2011) introduce many possible institutional factors which can affect accounting quality. According to Pope and McLeay (2011), the environment is regulated stringently, considering all the rules surrounding the financial reporting process in each country. Examples of these rules are security market rules, tax authority rules, and industry frameworks issued by governments.

In the context of IBI, Islamic banks are voluntary in all Islamic countries except for Iran and Sudan (Casper, 2012). In countries where Islamic banking is optional, Sharia's supervisory system must be in place to ensure the stability and development of the IFS (Grassa, 2013b). There are two types of Sharia supervisory system, operating at the national or institutional level. For example, the Central Bank of Bahrain plays both of these roles; however, Saudi Arabia has neither, and delegates the responsibility to individual institutions to self-regulate on a voluntary basis (Grassa, 2013b). The existence of a centralised Sharia committee enhances compliance with Sharia at an institutional level, and acts as a judiciary in resolving conflicting opinions between Sharia advisories and institutions, which is the case in the UAE, Qatar, and Kuwait. The need for a centralised Sharia committee to advise and resolve conflicts can also influence decision making related to IBI in the country, such as accounting regulations and accounting standards adoption. As a result of the discussion above, and following the structure of EDT, the following hypothesis has been developed:

H6: The existence of a centralised Sharia Committee in the country is more likely to be related to accounting standards adoption in IBI.

Sharia Governance Regulation

The Islamic finance sector has its own unique features when compared to the conventional finance sector. Therefore, regulations related to IBI, such as accounting and auditing in Islamic institutions, Sharia governance, and *Sukuk* regulation, can lead to a progressive, healthy financial reporting environment in countries where Islamic banks operate. Problems such as information asymmetry and agency costs can be mitigated against, which will lead to increased transparency and reliability of financial reporting. Laws in Islamic countries are

built on the foundations of Sharia law, which is the source of all the other judiciary systems in Islamic countries. According to Grassa (2013a), a framework for Sharia governance is becoming more essential due to the rapid development of the Islamic finance sector. “Sharia governance is defined as the internal mechanism which helps to ensure that an Islamic financial institution complies with Sharia in its operations and activities and which helps it to achieve the objectives of *maqasid al-shari’ah*” (Grassa, 2013a, p.171). Sharia governance regulations can affect the accounting standards adoption process, since Islamic banks are required to comply with the Islamic principles. The enforcement mechanisms in this industry operate in two distinctive ways. There is a monitoring role to enable the identification of non-compliance, and there is an action role where regulatory tools can be utilised to bring companies back into compliance. As a result of the discussion above, and following the structure of EDT, the following hypothesis has been developed:

H7: The existence of Sharia governance regulations in the country is more likely to be associated with accounting standards adoption in IBI.

4.5 Hypotheses Development for Consequences of Adoption of Accounting Standards

4.5.1 Economic Consequences of Adoption of Accounting Standards

The consequences of adopting accounting standards can be investigated using different perspectives. Some research argues that the objectives of the standard bodies for improving the comparability or the transparency is the right measure for the benefit of adoption, as discussed in the above section. Other studies look at how much the financial numbers or disclosures improve after adoption (e.g. Atanassova, 2008; Verriest et al., 2010). Disclosure can also be used as a measure to describe how much information asymmetry has reduced, which is a kind of favourable economic consequence for the issue of accounting standards by standards boards and adoption of certain accounting standards in the country (Scott, 2012). The section below discusses the importance of achieving disclosure improvement when adopting certain accounting standards in the country, as this is one of the main issues that can be improved by standards adoption. Disclosure can also be one of the main areas that, if improved, will lead to other improvements at the micro and macro levels in the country.

According to Pope and McLeay (2011), economic consequences and disclosure desired by the policy makers of adopting IFRS can happen only if there are improvements in the financial statements figures. This can happen when improvements occur from compliance with the disclosure requirements after adoption. It is also possible through improvements in the properties of accounting numbers which are relevant to financial statement users, as a result of the change in accounting standards adoption. The possibility of a change to accounting numbers occurs when the measurements and the recognition rules differ between the adopted standards. In relation to disclosure, admittedly the literature is inconsistent about how much IFRS adoption can improve the disclosure of financial statements. Atanassova (2008) reveals that after switching to IFRS, the Bulgarian banks did improve the quality of their disclosure. In a study to compare first time adoptions of IFRS with prior GAAP reporting, Verriest et al. (2010) found that disclosure was improved – especially when the firm enjoys strong corporate governance policies. This inconsistency in the literature regarding the result of the adoption of each set of accounting standards implies that the improvement of adopting any accounting standard is context-specific, as further reported by Pope and McLeay (2011).

Leuz and Wysocki (2016) discuss that disclosure and financial reporting are crucial core policy issues, and deserve more attention from academic research. For Leuz and Wysocki (2016), there is demand for further economic or cost benefit analysis for current as well as past regulations and standards, especially after the series of recent financial scandals and crises which resulted in reformation of disclosure and reporting regulations. Another reason is the trend for countries to adopt IFRS in an attempt to increase the harmonisation and convergence of accounting standards. In addition, issues like disclosure and financial reporting are current global issues, as a result of the competition between countries' national capital markets in being international. Leuz and Wysocki (2016, p.2) explain that both “regulating disclosure and setting accounting standards are intertwined”, and they recommend studying the economic effects of both as a first-order importance instead of studying them as part of corporate reporting.

There are a lot of studies that summarise the arguments for and against disclosure requirements. Examples of studies that discuss the effect of particular standards include Holthausen and Leftwich (1983), Watts and Zimmerman (1986), Fields et al. (2001), and Kothari (2001). However, the focus of this research is to study the difference of disclosure

impacted by the adoption of different accounting standards. Thus, this research will concentrate on studies such as Hart (2009), Zingales (2009), Bushman and Landsman (2010), and Leuz (2010).

Generally speaking, there are two types of effects that can be quantified by studying improved disclosure at the micro level. There can be real effects and capital market effects, as explained by Leuz and Wysocki (2016). While capital market effects reflect the behaviour of the information receiver, real effects relate to the non-reporting behaviour of the information sender: either the disclosing manager or the reporting entity. Non-reporting behaviour can be related to investment, use of resources, or consumption (Leuz & Wysocki, 2016). In regard to capital market effects, the two most heavily discussed capital market effects of improved disclosure at micro level are market liquidity and the cost of capital, as there are direct theoretical links. Other economic benefits discussed in the literature are Tobin's q theory, investors' portfolio allocations, capital raising, and structure and investment behaviour.

4.5.2 Outcomes of Improved Disclosure at Micro Level

Capital Market Effects

The market liquidity effect of improved disclosure is discussed widely throughout the literature. Copeland and Galai (1983), Glosten and Milgrom (1985), Kyle (1985), and Admati and Pfleiderer (1988) argue that the information asymmetries among investors introduce the problem of adverse selection into share markets. Adverse selection can result from the actions of uninformed (or less informed) investors by exiting the market to minimise potential losses; hence, they worry about trading with better informed or private investors. This can reduce the liquidity of share markets, hence the ability to quickly sell and buy shares will be reduced. Verrecchia (2001) discusses that the adverse selection problem can be reduced to improve market liquidity through corporate reporting and disclosure. This effect of improved disclosure on information asymmetries and market liquidity is also confirmed by a number of other studies, including Welker (1995), Healy et al. (1999), Leuz and Verrecchia (2001), Heflin et al. (2005), and Brown and Hillegeist (2007).

Another aspect of the capital market economy's link to disclosure and financial reporting which has been widely analysed is firms' cost of capital. There are several theories concerning this link, as summarised in Leuz and Wysocki (2016). One theory is that the link

between disclosure and liquidity could also result in a cost of capital effect, where the illiquidity and bid-ask spreads could increase the trading cost of investors and they will expect to be compensated in the equilibrium (Amihud & Mendelson, 1986; Constantinides, 1986). Another theory suggests that more disclosure and better reporting can improve risk sharing in the economy, resulting in a reduction of the market- risk premium. These effects are particularly apparent in two situations: when investors are not aware of all firms in the market, and when less risky investors are afraid to hold shares because of adverse selection concerns (Diamond & Verrecchia, 1991; Merton, 1987). The final theory shows there is a direct link between disclosure and expected returns (cost of capital) arising from estimation risk (see e.g. Barry & Brown, 1984, 1985; Brown, 1979; Coles & Loewenstein, 1988; Hughes et al., 2007; Jorgensen & Kirschenheiter, 2003; Lambert et al. 2007, 2012). The results of the empirical literature for the economic link between disclosure and cost of capital are inconsistent. Some studies document negative associations (e.g. Botosan, 1997), while others who examine this link outside the USA document different results than the ones in low disclosure environments (e.g. Daske, 2006; Hail, 2002). Conversely, some studies conclude that there are no associations between disclosure and cost of capital (e.g. Larker & Rusticus, 2010).

Other capital market economic links of disclosure are discussed in the literature from different perspectives. For example, some studies examine capital raising activities with disclosure quality and quantity, rather than the cost of capital (e.g. Frankel et al., 1995; Healy et al., 1999; Lang & Lundholm, 2000; Shroff et al., 2013). Other studies examine the link between firms' reporting quality and cost of equity; most of these studies reported a negative relation (e.g. Aboody et al., 2005; Barth et al., 2013; Ecker et al., 2006; Francis et al., 2005; Kim & Qi, 2010; Ogneva, 2012). Studies that focus on the cost of debt (e.g. Zhang, 2008) report that firms who report conservative return earnings usually obtain lower interest rates from lenders; this is in contrast to Francis et al. (2004), who reported the opposite phenomenon.

Real effects

There are several links which have been highlighted in the literature which reveal the real effects of improved disclosure. One proposed link is that better disclosure reduces information asymmetries, and better disclosure and reporting can subsequently improve the efficiencies of outside parties such as investors' and analysts' decisions. This can be reflected

in more accurate managerial decisions (e.g. Bushman & Smith, 2001; Lambert et al., 2007; Lombardo & Pagano, 2002). Other studies suggest that there may be a link between disclosure and reporting quality with higher investment efficiency (e.g. Badertscher et al., 2013; Bens & Monahan, 2004, 2006; Biddle & Hilary, Biddle et al., 2009; Bushman et al., 2006; Cheng et al., 2013; Goodman et al., 2014).

4.5.3 Outcomes of Improved Disclosure at Macro Level

Leuz and Wysocki (2016) assert that the effect of a firm's disclosure can trigger many effects to other firms, such as those in the same industry or management of other firms (competitors) as well as investors. For example, Dye (1990) and Admati and Pfleiderer (2000) report that the effects of the disclosure information of one firm can result in information spillover and externalities. It also can reduce agency problems in other firms (Leuz & Wysocki, 2016). The disclosure of operating performance and governance changes can provide useful benchmarks for other firms in the industry, and gives more information to investors which ultimately leads to a reduced cost of monitoring so investors can better evaluate choices. A further effect is information transfer, since the earnings announcement of one firm also gives information about the earnings of other firms, which emphasises that there is information transfer (Baginski, 1987; Clinch et al., 1987; Foster, 1981; Han et al., 1989; Han & Wild, 1990; Olsen & Dietrich, 1985). Newer studies consider the effect of firms' misreporting on competitors or the industry as a whole; misreporting has an effect on much more than just penalties of the market regulator, as they have a spillover effect on competitors (e.g. Gleason et al., 2008; Silvers, 2016) as well as on the investment decisions of their peers (e.g. Beatty et al., 2013; Durnev & Mangen, 2007; Sadka, 2006; Sidak, 2003).

4.6 Consequences of Adoption and Disclosure in Developing Countries

The consequences of accounting standards adoption tend to be discussed in terms of IFRS adoption, mandatory and voluntary adoption, or in comparison with other local standards such as German GAAP or US GAAP. Most of the literature, as per the discussed review papers above, mainly covers developed countries. However, there is a paucity of studies with a focus on IFRS adoption in developing countries, a point also raised by Mohammadrezaei et al. (2013). Compared to the huge amount of literature studying the effects of IFRS adoption at firm level in one country, there are significantly fewer papers discussing the effects of

IFRS adoption across several countries. This study tries to establish a link between financial reporting standards adoption and disclosure to improve the reporting quality in the country. In addition, this research considers studying the link between how mandated financial accounting standards can also change the disclosure requirement in the country. The following section presents a range of literature discussing, in particular, the macroeconomic effects of mandated financial reporting regulation and disclosure.

Corporate Disclosure

Corporate governance can refer to mechanisms used to help resolve agency problems in a firm (Hart, 1995). There are different types of CG in the world; according to Beekes et al. (2016), the type of CG depends on the type of institutional investors, shareholders, managers and debt holders in the country. Therefore, different countries can end up with different CG procedures. Indeed, it is commonly believed that better governed firms should disclose more information to stakeholders and be more transparent, and more monitoring mechanisms are available with CG. La Porta et al. (1998) also concluded that, for example in common law countries, there is more governance to monitor disclosure in the equity market. Therefore, common law countries usually provide greater levels of investor protection.

Hart (1995) explains the principal-agent theory regarding the relationship between firm, owner or shareholder principles and firms' CEO agents. Hart explains that the agent acts in self-interest at the expense of the principal's best interest. The cause of the problem is that the principle cannot observe all agent actions, which results in information asymmetry. The agent's opportunistic behaviour can be restricted by providing the manager with incentives such as share options or by incurring monitoring costs, such as auditing the firm's financial statements. Usually, there is a contract to specify the duties of the agent toward the principle, however Hart (1995) highlights that contracts are often incomplete. Fama and Jensen (1983a, 1983b) discuss that the enforcement of contracts is costly, and Beekes et al. (2016, p.206) describe CG as "the framework for resolving matters not fully specified in the contract".

CG has many other roles (OECD, 2004), including protection of shareholders' rights, the equitable treatment of shareholders, good disclosure practices and firm transparency, and an effective board. Therefore, CG disclosure can actually be useful in some situations, as summarised in Beekes et al. (2016). First, it can reduce information asymmetry (Bushman et

al., 2004) and also help the shareholders to monitor the management's activities. Second, it can reduce the cost of capital, as it provides reassurance to investors (Botosan, 1997; Sengupta & Zhang, 2015). Third, firms which disclose more can also enjoy more stock liquidity, hence more analysts are able to analyse their information due to the lower information cost (Helay et al. 1999). Moreover, disclosure can also work as an indicator of a firm's quality to attract potential investors (Akerlof, 1970).

Very similar roles were reported by Ho and Wong, (2001, p.143), in that "more governance mechanisms will strengthen the internal control of companies and provide an intensive monitoring package for a firm to reduce opportunistic behaviour and information asymmetry". Therefore, governance in general helps to control fraud and illegal activities in addition to reducing information asymmetry.

There was concern about whether corporate governance introduced in Western countries disagrees with the Islamic principles of Islamic corporate governance. The Gulf countries and others in this research are Muslim countries, and any corporate governance recommended by most of these countries must agree with the Islamic religion. A study by Abu-Tapanjeh (2009) assesses how compatible Islamic instructions for business are to corporate governance, and it was pointed out that the principles of Islam are very much compatible with the principles of corporate governance in the OECD.

Baydoun et al. (2013) present an important paper which gives a clearer picture of the corporate governance in five Gulf States (Kuwait, Bahrain, the United Arab Emirates, Qatar, and Oman). In their paper, the authors compare corporate governance in the Gulf States using information from the Organization for Economic Co-operation and Development (OECD, 2005) survey data. They constructed measures of the corporate governance to compare and contrast the availability and non-availability of corporate governance in the Gulf States, taking into account the development in the countries. The OECD framework has three main categories to measure corporate governance in the MENA countries. These categories are: shareholder rights and obligations, internal enterprise processes, and transparency. Their findings show that Oman is the only state which has a very clear structure of corporate governance. In 2002, Oman was the first country to establish corporate governance regulations through issuing a code of corporate governance. In 2006, the Dubai International Financial Centre (DIFC) established the Hawkama (Governance) Institute as part of an

association with international agencies to harmonise corporate governance in the UAE (Baydoun et al., 2013).

Another study concerning governance in the MENA region was conducted by the Union of Arab Banks (2003), who studied governance practices in public listed companies in Kuwait, Saudi Arabia and the UAE, including the non-GCC countries of Lebanon and Jordan. The findings of the studies by the Union Arab Banks and Baydoun et al. (2013) suggest that there is a need for a clearer corporate governance system in the Gulf countries to encourage transparency, “Especially that most ownership and control of companies reside in substantial family corporate holdings and that boards of directors are dominated by controlling shareholders, their friends and relatives” (Baydoun et al., 2013, p.11).

Abdullah et al. (2015) investigated the determinants of corporate governance disclosure in Southeast Asian and GCC countries. They investigated 67 Islamic banks, and how the strength of corporate governance in Islamic banks can result in increased levels of voluntary disclosure. Particularly, they investigated how board independence, board size, the separation of the roles of board chair and chief executive officer (CEO), audit committee independence, audit committee size, and audit committee financial expertise can all lead to higher levels of disclosure practice in Islamic banks.

Grassa and Matoussi (2014) compare and contrast the state of the governance system in the Gulf countries (Kuwait, Bahrain, United Arab Emirates, Qatar, and Saudi Arabia) with the governance system in Southeast Asian countries (Malaysia and Indonesia). These are the leading countries for Islamic finance. They collected data from 83 Islamic banks in these countries from 2002 to 2011. The mean and the median were used to compare and contrast the governance system in these countries.

The findings of Grassa and Matoussi’s (2014) study show that there are huge differences in the governance system between the GCC countries and the Southeast Asian countries. According to Grassa and Matoussi (2014), this implies that there is a need for further research to analyse the governance system in countries which allow Islamic finance.

CSR Disclosure

Corporate social responsibility (CSR) research emerged in the middle of the 20th century, and the concept of this term has changed a lot since it first came about. The focus of CSR changed from being a tool to maximise the wealth of shareholders toward being more considerate of society's needs (Mele, 2004). Therefore, many definitions can be found in the literature which attempt to define its actual meaning. One definition of CSR is “the duty of firms to create wealth in ways that avoid harms to, protect or enhance societal assets” (Steiner & Steiner, 2009, p.135), while Hopkins (2005, p.22) wrote that one of the objectives of CSR is “to create higher and higher standards of living, while preserving the profitability of the corporation, for its stakeholders both within and outside the corporation”. Other definitions include Guthrie and Parker's (1990) view, which states that the function of CSR is not new for corporations as it has been used previously to enhance decision making internally and externally. Gray et al. (1987) define CSR as being an operational tool used by business entities to demonstrate social responsibilities. Gray et al. (1996) also explain that companies disclose their CSR activities to discharge their accountabilities. Similar concepts are discussed by Lewis (2001) for the purpose of accounting and disclosing Sharia transactions, as he emphasises that the purpose of accounting Islamic transactions is to discharge the accountability of the business toward society.

As can be seen from the definitions above, the term ‘CSR’ can be understood as an obligation which serves different objectives for both corporations and society. The dimensions of the CSR concept are clearly summarised by Carroll (1991) as he notices that the research on CSR can be categorised into four dimensions: economic, ethical, legal, and philanthropic responsibilities. Following this framework for CSR disclosure, any business can enjoy a number of advantages, for example creating positive relationships with consumers and stakeholders, or developing an attractive corporate image. Furthermore, CSR enhances corporate reputation with all stakeholders and many scholars believing that CSR can be considered long-term profit maximisation (Glautier & Underdown, 2001). Friedman (1962) also argues that the social responsibilities of business management can result in increased firm values of the business in the long run.

Van der Laan Smith et al. (2014) question the effect of mandatory IFRS adoption on the CSRD, considering CSRD is voluntary disclosure. Their paper contributes to the literature by investigating how the mandatory adoption of accounting standards can improve the voluntary

disclosure of CSR. Stockholder theory was used as a base for the study. The study considered samples from shareholder-oriented countries such as Australia and the UK, and also considered firms from stakeholder-oriented countries such as Belgium, France, Germany, Italy and the Netherlands. The sample included fifty European companies and nine Australian companies. The findings show that the UK and Australian firms experienced a significant improvement in CSRD after the adoption of IFRS, unlike the stakeholder-oriented countries as the results did not show any improvement in regard to CSRD after IFRS adoption.

The existing literature for the CSR in IBI has two approaches. One approach focuses on the level of CSRD (e.g. Abdul Rahman et al., 2010; Aribi & Gao, 2012; Haniffa & Hudaib, 2007; Hassan & Harahap, 2010; Maali et al., 2006), or the determinants of CSR in IBI (as in El-Halaby & Hussainey, 2015; Farook et al., 2011). However, there are no CSR disclosure scores calculated at country level covering all IBs in the countries allowing Islamic finance.

El-Halaby and Hussainey (2015) investigate the determinants of CSRD in Islamic banks in 25 countries for 138 Islamic banks. Content analysis was used to examine the compliance with social disclosure based on AAOIFI governance standard N^o.7. The study was conducted for the year 2013. The annual reports of 138 banks were examined to ascertain the compliance score for each bank. The result of the study reveals that there is an association between a bank's CSRD and its characteristics, such as bank size, accounting standards, and the existence of a Sharia auditing department. In addition, the result shows an association between CSRD and country level characteristics, such as GDP growth.

Aribi and Gao (2012) investigated the influence of Islam on corporate social responsibility disclosure in IFIs, with a focus on the narrative disclosure of 21 IFIs from GCC countries. The authors utilised content analysis to conduct the study. The study confirms that Islam has a strong influence on the CSRD in IFIs; hence, most of the items disclosed in the reports were produced by the SSB. IFIs also produce other items, such as *Zakah*, interest-free loans, and the confirmation of compliance with Sharia in addition to other philanthropic activities. Aribi and Gao's (2012) research made a valuable contribution to the CSRD literature, as they investigate the role of religion as a possible determinant for CSRD. The authors also recommend considering the social-cultural determinants of CSRD. In their methodology, Aribi and Gao (2012) focus on examining the influence of Islam in CRSD, and use the main principles of Islam (e.g. *Zakah*, *Al-qard al-hassan*, *Ihssan*, Brotherhood) to construct the categories of the content analysis checklist. Therefore, the content analysis of their study was

constructed to include the following categories: Employee, Community, Charity, *Zakah* Products and Services, Customer, Sharia Board Report, and Other. They concluded that Islam is one of the main determinants of CSR in IFIs. Their conclusion is also consistent with results from Ullah and Jamali (2010), who view Islam as a broader framework for CSR than any other theoretical framework.

Kamla and Rammal (2013) examine 19 Islamic banks through content analysis to examine social reporting in Islamic banks, including social justice, poverty eradication, and redistribution of wealth. The results show that the Islamic banks included in the study lacked specific or detailed information regarding social reporting, which contrasts to the information they provide regarding adherence to Sharia principles.

Regarding the requirements of CSR disclosure in IBI, there are two main types of disclosure requirements described under CSR activities in all businesses' financial statements and annual reports. One requirement relates to the Sharia compliant items, such as *Zakah* and the *Qard Hassan*. The other concerns the universal requirements of CSR activities, such as charitable activities, employee welfare, and internal environment preservation policies.

CSR disclosure in IBI is mandatory, as the companies' social responsibilities are required by Sharia. For example, the disclosure of *Zakah* and provenance loans (*Qard Hassan*) are required by Sharia law to ensure that the individuals as well as the entity (Islamic bank) fulfil their responsibilities toward society (*Umma*), as this is an Islamic duty. The difference appears in how much detail and how many items an Islamic bank can disclose about its CSR over the course of the year. Sharia provides broad guidelines for *Zakah*, for example, which is an Islamic obligation that must be disclosed as part of banks' activity, but may not guarantee the full and appropriate disclosure of *Zakah*. The accounting standards adopted by Islamic banks can actually mandate the minimum requirements for disclosure, as is the case in the standards issued by the IFSB. The IFSB issued two standards for reporting CSR in countries adopting IFRS to record Sharia financial transactions, including IFRB 3 and IFSB 10. AAOIFI also issued FAS N^o.7 for reporting and disclosing CSR activities in Islamic banks using AAOIFI FAS when reporting Sharia financial transactions. AAOIFI (2010) defines CSR as "all activities carried out by an IFI to fulfil its religious, economic, legal, ethical and discretionary accountabilities as financial intermediaries for individuals and institutions".

Usually, the adoption of one set of accounting standards in a country's IBI is followed by the issue of other standards and guidelines or frameworks in order to highlight any misconceptions in the financial reporting tasks. For instance, the adoption of IFRS in Malaysia was closely followed by the issue of IFSB2 – 25 standards, guiding principles, and technical notes for the Islamic financial services industry (IFSB, 2016). According to the IFSB 4, titled “Disclosure to promote transparency and market discipline for institutions offering Islamic financial services”, Islamic banks report their Sharia compliant financial transactions in addition to the international CSR items. The following items relate to the Sharia governance practices in the Islamic banks:

- The system employed by the IIFS to insure Sharia compliance.
- How Sharia non-compliant earnings and expenditure occur and how they are disposed of.
- Statement clarifies if Sharia compliance is mandatory or not.
- The nature, size and number of Sharia compliant violations during the year.
- Annual *Zakah* contributions of IIFS.
- Remuneration of Sharia board members.

On the other hand, AAOIFI also issue further CSR standards in order to give more specific guidelines to Islamic banks on what to report regarding their CSR activities. FAS 7 includes the governance and CSR standards for Islamic banks following AAOIFI accounting standards (AAOIFI, 2010). Islamic banks are advised to report their activities in the following areas:

- *Zakah*
- *Qard Hassan*
- Late repayments and insolvent clients and avoiding onerous terms
- *Waqf* management
- Earnings and expenditure prohibited by Sharia

² <http://www.ifsb.org/background.php>

- Screening and informing clients for compliance with Islamic principles.

The discussion above leads to the suggestion that mandating financial reporting in IBI can be linked to increase or decrease in disclosure requirements for IBI across countries. Therefore, the following hypotheses are designed to examine this link in the IBI.

H8: Corporate Governance disclosures in Islamic banks are associated with the mandated accounting standards from the government.

H9: Corporate Social Responsibilities disclosures in Islamic banks are associated with the mandated accounting standards from the government.

4.7 Research Methods in Previous Islamic CG and CSR Literature.

With regard to the research methods used in previous literature, it is noticeable that the previous papers are either conceptual papers or papers using primary data through content analysis or disclosure index. Unlike this study, where secondary data are used from Islamic financial indicators (Zawya). For example Aribi & Arun (2014) they used 18 in-depth interviews in 9 IFIs in Bahrain, to investigate IFIs manager's perception on CSR. Siwar & Hossain (2009), used Open ended questionnaire to study of 50 listed companies in Malaysia in the purpose of examining the relationship between the concepts of Islam with the Malaysian managers' opinions where similarity in the opinions are found. Mohammed (2007), Interviewed a Sample of 6 Islamic banks from Malaysia, UAE, Saudi Arabia and UK, to explore notions of Islamic philosophy related to social responsibility and justice. He found that IB compliance to Sharia usually is socially responsible. Yahya (2005) used the weighted disclosure index to investigate the actual practice of CSR in IFIs and Only 102 companies from 194 sample companies disclose their social activities. Farook & Lanis (2005) used a disclosure index to measure CSR levels of 27 IFIs operating in 14 countries and ascertain the determinants of its disclosure. The results show a difference in disclosure levels within the sample, and it is suggested that a major source for the variation is the socio political context within which the IFIs operate. Anuar et al. (2004), used content analysis to examine the difference in environmental disclosure between Sharia-approved companies and non-Sharia-approved companies. The results provide some evidence that the Sharia-approved companies have a higher level of environmental reporting compared with non-Sharia-approved companies.

In terms of conceptual papers, there are four main papers for the corporate governance in general and CSR in particular. Summary of the papers and their contribution are added below. Haniff(2002) develop a conceptual framework based on the Sharia for Islamic social and environmental disclosure. The results suggest that the Islamic social responsibility to disclose practice should be different from conventional social reporting because of the different underlying principles. Kamla et al. (2006) paper elaborates and discusses the key Islamic principles and their implications to accounting for the environment. The paper concluded with many suggestions for accounting for the environment. Williams & Zinkin, (2009) conceptual paper looked at whether the tenet of Islam is consistent with the ‘Ten Principles’ of responsible business outlined in the UN Global Compact. The result shows that Islam often goes further and has the advantage of clearer codification of ethical standards, as well a set of explicit enforcement mechanism. Basah & Yusuf (2013) paper analyse the relationship of Islamic banks and CSR performance. They concluded that, the concept of Islamic banks that comply with religious provision should exhibit more proactive CSR activity and policies. Islamic banks’ performance should be superior to conventional bank counterpart.

4.8 Summary

This chapter discusses the literature and the hypotheses development of the two main objectives of the study. A) The determinants of accounting standards adoption in IBI and B) The consequences of adopting accounting standards in relation to disclosure practices in the Islamic industry.

In regard to the determinants literature, it discussed the two main approach appear in the literature to study the determinants as some researchers focus on the country level factors as determinants for the accounting standards adoption while others concentrated on the firm characteristics as possible determinants for accounting standards adoption. The hypotheses for the determinants were formed on the bases of the EDT and the literature discussed in the chapter. Seven hypotheses were formed, one of them external openness economy is related to the external environment in the studied countries. While the other six hypotheses are related to the internal environment in the countries including: economic growth, political stability, level of education, financial press and existence of sharia committee and Sharia governance

regulations in the countries. The chapter also highlight how adoption of accounting standards can be used to achieve important macro level objectives for the governments such as encouraging economic stability and foreign direct investment (Mueller, 1983).

In regard to the possible consequences of accounting standards adoption many papers are discussed in the literature review section with a special highlight to the review papers in this field (e.g. Ahmed et al., 2013; Brüggemann et al., 2013; Mohammadrezaei et al., 2013; Soderstrom & Sun, 2007; Pope & McLeay, 2011). Summarizing the review papers gave a clear idea about the shortages of investigating the consequences of accounting standards adoption in the developing countries in general and the none existence of investigating it the Islamic banking industry. Many consequences at both micro and macro level were highlighted for the adoption of accounting standards in general. However a special attention was given to the disclosure practices driven by the mandating different accounting standards a cross countries. The special attention to the disclosure practices was a result of the recent financial scandals in the last decade. The literature highlighted the link between the disclosure practices in the country and the accounting standards adopted. Particularly, it highlighted the importance role of accounting standards on the disclosure practices and the role of disclosure in many consequences at all levels. The literature also highlighted the shortages of any studies that investigate such link between the accounting adoption and the disclosure practices in Islamic banking industry. This shortage of such studies in IBI encourage to form a research to study the link between adoption of accounting standards and disclosure practices specially that Islamic banking industry have more duty to disclose more per the requirements of Sharia. After identifying the literatures gabs the challenge was to identify the right research methods to investigate the two objectives of the research. The next chapter is discussing in details the research methodology used to guide the research steps at a country level.

CHAPTER FIVE: RESEARCH METHODOLOGY

5.1 Overview

This chapter has two main sections: section 5.2, which discusses the philosophy, paradigm of enquiry, and the methodology of the study in detail. In addition, this section discusses the approach, the scope, and the triangulation, as well as why this study is approached at country level and not at bank level. Section 5.3 discusses all relevant information concerning data collection, sources, and sampling. In addition, this section discusses the definition and measurement of the dependent variables, explanatory variables, control variables, and the regression models used in the study.

5.2 Philosophy, Paradigm of Enquiry, and Methodology

This section includes a detailed discussion about the philosophy of the study as well as about the paradigm of enquiry, and a discussion about the study's methodology.

5.2.1 Post-Positivism

According to Howell (2013 p.43), post-positivism assumes that “social science should establish laws and as with the natural sciences such laws should be beyond challenge”. Popper (1994, cited in Howell, 2013) argues that theory should be open to criticism in order to test their validity, and verify and purify social science from inappropriate or ineffective theories. When generalisation cannot be verified, then it can be falsified. For example, Popper (2002) explains that no matter how many times you see a white swan, you cannot generalise that ‘all swans are white’. However, if one black swan is spotted, then we can safely state that ‘not all swans are white’. Therefore, Popper (2002) argues that if confirmation in social science is difficult, then verification is easier. It is worth to mention that, the falsification concept highlighted in this research is part of the research process only where the hypotheses are formed in a way to challenge the EDT in new environment which is the Islamic finance environment in different countries. However, falsification in Islamic Sharia is not included or intended to falsify any Sharia concept as it is not impossible in Islam. Islam is passed in Sharia which derived from Al Quran, and authentic Sunnah with Ijtihad (derived rule), Ijma’ (consensus) and qiyas (deductive analogy). Hence any Islamic concept

related to Sharia is not intended to be falsifying in this research as falsifying the sources of Sharia is not possible.

Howell (2013) highlights the ontology, epistemology, axiology and methodology most fitting to this paradigm. **Ontology**: reality may only be understood imperfectly and probabilistically, therefore it is encouraged to criticise existing reality. In other words, reality exists, but humanity is unable to fully understand it. **Epistemology**: abandonment of total separation of investigator and investigation; however, objectivity still can be pursued through falsification, which works as test for the validity of the theory. **Axiology**: research is value laden; the researcher is biased by world views, cultural experiences and upbringing. These will impact on the research. **Methodology**: multiple modified scientific experiments which pursues the falsification of hypotheses. May also include qualitative methods. Post-positivist theory is not about discovering immutable law as in the positivism perspective, but approximation of truth. It is also important that theory development is criticised through falsification to get rid of poor theories, otherwise objectivity will be undermined (Popper, 1994, cited in Howell, 2013).

5.2.2 Paradigm of Inquiry

The literature highlights that the journey of founding reality, knowledge and truth is a chain of many important elements: ontology, epistemology, objectivity and subjectivity, and embedded in each perspective and theory are the main components of this chain. In any research field, many researchers have preconceptions about all these elements before starting the investigation process. This perception regarding each element identifies the direction of each step in the research process, such as methodology, research approach and methods of data collection. These elements are the components of the paradigm of enquiry of the different philosophical perspectives, which are positivist and interpretive (Weber, 2004). However, in Howell (2013), they are named as positivism and phenomenological. According to Guba and Lincoln (2005), 'paradigm' is the basic set of beliefs that guide actions; a paradigm has four elements which help to guide the researcher in investigating a research topic. These elements are ontology, epistemology, axiology, and methodology. The characteristics of these elements and how they fit into research is discussed by authors such as Howell (2013), Denzin and Lincoln (2000) and Collis and Hussey (2009).

Typically, the researcher will identify the paradigm of inquiry to be used in their research based on the nature of research topic, or based on whether a certain paradigm is more acceptable to the supervisor or journal editor, or because it is the most commonly used paradigm in the research area (Collis & Hussey, 2009). The main difference between the two main paradigms of inquiry (empiricism and phenomenological) is in the way they perceive reality, which is considered the milestone in driving all research components such as methodology, methods and data collection. Empiricism is the stance that reality exists outside, and can be discovered and understood fully through positivism and partially through post-positivism. From the phenomenological viewpoint, reality exists within human thoughts. For this reason, a further inductive approach to social science research has been introduced where the researcher is an important part of their research plan. Thus, the phenomenological research type is more subjective than empiricism, which considers that the research process should be conducted without the involvement of the researcher. Empiricism has a higher degree of objectivity than phenomenological research.

This research aims to discover the cause and effect of accounting standards adoption on the reality of each country. Accounting standards adoption is a strategic decision in each country which, as highlighted in the literature, has many economic and non-economic consequences following such a decision. The philosophical base of this research topic is that reality is external, and can be discovered partially without the need for human interpretation. This understanding of reality suggests the use of the post-positivism paradigm of inquiry as it is assumed that reality cannot be understood fully, however it is possible to be understood partially (Howell, 2013). The use of this paradigm of inquiry to investigate the current research has also been determined as the studied topic involves cause and effect, which is usually associated with the post-positivism paradigm of inquiry.

To be able to form a research design for the research questions, it is very important to first present our perception of reality and then design a paradigm of inquiry to help in investigating the research question to obtain quality knowledge. A paradigm of inquiry, as written by Collis and Hussey (2009, p.55) is “a framework that guides how research should be conducted, based on people’s philosophies about the world and the nature of knowledge”. Following the post-positivism perspective in the investigation of this research question, the **ontology** of this perspective suggests that reality exists externally and can be understood only probabilistically, as humans cannot understand it fully (Howell, 2013). The **epistemology** of

this research perspective asserts that total separation between researcher and his/her investigated research is not possible, and certain degree of subjectivity therefore exists; **objectivity** can be pursued through falsification of the hypotheses, which results in research validation.

In terms of **axiology**, this research follows the post-positivism perspective whose aim is to explain the situation of the adoption without attempting to understand further, as this perspective assumes that research is value-free where the researcher is independent from the research under investigation. The research topics here are dealt with as objects that exist before the interests in them take place, so they existed prior to the research and they will continue to exist after the research has been completed (Collis & Hussey, 2009). Therefore, for the **methodology**, scientific methods are used in this research to discover the intended reality of the research questions, and secondary data are collected from various resources in order to answer those questions. The environmental factors are operationalised and appropriate measures are assigned to it, then causality is measured between the variables (Collis & Hussey, 2009). Understanding reality in this way gives the researcher a plan for how to design the research in terms of forming the hypotheses, choosing the methods, and collecting data. Detailed methodology and statistical methods are discussed in the following section.

On the other side the elements of paradigm of inquiry from Islamic perspective are varying differently, the ontology, and epistemology of Islam are discussed below as in (Asutay, 2012 and Mukhlisin, 2016).

The ontology in Islam is Sharia which establishes reality that leads humans to understand existence and purpose of life (Mukhlisin, 2016). To operationalize any ontological principles such as the existence of God or the Day of Judgment and the need to worship God an epistemology is required. The epistemology in Islam which can demonstrate how to worship God and how to fulfil the fundamental beliefs in Islam is (the objective of Islam) or *Maqasid al Shariah*. Maqasid al Sharia are defined as “human well-being” (Asutay, 2015).

Therefore, Maqasid al Sharia “operates how to fulfil Shariah and validate knowledge and deeds to fulfil Islamic principles” (Mukhlisin, 2016, p. 3). There are different views for Maqasid al Sharia coming from different scholars. The first discussion about Maqasid al Sharia came from scholars like Al-Ghazali, Ibn al-hajid and al Shatibi by defining the

primary needs for human (dharuriyyaht) which include, the safeguarding of five principles: 1) protection of religion (din) 2) protection of life (nafs) 3) protection of intellect (aql) 4) protection of wealth (mal) and 5) protection of lineage (ansab) (Chapra, 2008a & b, p. 5-6). The above discussed primary needs they work as the human as well as the countries road map to ensure long term economic development and welfare of people. As well as fulfilling the ontological aspects of Islam for example worshipping God and preparing for the day of judgments (Mukhlisin, 2016). Another view for Maqasid Al Sharia are discussed by Abu Zahrah, according to him there are three components for Maqasid Al Sharia: 1) educating the individual (tahzib al fard) 2) establishing justice (iqamat al adl) 3) ensuring welfare of society (jalb al Maslaha) (Abu Zahara, 1997, p. 365). Third view of Maqasid al Shariah is presented by Auda (2008) where he classified it into categories according to the context i.e economy, philosophy, politics and social. Therefore it divided into three levels: 1) General maqasid 2) specific maqasid and 3) partial maqasid.

In terms of methodology, usually researchers will use the elements of any view of maqasid al shariah and operationalised them into dimensions and elements that are out to exist in the financial reporting standards for the IFIs. Other researchers will use other broad principles such as that IFIs should operate under Islamic ethical values thus IFIs should disclose under Sharia standards and values on their financial reporting.

In this research, the purpose is not to evaluate the performance of the IFIs in terms of assessing the fulfilment of maqasid Al Sharia. However, this research has the aim of comparing between which accounting standard (AAOIFI or IFRS or local) is promoting more corporate disclosure and CSR disclosure. Assuming that all of the three accounting standards are complying with Shariah as AAOIFI organisation, IFSB for IFIs and local authorities confirms about their standards. Therefore, the methodology for the thesis is as stated in the section below in order to find the link between the adoption of each set of the accounting standards and the disclosure score in the country.

Content analysis is one of the methods which could be used to find out the disclosure score for each country included in the study by analysing the annual reports manually. However and hence there are 30 countries included in the study with different economies of scale and this need to be taken in consideration while calculating the disclosure score in addition to other country differences such as population, the number of IFIs, the inflation and the gross domestic product to give a comparable score at the end. the researcher prefer to use the

Thomson Reuters (Zawya) reports hence the calculation of the disclosure score for each country is taking in consideration all the country differences therefore the comparison is possible between countries adopting different set of accounting standards.

5.2.3 Methodology

The **methodology** suggested for the research topic is a **cross-sectional study**; hence, 30 countries were selected to allow comparison between the different causes and effects of using various accounting standards. In this paradigm of inquiry, a theory is tested and a framework is identified before data collection begins. Environmental determinism theory is used in this research as a framework to design hypotheses. This theory suggests the existence of internal and external environmental factors that can affect the accounting quality and regulations. The hypotheses formed are based on the internal environmental factors, which are educational, economic, political, and cultural, as well as external environmental factors such as the colonial history of the country and the openness of the economy. Since the analysis is conducted at country level, environmental factors such as culture, education, economy, and political systems related to each country are collected using secondary data available from reliable international sources such as the World Bank indicator database. This research focuses on one industry across 30 countries, namely the Islamic banking industry (IBI). There are three main accounting standards used in this industry: local standards, International Financial Reporting Standards (IFRS), and Accounting and Auditing of Islamic Financial Institutions (AAOIFI). The reliability of this research is very high as the same analysis will be carried out for countries using local standards, countries using AAOIFI and countries using IFRS. The role of researcher in the post-positivism research is not fully excluded; therefore, to ensure objectivity, falsification of the hypotheses will take place to overcome this weakness (Popper, 2002). Popper (2002) argues that while confirmation in social science is difficult, verification is easier. Falsification is considered in this research as it is a means to verify the theory, which either leads to its conformation or rejection – hence increasing the validity of the research (Howell, 2013). Howell (2013: p. 188) defines positivism research: “validity involves the extent to which measurement is accurate and what is supposed to be measured is actually being measured”. Validity is usually very low in the positivist approach, as it is very difficult to ensure that a test is truly measuring the phenomena under examination as expected. Nevertheless, the validity of positivist research can be increased through falsification (Popper, 2002). Falsification is included in this research through forming

hypotheses that test different powers other than environmental factors in itself only which influence accounting standards adoption in each country, such as external, internal powers and enforcement powers.

Considering that the post-positivism paradigm of inquiry has been adopted for this research process, the types of methodology applied to this research keep the characteristics of this paradigm. It is for this reason that the methodologies typically applied to the phenomenological paradigm of inquiry, such as critical theory, ethnography, and action research, were excluded from this research as the features of these methodologies do not usually support the adapted positivism paradigm. Another rationale for choosing cross-sectional methodology is the objective of the research, as discussed by Howell (2013), while a third rationale for applying this methodology is the literature surrounding the research objective (Collis & Hussey, 2009). The selection of the right statistical tool will help provide the necessary advantages in accomplishing the research with the highest objectivity and accuracy possible; thus, logistic regression was chosen for use in this research.

5.2.4 Cross-Sectional Studies

The methodology suggested for the research topic is cross-sectional study; hence, 30 countries have been selected to allow the comparison of the different causes and effects of using various accounting standards. Cross-sectional studies are often used to discover the economic characteristics of large numbers of organisations, people, or countries. This type of methodology is designed to investigate data collected from different contexts. Usually, the main purpose of cross-sectional studies is to find out similarities and differences between people, organisations, industries or countries. The main problem with this methodology is how to select enough samples to effectively represent the population. Another problem is how to idealise the phenomenon under investigation properly, and isolate it from any other variables which can affect the correlation. In addition, and as with all positivist methodologies, the result of the analysis usually tells us if the relationship exists or not, but it does not go any further in explaining the reasons for this (Howell, 2013). Despite these drawbacks, this methodology is inexpensive and can be easily repeated across different time periods.

5.2.5 Research Approach

There are two main approaches for research/reasoning: deductive and inductive. Robson (2002, cited in Saunders et al., 2007) lists five sequential stages through which deductive research will progress:

1. Deducing a hypothesis (a testable proposition about the relationship between two or more concept and variables) from the theory.
2. Expressing the hypothesis in operational terms, which proposes a relationship between two specific concepts or variables.
3. Testing this operational hypothesis.
4. Examining the specific outcome of the inquiry.
5. If necessary, modifying the theory in the light of the findings.

Inductive reasoning works the other way, moving from specific observation to broader generalisation and theories:

1. Informally sometimes called the 'bottom up' approach.
2. The emergence of the social sciences in 20th century led social science researchers to be wary of deduction.
3. Researchers adopting the inductive approach are more likely to work with qualitative data and use different methods to collect these data to establish different views of phenomena.

According to Creswell (2009), the most important criterion to decide which of the above two approaches is best, is the nature of the research topic. When a wealth of literature is available for a certain topic which the researcher can then put into a theoretical framework and develop a hypothesis, such a topic will take a deductive approach over inductive. Therefore, this research follows the deductive approach for these reasons.

The research design is to decide, in a logical way, what type of data should be used to answer the research question. This requires clarity about which data to use and how it should be analysed.

5.2.6 Research Scope

This research does not consider studying the effects of each standard or the role of each regulation. Instead, the research focuses on studying how using different accounting standards can affect disclosure regulation in each country.

The focus of this thesis is not to study the countries adopting accounting standards voluntarily, as they do not provide an indication of desirability for the regulations. In the consequences section, the study concentrates on the change to the disclosure score as a consequence of accounting standards adoption. Additional details about which countries are included in the study and why are discussed in the ‘sample selection’ section below.

5.2.7 Triangulation

During the research period, a visit to the AAOIFI organisation was arranged for and carried out in July 2015. The purpose of the visit was to try to collect some primary data by interviewing a number of key figures in the AAOIFI organisation, to gain confirmation of the data regarding which countries adopted AAOIFI mandatorily and voluntarily. Mr. Khaled Al-Sheikh, the accounting and finance consultant, agreed to be interviewed. Two basic questions were asked of Mr. Al-Sheik in the interview. Firstly, which countries have adopted AAOIFI on a mandatory or voluntary basis? Secondly, what are the determinants of adopting AAOIFI in IFIs? Unfortunately, Mr. Al-Sheik confirmed that AAOIFI does not keep any records of which countries adopt its standards for their IFIs. According to him, most countries adopt them voluntarily. He specified Bahrain as the only country he is aware of that mandated AAOIFI for IFIs. In regard to the second question about the determinants of adopting AAOIFI standards, there was no possible answer as a result of insufficient information about the first question. However, Mr. Al-Sheik provided many reasons as to why countries prefer not to use AAOIFI for their IFIs. This left the door open in terms of investigating the determinants of adopting AAOIFI standards, which could be a major contribution to research in this field. In addition, it is worth finding out which countries have adopted AAOIFI standards on a mandatory or voluntary basis. In another attempt to confirm the data regarding countries using AAOIFI, the researcher requested information about which countries have adopted AAOIFI standards – both mandatory and voluntary – from the Islamic banker

webpage³. The Islamic banker webpage is a professional site which includes many scholars from Islamic finance – some of whom are employed at AAOIFI. The answer to my question came from Mohammed Baker Iqbal, a cooperative development manager in AAOIFI. He stated that AAOIFI has been mandated in the countries listed in Table 2 (Bahrain, Jordan, Lebanon, Sudan, Qatar, and Oman). AAOIFI standards are also considered the base for other accounting standards adopted by countries such as Malaysia, Indonesia, the United Arab Emirates, and Kuwait.

5.2.8 Why a Country Level Study?

Mueller (1983) explains that firms will set their objectives towards the national objective of the country. However, countries lean more toward issuing national policies and then adopting administrative procedures to implement the policies. These policies, whether for firms or for countries, are not always clear; however, there is no doubt of their existence for the purpose of guiding organisations. Mueller emphasises that firms set very specific goals as they mainly focus on a small group of stakeholders, unlike nations. Therefore, he argues that “firm goals normally follow rather than lead economic policies” (Mueller, 1983, pp13-14). Mueller does admit that firm goals can have an effect on national policy, but as part of the public interest. Hence, this study prefers to investigate the determinants and consequences of adopting accounting standards in IBI at the country level instead of at bank level, initially. Another reason is highlighted by Wysocki (2011, p.309), who emphasises that “determinants and outcomes of both accounting institutions (including IFRS) and non-accounting institutions are fundamentally intertwined”. In other words, studying the determinants and outcomes of IFRS adoption can occur if taking into consideration other institutions in the country. This study takes place at country level in order to consider all other institutional factors while examining the determinants and outcomes of accounting standards adoption. To be more specific, Wysocki (2011, p.312) discusses that the “institutional view of accounting [...] emerges endogenously in an economy” therefore, the efficiency and quality of an accounting system in a country is influenced by many factors including “legal system, corporate governance mechanisms, and the existence and enforcement of laws governing investor protection and disclosure standards” (see also Kothari, 2000). Wysocki (2011) concludes that all the aforementioned institutions are interdependent, therefore this study takes all of these institutions into consideration. In addition, Wysocki (2011) discusses the challenges involved

³ <https://www.islamicbanker.com/>

in the methods used to identify the accounting or non-accounting institutions which affect the economy, and recommends several solutions for cross-country level studies. Other historical studies also emphasise the role of both accounting and auditing as an institution which helps to enforce contracts and collect debt, thus resulting in economic development (North, 1990; Watts & Zimmerman, 1983). These studies also highlight the importance of quantifying the effect at country level.

5.3 Data Collection, Sampling, and Variable Measurements

This section of the research methodology chapter concentrates on the data collection process, the dependent and independent variable details, as well as the measurements for all variables. This section also outlines the efforts made by the researcher in attempting to collect primary data to help in the research, and how this effort consequently changed the research from being based on primary data to secondary data research. This section also illustrates why the research takes place at the country level rather than at bank level. Finally, this section illustrates the models used in the research to answer the research questions.

For the purpose of investigating the determinants of AAOIFI, IFRS, and local standards adoption in Islamic banks, the sample is selected from the ‘Zawya’ website⁴. Zawya is one of the most reliable data sources available, as Thomson Reuters handles the databases for Islamic finance activities in the Middle East as well as other countries operating Islamic finance. The website offers numerous online services, as well as providing a wealth of information important to businessmen, professionals, governments and legal authorities. Zawya has also developed an annual development indicator for Islamic finance across countries. This indicator is used worldwide as measure for the development of Islamic finance in each country. This research uses the data available from the annual development indicator reports for Islamic finance as published by Zawya. The most important data are summarised from these reports and are used to test the hypotheses developed in this research.

Out of the total number of countries offering Islamic finance, only 54 countries operate Islamic banks/windows. Out of those 54 countries, the sample was restricted to 30 countries to allow comparison between determinants of adopting AAOIFI, IFRS and local standards by including the same number of countries in each group. The sample is divided as follows: 10

⁴ <http://www.zawya.com/islamic-finance-development-indicator/>

countries that have adopted AAOIFI, 10 countries that have adopted IFRS, and another 10 countries that have adopted local standards.

The biggest challenge in the research was when there is clear deviation from the law in a country. For example, some countries (e.g. Mauritania) have been excluded from the sample because the financial reporting law in the country demands IFIs report using one set of accounting standards, although most IFIs use different accounting standards. In another example, a country (e.g. Afghanistan) may issue their annual reports to comply with both IFRS and AAOIFI standards, which indicates that there is no mandated set of accounting standards in the country for IFIs. Such discrepancies, where the law regarding financial reporting differs to the accounting standards used in practice, highlight the weakness of the enforcement mechanisms in those countries and thus including such countries in the research may mislead the results as a whole. Some countries (e.g. Djibouti, Gambia, Ghana, Guinea, Uganda and Somalia, Kyrgyzstan) are excluded from the sample as there is no evidence of which accounting standards are being used in their Islamic banks, either because there are no electronic annual reports or the annual reports are in languages other than English or Arabic. Ethiopia was excluded from the sample as the main bank offering Islamic finance (ZamZam) ceased operations in Islamic finance in 2012.

The similarities between countries in each group after comparison to the other two groups are based on economic size. Gross domestic product (GDP) is used as a measure for economic size, as in Zeghal and Mhedhbi (2006).

Table 2: GDPPC (Gross Domestic Product Per Capita) for Sample Countries

Countries using AAOIFI	GDPPCG	Countries using IFRS	GDPPC G	Countries using Local Standards	GDPPCG
Bahrain	3.547	Albania	2.002	Bangladesh	4.835
Jordan	0.803	Bosnia and Herzegovina	1.405	Brunei Darussalam	3.813
Lebanon	0.803	Kenya	2.580	Egypt, Arab Rep.	-0.043
Mauritius	3.413	Kuwait		Indonesia	3.709
Oman		Malaysia	4.485	Iran, Islamic Rep.	0.172
Qatar	2.694	Nigeria	3.519	Iraq	-9.200
Sudan	0.892	Saudi Arabia	1.171	Maldives	5.665
Syrian Arab Republic		South Africa	-0.063	Yemen, Rep.	
Tunisia		Thailand	0.303	Pakistan	3.218
West Bank and Gaza	-4.370	United Arab Emirates	3.079	Turkey	1.617
Average GDPPCG	1.112		2.053		1.532

As discussed above, the countries in each category are chosen based on the GDPPC of each country. The first step was to identify the countries using AAOIFI, hence it turned out to be

the standard used the least among the three standards studied. The GDPPC of each country was then used to place the countries in each group. For example, the groups of countries using IFRS are identified based on their GDPPC and the countries with the closest GDPPC to the AAOIFI group were included in the IFRS group. The same technique was used to identify the countries to be included in the local standards group. The table shows that the countries in the IFRS group have higher GDPPC; however, the sample of countries included in the group is the ones with the least GDPPC. Another reason for the low GDPPC in the AAOIFI group is due to missing information for certain countries.

The purpose of this task was to group three sets of countries together whose economic size is similar to each other. As can be seen from the table, the countries using IFRS have the highest average GDPPC at 2.053. Unfortunately, the average could not be matched any further between the three groups. The sample size covers the adoption as of 2014. The data were collected for the studied variables for three years (2012, 2013, and 2014), as this type of country level data is only available from 2012 on the Zawya website.

Table 3: Sample Selection

Data	Number of Countries	Countries
N°. of countries using AAOIFI	10	Bahrain, Mauritius, Jordan, Lebanon, Oman, Qatar, Sudan, Syria, Palestine, Tunisia
N°. of countries using IFRS	10	Albania, Bosnia and Herzegovina, Kenya, Kuwait, Malaysia, Nigeria, Saudi Arabia, South Africa, Thailand, United Arab Emirates
N°. of countries using local standards	10	Bangladesh, Brunei Darussalam, Egypt, Indonesia, Iran, Iraq, Maldives, Yemen, Pakistan, Turkey
Total sample size of the study	30 countries	

Note: Additional details of the countries allowing Islamic finance worldwide are presented in Appendix D

The type of data being utilised in this study is panel wide and short, as the number of units (countries) are more than the time period (year). “Using panel data sets of this kind we can account for unobserved individual differences or heterogeneity” (Hill et al., 2012, p.538). The dataset being used in this study is considered panel data because the same number of countries is being studied across different years. The unit being included in the analysis does not change, and is being observed three times.

All the variables used in the analysis, along with their codes, definitions and sources are available in Table 4.

Table 4: Variables: Codes, Definitions and Data Sources

Variables	Code	Definition	Data Source(s)
Category 1	AAOIFI	Accounting and Auditing of Islamic financial Institutions accounting standards	AAOIFI org., Central bank of country, Annual reports of Islamic banks in the country
Category 2	IFRS	International Financial Reporting Standards	Central bank of country, Annual reports of Islamic banks in the country
Category 3	Local	Local Accounting Standards	Central bank of country, Annual reports of Islamic banks in the country
General Corporate Governance Disclosure Score	GCGDS	Score of disclosure related to general corporate governance in IFIs based on assessment through index designed by Zawya Co. Items of index in Appendix C	Islamic Finance Indicators
CSR Disclosure Score	CSRDS	Score of disclosure related to corporate social responsibilities in IFIs based on assessment through index designed by Zawya Co. Items of index in Appendix C	Islamic Finance Indicators
A) External Variables			
External Economic Openness	EEO	% of export to GDP + % of imports to GDP. It is measured annually at the country level.	World Bank's World Development Indicators Database
B) Internal Variables			
Stage of Economic Development	ECO	Growth Domestic Product per Capita in (\$). It is measured annually at the country level	World Bank's World Development Indicators Database
Political Systems	PS	Political Stability score measured between 2.5 and -2.5 in the world governance indicators.	World Bank's Worldwide Governance Indicators Database
Level of Education	LE	Number of Islamic institutions offering training in the country.	Islamic Finance Indicators
Financial Press	FP	Number of exclusive & regional Islamic finance news and articles.	Islamic Finance Indicators
C) Enforcement mechanism			
Sharia Gov. Reg.	SGR	Existence of Sharia Governance Regulation.	Islamic Finance Indicators
Judiciary	CSC	Existence of Centralised Sharia Committee	Islamic Finance Indicators

CHAPTER SIX: THE DETERMINANTS ANALYSIS AND FINDINGS

6.1 OVERVIEW

This chapter consists of two main sections which will present the analysis and the findings of the consequences objective in the thesis. The first section covers tables and illustrations for dependent and independent variables as well as discussion about the models applied. The second section will cover the statistical summaries, discussions around the correlation, multicollinearity, and the multinomial regression analysis for the determinants, and the marginal effect analysis.

6.2 VARIABLES AND MODELS FOR DETERMINANTS

This section is covering many topics for the determinants including: dependent variables, explanatory variables, The multinomial logit formulas and regression model for marginal effect.

6.2.1 Dependent Variables for Determinants

For the purpose of this study, three categories are used to represent each of the three accounting standards, which are represented by numerical values 1 to 3. Category 1 represents countries adopting AAOIFI standards in IBI, category 2 represents countries using IFRS in IBI, and category 3 represents countries that compile local accounting standards to use in IBI. The countries of each category, the selection criteria, and data sources are illustrated in Table 3, while the different category names and codes of the dependent variables are illustrated in Table 4. In the paper, the terms outcome 1, 2 and 3 are also used to represent categories 1, 2 and 3. Those two terms are used synonymously throughout the study.

6.2.2 Explanatory Variables for Determinants

The explanatory variables in Table 4 are classified into external, internal, and enforcement variables. Throughout the paper, the term ‘predictors’ is often used to describe the explanatory variables. Both terms – explanatory variables and predictors – are interchangeable.

This classification approach gives the variables explicit recognition in relation to the adoption process of accounting standards. The variables tested in this paper are based on EDT; whilst the measurement used for some variables is chosen to represent IFI in the country. For example, the level of education in a country is measured by the number of institutions in the country teaching Islamic finance courses. In addition, the financial press variable is measured by using the number of articles published about Islamic finance in each country. The other country level variables, such as political stability, economic development, and external economic openness, are measured at country level using the measurements and sources illustrated in Table 4. This study attempts to demonstrate that environmental factors are likely to influence accounting quality and accounting standards adoption, as have other studies (Arpan & Radebaugh, 1985; Belkaoui, 1983, 1985; Mueller, 1963; Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013).

In addition to the continuous explanatory variables suggested by EDT, this study has also included discrete variables related to the enforcement mechanism in each country. This is potentially related to the adoption of accounting standards in the country, since the IBI should be compliant with Sharia. These two variables are the existence of SGR and the existence of CSC. The data relating to these two variables were collected from Zawya. The role of enforcement mechanisms to improve accounting quality has been discussed in previous literature (Cooke & Wallace, 1990); however, the role of these two enforcement variables is being investigated for the first time in relation to the adoption of accounting standards in the IBI.

6.2.3 The Multinomial Logit Formulas

The model in this section is designed to test hypotheses H1, H2, H3, H4, H5, H6 and H7 to identify the possible determinants of accounting standards adoption in IBI. This model was designed according to the suggested literature of testing the determinants of IFRS adoption in different countries. However, previous studies used binary logistic to test the determinants of adoption against non-adoption, while this model is for MNL to test the determinants of countries adopting either AAOIFI, IFRS, or local accounting standards in IBI in different countries.

In this model, we assume that there are Y possible outcomes in the data. The dependent variables of Y can take J values; for example, 1, 2,..... J-1. In this study, we are modelling

different types of accounting standards used in the Islamic banking industry, AAOIFI, IFRS and local standards which means we have J=3. The numbering goes arbitrarily with the categories, which means it does not go in order. This can be summarised as follows:

Y=1 if countries adopt AAOIFI, Y=2 if countries adopt IFRS, and Y=3 if countries adopt local.

The simple logistic model has the following form:

Equation 1: $\text{Log}(Y) = \text{natural log (odds)} = \ln \left[\frac{P_i}{1-P_i} \right] = \alpha_0 + \beta X_i$

Taking the antilog of Equation 1 on both sides, one derives an equation to predict the probability of the occurrence of the outcome of interest, as follows:

Equation 2: $P = \text{Probability (Y = outcome of interest | X = x)}$,

$$a \text{ specific value of } x = \frac{e^{\alpha + \beta x}}{1 + e^{\alpha + \beta x}}$$

According to Equation 1, the relationship between logit (Y) and X is linear. Yet, according to Equation 2, the relationship between the probability of Y and X is nonlinear. For this reason, the natural log transformation of the odds in Equation 1 is necessary to make the relationship between a categorical outcome variable and its predictor(s) linear. Extending the logic of the simple logistic regression to multiple predictors, one can construct a complex logistic regression for Y such as ‘AAOIFI accounting standard adoption’, as follows:

Model 1: Equation 3: $\text{LOG}(Y_i) = \ln \left[\frac{P_i}{1-P_i} \right] = \alpha_0 + \beta_1 EEO_i + \beta_2 ECO_i + \beta_3 PS_i + \beta_4 LE_i + \beta_5 FP_i + \beta_6 SGR_i + \beta_7 CSC_i + \varepsilon_i$

Equation 4: $P = \text{Probability (Y = outcome of interest | X = x)}$,

$$a \text{ specific value of } x = \frac{e^{\alpha + \beta_1 x_1 + \dots + \beta_j x_j}}{1 + e^{\alpha + \beta_1 x_1 + \dots + \beta_j x_j}}$$

Where:

P is the probability of the outcome of interest (Y) such as AAOIFI accounting standard, α_0 is the y intercept, β is the regression coefficient, and $e = 2.71828$ is the base of the system of natural logarithms. X are the set of the predictors can be categorical or continuous, but Y is always categorical, ε is the error term.

The empirical analysis in this study examines the determinants of adopting AAOIFI and IFRS in IBI compared to local standards. There are numerous studies which have investigated

the determinants of adopting IAS using Binary Logistics Regression (BLR) (Dumontier & Raffournier, 1998; Leuz & Verrecchia, 2001; Tarca, 2004; Trembley, 1989; Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). BLR is limited to examining the determinants of adopting one particular set of accounting standards in comparison to not adopting it. However, in this study, MNL is used for three reasons. Firstly, it enables a broader scope for comparison between countries adopting different accounting standards, for example comparing countries adopting the AAOIFI accounting standards with countries adopting other standards such as IFRS and local standards. Secondly, it enables analysis of the determinants of adopting more than one standard using the same sample in one statistical operation. Finally, a statistical feature for MNL is that “it assumes the data are case specific, meaning that each independent variable has one value for each individual” (Long & Freese, 2014, p.385). The only drawback of MNL is the complexity of interpreting the results, which is predominantly caused by the nonlinearity of the model.

This model is different to other models in previous studies as it, for the first time, is designed to be used to test the determinants of accounting standards adoption; previous studies use binary regression, hence there were two choices in the model adoption versus non adoption (e.g. Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). This model differs to the previous models as it considers examining the determinants of adopting AAOIFI, IFRS, and local standards within the same model. In addition, compared to previous studies, this model introduces Sharia enforcement mechanisms as a possible determinant for accounting standards adoption in IBI. No other studies consider this in the literature. Another new variable in the model is financial press, as no other studies consider the media as possible determinants of accounting standards adoption.

6.2.4 Regression Model for Marginal Effect

The marginal effect can be simply described as changes in probabilities. It measures the change in the probability of an outcome for a change in x_k , holding all other independent variables constant at specific values. The marginal effect of any variable actually depends on the specific value of all independent variables.

There are three approaches for the marginal effect calculation: first, marginal effect at mean (MEM) – in this approach, the marginal effect of x_k is calculated with all variables held at their mean. The second approach is the marginal effect at representative values (MER),

where the marginal effect of x_k is computed with variables held at specific values that are selected to answer the research question being considered. The MEM is one example of the MER. The third approach of the marginal effect is the average marginal effect (AME), where the marginal effect for each observation (x_k) is computed at its observed values (x_i) and then the average of these effects is computed.

The marginal effect approach used in this research is the AME, where the dy/dx option is used to calculate the marginal effect. The dy/dx option indicates that changes for all independent variables are to be computed. Using this option for the marginal effect can help calculate the amount of change in a regressor if the variable is a continuous variable or a discrete (factor/ dummy) variable. For a continuous variable, “margins estimates the marginal change, which is the partial derivative or instantaneous rate change in the estimated quantity with respect to a given variable, holding other variables constant” (Long & Freese, 2014, p.163). For factor variables, “margins calculates the discrete change, which is the difference in the prediction when the factor variable is 1 compared with the prediction when the variable is 0” (Long & Freese, 2014, p.163). In terms of category variables such as age, “the change is from the base category to the value listed in column dy/dx ”.

The purpose of this model is to test the similarity of the environmental variables that can determine the adoption of accounting standards in IBI independently. This model will allow investigation of the determinants for each group of countries adopting AAOIFI, IFRS or local standards – but not in relation to any other group, unlike MNL analysis.

Model 2:
$$\frac{\Delta \Pr(y_i=1/x_i)}{\Delta x_k} = \frac{1}{N} \sum_{i=1}^N \frac{\Delta \Pr(y_i=1/x_i)}{\Delta x_k}$$

Long and Freese (2014) explain that this formula for the marginal effect calculates the average marginal effect, as “it computes the marginal effect of x_k for each observation at its observed values x_i , and then computes the average of these effects” (p.242).

6.3 Findings and Discussion of Determinants

6.3.1 Descriptive Analysis

Table 5 shows the descriptive statistics of the independent variables. Panel A displays the descriptive statistics of the continuous variables in the model. They include external economic openness, stage of economic development, political system, level of education, and financial press. Panel B presents the frequencies of discrete variables.

Table 5: Sample Descriptive Statistics for Continuous Variables

Panel A: Descriptive Statistics for Continuous Variables						
Adoption	Variable	N	Mean	SD	min	max
AAOIFI	EEO	20	96.4432	35.5026	21.65651	133.5484
	PS	30	-0.86166	1.299965	-2.75742	1.210541
	ECO	25	1.32352	3.927479	-7.09576	11.08503
	LE	30	6.6	5.727128	0	21
	FP	30	306.8333	405.0693	0	1609
IFRS	EEO	28	98.88012	46.68173	30.2	185.5995
	PS	30	-0.39448	0.840843	-2.10576	0.8922639
	ECO	29	1.935306	1.838666	-3.43745	6.076476
	LE	30	14.13333	21.99174	0	99
	FP	30	783.1333	1168.991	13	4216
LOCAL	EEO	25	83.19413	56.82001	31.16821	219.2552
	PS	30	-0.99125	1.066748	-2.68628	1.267537
	ECO	30	1.841595	3.928445	-9.20013	9.281366
	LE	30	6.3	7.134907	0	24
	FP	30	292.8667	444.6324	30	2447
TOTAL	EEO	73	92.84055	47.70829	21.65651	219.2552
	PS	90	-0.74913	1.103738	-2.75742	1.267537
	ECO	84	1.719759	3.325924	-9.20013	11.08503
	LE	90	9.011111	14.07643	0	99
	FP	90	460.9444	784.6522	0	4216
Panel B: Descriptive Statistics for Discrete Variables						
	Dummies	0 (%)	1 (%)			
AAOIFI	SGR	15 (50%)	15 (50%)			
	CSC	24 (80%)	6 (20%)			
IFRS	SGR	18 (60%)	12 (40%)			
	CSC	21 (70%)	9 (30%)			
LOCAL	SGR	18 (60%)	12 (40%)			
	CSC	18 (60%)	12 (40%)			
<i>Table 4 for Variables' Codes, Definitions and Data Sources</i>						
General Corporate Governance Disclosure Score (GCGDS), CSR Disclosure Score (CSRDS), External Economic Openness (EEO), Stage of Economic Development (ECO), Political Systems (PS), Level of Education (LE), Financial Press (FP), Sharia Governance Regulation (SGR), Centralised Sharia Committee (CSC).						

As can be seen from Panel A, a variation in the mean, a minimum, and a maximum value exists across all of the continuous explanatory variables. The External Economic Openness (EEO) variable's means for AAOIFI, IFRS, and local standards for country categories 1, 2, and 3 are 96.44m, 98.88m, and 83.19m, respectively. The mean of this variable indicates that the countries which adopt IFRS are more open to external economies compared to countries adopting AAOIFI or local standards. The mean also indicates that countries using local standards have less EEO compared to the countries using AAOIFI and IFRS.

The Political Stability (PS) variable has a negative mean in all three groups, where for category 1, 2, and 3 the mean is -0.86, -0.39, and -0.99, respectively. The mean results indicate that countries adopting IFRS are more politically stable than countries in the other two categories.

The Economic Growth (ECO) variable's means for categories 1, 2, and 3 are 1.32, 1.93, and 1.84, respectively. From these results, it is clear that countries adopting IFRS and local standards experience more economic growth than countries adopting AAOIFI.

The Level of Education (LE) variable's means in the three categories are 6.6, 14.12, and 6.3 for countries adopting AAOIFI, IFRS, and local standards, respectively. A conclusion can be drawn from the mean of the LE variable, which is that countries adopting IFRS have almost twice the number of institutions that offer Islamic finance courses when compared to countries adopting AAOIFI or local standards.

The Financial Press (FP) variable has the most variation amongst the independent variables; the minimum value in the FP variable is 0, which is in the AAOIFI category, whilst the maximum value is 4216, which is in the IFRS category. The mean of FP for the three categories are 306.83, 783.13, and 292.86 for AAOIFI, IFRS, and local standards, respectively. The mean figures indicate that the AAOIFI category has the least number of Islamic finance-related news articles per year. In contrast, the IFRS category has the highest number of articles per year.

Panel B illustrates the descriptive statistics of the discrete variables, where: a value of '1' indicates the existence of either governance regulations or the existence of a centralised Sharia committee in the country; whilst a value of '0' indicates an absence of both. The results show an interesting variation between the two variables, as it would be reasonable to expect either the existence of both or neither within a country. However, the existence of Sharia governance regulations does not necessarily mean that there will be a centralised Sharia committee in the same country. For example, as shown in Panel B, there are two countries adopting AAOIFI which only have a centralised Sharia committee, without Sharia governance regulations. In the categories where countries adopt IFRS or local standards, there are four countries from each group which have a centralised Sharia committee without Sharia governance regulations. The variation of the variables proves that the environment of different countries can differ significantly. Therefore, the different accounting standards used in those countries could be related to the different environmental variables.

Table 6: Correlation Matrix

Variables	Adoption	EEO	PS	ECO	LE	FP	SGR	CSC
Adoption	1							
EEO	-0.1158	1						
PS	-0.0482	0.5912** *	1					
ECO	0.0605	0.0374	-0.0124	1				
LE	-0.0087	0.2557**	0.1394	0.1588	1			
FP	-0.0073	0.2745**	0.2359**	0.1552	0.7337** *	1		
SGR	-0.0824	0.1535	0.1826	0.2216**	0.3597** *	0.3587** *	1	
CSC	0.1782	-0.0859	0.0803	0.223**	0.5191** *	0.4431** *	0.6018** *	1

Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)
 Variables definitions and measurements are the same as summarised in Table 2
 , * and * indicate significance at .1, .05, and .01 respectively

6.3.2 Correlation

A correlation matrix of the variables for the MNL model is given in Table 6. An examination of the partial correlations generally indicates weak correlations across the all of the variables. This suggests that each explanatory variable provides unique information, which will be discussed in more detail during the multivariate analysis. According to Gujarati and Porter (2009), strong correlation between pairs of variables may cause problems with multicollinearity. Thus, the Variance Inflation Factor (VIF) was calculated after running the logistic regression to check for the multicollinearity problem, as this can affect the reliability of the estimates (Acock, 2008). According to Field (2009), multicollinearity exists if the VIF value is greater than 10. The results from this study have zero VIF values above 10, which alleviates any concerns regarding the presence of the multicollinearity problem. The average value for the VIF is 1.67, with the highest and lowest values being 2.44 and 1.06, respectively.

Furthermore, as shown in Tables 7 and 8, the standard error for all variables are less than 2, which also indicates that multicollinearity is absent from the model.

6.3.3 Multinomial Logistic Analysis

Tables 7 and 8 show the MNL analysis results for the AAOIFI, IFRS, and local standards. The probability of the model chi-square of 30.74 is 0.0060, less than or equal to the level of significance of 0.05. The null hypothesis that there would be no difference between the model with independent variables and the model without independent variables was rejected. The existence of a relationship between the independent and dependent variables was supported. The log likelihood has increased from -79.515 to -65.48, which indicates an overall goodness of fit for the model. The pseudo R^2 value is 0.1765; since the MNL does not have an R^2 as in the ordinary least square regression, other measures have been introduced as a replacement such as the pseudo R^2 . Even though the proportion of variance for the response variables is not measured exactly, they still explain how much the predictors can add value to the model (Institute for Digital Research and Education, 2016). In general, they are used as an equivalent to R^2 to indicate the goodness of fit of the model. The reported pseudo R^2 value of 0.1765 does not indicate any problems with the model, and thus there is no concern about the overall fit of the model. The log likelihood test performs the same role as the F-test of R^2 and tests whether the explanatory variables *as a whole* explain Y.

The difference in MNL regression is that there are multiple interpretations for an independent variable in relation to different pairs of groups. In this study, the AAOIFI and IFRS categories were set as the base category interchangeably in the regression. This allows the reporting of the determinants, using each accounting standard as a comparison to the other two standards. The results of the MNL are shown in Table 7 for AAOIFI and Table 8 for IFRS. Local standard adoption determinants in comparison to AAOIFI and IFRS can be ascertained from both tables.

Both Tables 7 and 8 report the coefficient of the predictors, the Relative Risk Ratio (RRR), and the p values for both. For the MNL, the coefficient, or the parameter estimate, is calculated relative to the referent group. This means that a unit change in the predictors equates to a change in the outcome by the value of the coefficient relative to the referent group. However, it is always recommended to use the RRR or the odd ratio to explain the effect of the unit change of the predictors, instead of the coefficient. Hence, the relationship

between the probability of Y and X is nonlinear for the coefficient of the MNL. Long and Freese (2014, p.136) explain that “in nonlinear models, the effect of a change in a variable depends on the values of all variables in the model and is no longer simply equal to a parameter of the model”. For this study, the odd ratio is the same as the RRR; therefore, the RRR is reported in Tables 7 and 8 to demonstrate how the change in predictor X is affecting the outcome Y.

Table 7: Multinomial Log Analysis for Countries Adopting AAOIFI

Countries using AAOIFI in comparison with countries using IFRS								Countries using AAOIFI in comparison with countries using local standards					
Variables	Pred. Sign	Coef.	RRR/ ODD (β^e)	RR%	Std. Err.	z	p-value	Coef.	RRR/ODD (β^e)	RR%	Std. Err.	z	p-value
Const.	+/-	-1.094	0.335	66.5	1.095	-1	0.318	0.539	1.714	-71.4	1.119	0.48	0.63
EEO	+/-	0.010	1.010	-1	0.010	1.06	0.289	0.000	1.000	0	0.009	-0.04	0.967
ECO	+/-	-0.115	0.892	10.8	0.136	-0.84	0.399	-0.189	0.828	17.2	0.160	-1.18	0.239
PS	+/-	-0.692	0.500	50	0.449	-1.54	0.123	0.011	1.011	-1.1	0.407	0.03	0.978
LE	+/-	0.005	1.005	-0.5	0.060	0.09	0.929	0.082	1.086	-8.6	0.061	1.35	0.176
FP	+/-	-0.003	0.997	0.3	0.002	-1.81	0.07*	-0.003	0.997	0.3	0.002	-1.52	0.129
SGR	+/-	0.886	2.425	-142.5	1.118	0.79	0.428	0.818	2.266	-126.6	0.803	1.02	0.308
CSC	+/-	0.599	1.821	-82.1	1.371	0.44	0.662	-1.876	0.153	84.7	1.028	-1.82	0.068*
Likelihood ratio test: chi-square (14)					30.74								
Prop > chi-square					0.0060***								
Pseudo R²					0.1765								
Number of Obs.					73								
Log-Likelihood at zero					-79.515								
Log-Likelihood at convergence					-65.483								
Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)													
Variables definitions and measurements are the same as summarised in Table 4													
*, ** and *** indicate significance at .1, .05, and .01 respectively													
Formula used to calculate the RR% is: $RRR(I) = (1 - RR) \times 100$													

6.3.4 Determinants of using AAOIFI in Comparison to IFRS and Local Standards

The RRR in the MNL can be obtained by e^{coef} . To interpret the RRR, the following rules were used: $RRR > 1$ shows that there is an increased risk of the outcome; $RRR = 1$ shows that there is zero risk of the outcome; and $RRR < 1$ shows that there is a reduced risk of the outcome (Institute for Digital Research and Education, 2016). The standard interpretation for the RRR is: for a unit change in the predictor variable, the output is more/less likely to be affected by the RRR relative to the referent group taken into consideration, if other variables in the model are held constant. In addition to describing the outcome change using the RRR factor, translating the ratio (e^{coef}) to a percentage can make it easier to interpret the amount of change in the outcome relevant to one unit increase in a predictor. Therefore, Tables 5 and 6 include the Relative Risk percentages (RR%) for the RRR to make it easier to interpret the results. Using the data available in Tables 5 and 6, it is possible to discuss the results of the MNL in terms of how much one unit increase in the predictors are affecting outcomes 1, 2, and 3 in relation to the referent group.

For countries adopting AAOIFI standards compared to countries using IFRS standards, it is clear from Table 6 that one unit increase in EEO has -1% relative risk. The RRR is not significant at any level; thus, it is reasonable to suggest that if any country increased its EEO by one unit, this increase has 0% relative risk in changing from countries using AAOIFI to countries using IFRS. This also suggests that the increase in EEO has minimal effect as to whether a country adopts AAOIFI over IFRS, if other variables in the model are kept constant. The RR% of other predictors with no level of significance in the model analyse determinants of AAOIFI compared to IFRS, such as ECO, PS, LE, SGR and CSC, vary from 50 to -42.5. However, the p value for these predictors' RRR are not significant at any level, which suggests that the change in these predictors does not trigger any risk of a country changing their accounting standards from AAOIFI to IFRS.

Among the seven predictors examined in the model to find out the determinants of adopting AAOIFI standards compared to IFRS standards, only one had a significant value. The FP variable has a p value of 0.07, indicating that the financial press in countries adopting AAOIFI can be an important predictor in the model when compared to countries which adopt IFRS. However, the FP RRR is almost 1, which indicates that one unit increase in the FP variable is not associated with any risk of changing the output. This implies that the financial

press can be an important predictor in the model. However, the relative risk of changing the output of the model is minimal, which is indicated by the RR% of 0.3%.

In Comparison with Local Standards

When comparing countries adopting AAOIFI standards to countries adopting local standards, it is clear from Table 5 that the only predictor which indicates a significant RRR is the CSC. Hence, the RRR in this predictor is statistically significant at the 10% level of significance, with a p value of 0.068. The RR% is 84.7%, which indicates that this predictor can affect the adoption of AAOIFI standards when compared to local standards. In other words, this result suggests that the existence of a centralised Sharia committee will decrease the relative risk for a country adopting AAOIFI standards by a factor of 0.153, or 84%. This implies that if any country introduces a centralised Sharia committee, it is more likely to be using local standards as opposed to AAOIFI. This result is consistent with EDT theory, which states that enforcement mechanisms can be a predictor for accounting quality, and therefore hypothesis H7 is accepted.

On the other hand, the RRR of EEO, ECO, PS, LE, FP, and SGR are not statistically significant, which indicates that a change in these predictors are not likely to affect the adoption of AAOIFI standards when compared to local standards.

6.3.5 Determinants of using IFRS in Comparison to AAOIFI and Local Standards

The IFRS MNL results compared to those of AAOIFI and local standards are presented in Table 8. The chi square of the model is 30.74, the p value = 0.006, and the pseudo R^2 is 0.1765. The results of the MNL are the same as in Table 5 as the same variables were tested. However, the results in Table 6 refer to AAOIFI in Panel A and to local standards in Panel B. The RRR, the RR%, and the p value for IFRS adoption are given in both Panel A and Panel B to distinguish between IFRS, AAOIFI, and IFRS compared to local standards.

Table 8: Multinomial Log Analysis for Countries using IFRS

Countries using IFRS adoption in comparison with AAOIFI								Countries using IFRS adoption in comparison with Local					
Variables	Pred · Sign	Coef.	RRR/ODD (β°)	RR%	Std. Err.	z	p-value	Coef.	RRR/OD D (β°)	RR%	Std. Err.	z	p-value
Const.	+/-	1.094	2.896	-189.6	1.095	1	0.318	1.633	5.117	-411.7	1.148	1.42	0.155
EEO	+/-	-0.010	0.990	1	0.010	-1.06	0.289	-0.011	0.989	1.1	0.011	-0.99	0.322
ECO	+/-	0.115	1.122	-12.2	0.136	0.84	0.399	-0.074	0.929	7.1	0.104	-0.71	0.477
PS	+/-	0.692	1.999	-99.9	0.449	1.54	0.123	0.704	2.021	-102.1	0.381	1.85	0.065*
LE	+/-	-0.005	0.995	0.5	0.060	-0.09	0.929	0.077	1.080	-8	0.045	1.7	0.089*
FP	+/-	0.003	1.003	-0.3	0.002	1.81	0.07*	0.000	1.000	0	0.000	1.03	0.303
SGR	+/-	-0.886	0.412	58.8	1.118	-0.79	0.428	-0.068	0.934	6.6	0.987	-0.07	0.945
CSC	+/-	-0.599	0.549	45.1	1.371	-0.44	0.662	-2.475	0.084	91.6	1.153	-2.15	0.032***
Likelihood ratio test: chi-square (14)					30.74								
Prop > chi-square					0.0060***								
Pseudo R2					0.1765								
Number of Obs.					73								
Log Likelihood at zero					-79.515								
Log Likelihood at convergence					-65.483								
Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)													
Variables definitions and measurements are the same as summarised in Table 4													
*,** and *** indicate significance at .1, .05, and .01 respectively													
Formula used to calculate the RR% is: $RRR (I) = (1 - RR) \times 100$													

As can be seen from Table 8, Panel A represents the RRR for the category of countries which have adopted IFRS compared to AAOIFI. The results in Table 8 show that financial press can be more of an important predictor for IFRS adoption than for AAOIFI adoption, which was also shown to be true in Table 6. However, the RRR value is 1.003 and the RR% is 0.3%, which suggests that the relative risk of increasing FP by a unit has almost zero influence on changing the accounting standards adoption from IFRS to AAOIFI.

Panel B of Table 8 presents the RRR and RR% for countries adopting IFRS compared to local standards. There are three predictors with an RRR being statistically significant; these three predictors are PS, LE, and CSC. The PS and LE are statistically significant at the 10% level, while the CSC is statistically significant at 1%.

Table 8 shows the first set of results where the PS predictor has significant values, with an RRR of 2.021 and RR% of 102.21% at a 10% level of significance. The PS predictor has the highest RRR out of all of the predictors in the model. This suggests that the political stability of a country is a very influential predictor in the determinants of adopting IFRS standards. It also suggests that one unit increase in the PS is more likely to increase the relative risk of the country adopting IFRS instead of local standards by 102.21%. This implies that countries with a more stable political environment are more likely to adopt IFRS than developing local standards for the IBI. This result is consistent with EDT, and therefore hypothesis H3 is accepted.

A single unit increase in LE for countries adopting IFRS standards compared to countries using local standards will lead to an increase in the relative risk for countries in the IFRS category by a factor of 1.08, or 8%. This means that an increase in LE is more likely to increase the probability of using IFRS compared to local standards. This result is consistent with EDT, and therefore hypothesis H4 is accepted. This result is also consistent with previous literature, as the level of education is found to be one of the environmental factors affecting the accounting standards adoption for IAS (Dumontier & Raffournier, 1998; Tarca, 2004; Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013).

From Table 8, the other predictor which shows significance in the model is the CSC. The CSC predictors' RRR is 0.084 at the 5% level of significance. The existence of a centralised Sharia committee is more likely to decrease the relative risk of countries adopting IFRS compared to local standards by a factor of 0.084, or 91.6%. This indicates that the existence

of a centralised Sharia committee decreases the probability of adopting IFRS compared to local standards. This result is consistent with EDT, in that enforcement mechanisms can affect the accounting quality in the country, and that this influence can extend to accounting standards adoption.

The effects of the existence of a CSC had not been investigated before in the existing literature as an enforcement mechanism for IFRS adoption determinants. However, other enforcement mechanisms, such as the existence of capital markets (Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013) and governance variables (Delcours & Huff, 2015) in the country, were examined as accounting standard adoption determinants and were found to be associated.

6.4 Additional Analysis: Marginal Effects

From the data presented in Tables 7 and 8, it is possible to interpret the possible association of the explanatory variables of adoption. The RRR values, explained in the section above, show how one unit increase in the predictor is related to the outcome compared to the referred group, whilst all other variables are constant. However, the impact direction and magnitude of each predictor on the probability of adopting each accounting standard without being compared to any other group requires calculating the marginal effect (Long & Freese, 2014). The marginal effect is defined as the derivative of the probabilities that have substantive behavioural meaning (Louviere et al., 2000). For continuous variables, marginal effects actually measure the influence of one unit change in the explanatory variable has on the probability of selecting each outcome. For discrete variables (0, 1), margins calculate the discrete change, which is the difference in the prediction when the variable is 1 in comparison with the prediction when the variable is 0 (Long & Freese, 2014). The marginal effects are shown for each outcome, allowing the verification of the results reported in Tables 7 and 8. In addition, it is also possible to identify the main predictor for each outcome. Furthermore, it is also possible to compare how each predictor can influence each outcome positively or negatively.

The margin commands in STATA are just like the regression commands, as they compute the estimates as well as variance. The results of the margins for this study are presented in Table 9.

Table 9: Marginal Effects for Significant Covariates in Multinomial Logit Model

Variables	Prob (Y=1) (z-values)	Prob (Y=2) (z-values)	Prob (Y=3) (z-values)
EEO	0.000808 (0.63)	-0.0018731 (-1.19)	0.0010651 (0.68)
ECO	-0.025913 (-1.21)	0.0021989 (0.14)	0.0237141 (1.22)
PS	-0.0560448 (-0.91)	0.1258142 (2.21)***	-0.0697694 (-1.18)
LE	0.0076269 (0.86)	0.0070947 (0.97)	-0.0147216 (-1.9)*
FP	-0.0005031 (-1.79)*	0.0003095 (2.06) ***	0.0001935 (1.15)
1. SGR	0.1468496 (1)	-0.0809857(-0.49)	-0.0658639 (-0.54)
1.CSC	-0.1471992 (-1.12)	-0.2716354 (-1.98)**	0.4188346 (3.18)*

Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)
 Variables definitions and measurements are the same as summarised in Table 4
 *, ** and *** indicate significance at .1, .05, and .01 respectively

It should be noted that the marginal effect for each predictor on the different outcomes add up to zero. For example, the CSC marginal effect for outcomes 1, 2, and 3 are -0.1471992, -0.2716354, and 0.4188346, respectively, which total zero. This illustrates how margins give ranks to the probabilities of selecting one outcome over the other. For example, the CSC indicator for countries adopting local standards has the highest margin; therefore, the existence of a CSC in a country increases the probability of adopting local standards in IBI by 41.88%. The CSC margins of the other two outcomes are -14.72% for countries adopting AAOIFI, and -27.16% for countries adopting IFRS. It is very clear that the existence of a CSC has the biggest influence on adopting local standards as opposed to AAOIFI and IFRS. Negative values for the CSC margins for outcomes 1 and 2 supports this conclusion; hence, it indicates that the existence of a CSC is likely to have a negative influence on AAOIFI and IFRS adoption.

6.4.1 AAOIFI Standards Adoption

For countries adopting AAOIFI standards, it is clear from Table 9 that the predictor with the least statistically significant influence is FP. The margin is -0.0005, or 0.05%; therefore, a change in one unit in the FP predictor has minimal influence, even though the margin is statistically significant at the 10% level of significance. This result could be considered correct as long as the average number of news items per year were not taken into account. However, the significance of this predictor is in fact indicated when this average number is considered. This is because the mean value for FP in category 1 is 307, which means that the

impact on the outcome per year is equivalent to 15.3 times, which is considerable. The negative sign indicates that the increase in FP is more likely to affect AAOIFI adoption negatively. Therefore, the final result can be considered thusly: the negative impact of the one unit increase in FP per year can have a significant negative impact on AAOIFI adoption in a country. This result is consistent with EDT theory, and therefore H5 is accepted for Outcome 1. Zeff (2007) and Ball (2006) highlight the fact that newspapers and magazines in developed countries usually publish the financial performance of many companies and organisations. However, this is not the case in developing countries. In this research, FP is considered one of the awareness institutions that can affect the adoption process in a country. The association between FP and AAOIFI adoption also serves to highlight the role of FP in developing countries. Moreover, it indicates that adoption is affected by many institutional environments (Wysocki, 2011). The negative sign for the coefficient can be explained by the fact that as FP increases, there is more chance of a country adopting other standards than AAOIFI. The result for Outcome 2 is consistent with this conclusion as it shows a positive association between FP and adoption of IFRS in IBI. Another possible reason for these results, as presented in Table 9, is that countries adopting AAOIFI generally have fewer Islamic news outlets than the countries adopting IFRS.

All other predictors are not significant at any level, so it is therefore reasonable to conclude that for adoption of AAOIFI, there is no significant influence from any of the examined variables (EEO, PS, ECO, LE, SGR, and CSC) except for FP.

6.4.2 IFRS Standards Adoption

For Outcome 2, the statistically significant predictors are PS, FP, and CSC, and are shown in Table 9. The PS variable has a significant p value at the 1% level of significance, with a positive margin of 0.1258142, or 12.53 %. The positive margin of PS explains that a unit increase in the PS predictor increases the probability of Outcome 2 by 12.53%. It also indicates that countries that are more politically stable are more likely to adopt IFRS than the other two accounting standards in the IBI. This result is consistent with EDT, and therefore hypothesis H3 is accepted for Outcome 2. This result is also consistent with Al Akra et al. (2009), whose result confirms the role of a country's political system in the decision to adopt accounting standards. Zehri and Chouaibi (2013) also investigated the political system as a possible determinant for a country's decision to adopt accounting standards. Their result did not show any significance of the political system as determinants; however, this could be

related to the type of measure they used in their study which differs from the measure used in the current study. Zehri and Chouaibi (2013) employed the Gistel index to measure the political system in a country, while the present study utilises the Political Stability score to measure political system, measuring between 2.5 and -2.5 in the world governance indicators. Another possible reason for the inconsistent result between the two studies is the difference in the chosen sample countries. Purjalali and Meek (1995) confirm the role of a country's political system in changing the accounting system. Their results show that the change in the accounting system of Iran is a result of the Iranian revolution. Belkaoui (1983, 1985) also confirms the role of both the political system and economic growth of a country in developing an accounting system.

The second predictor which is statistically significant for Outcome 2 is FP. FP has a margin of 0.0003095 which is statistically significant at the 1% level of significance. This result suggests that an increase in the financial press in a country by one unit increases the probability of adopting IFRS in IBI by 0.03%. However, as the mean of the FP predictor for countries adopting IFRS is 783, it is reasonable to expect a low margin value. The impact of 783 news items and articles by 0.03% is 23.5, which indicates that the FP variable has a significant influence on Outcome 2. This result is consistent with EDT, and therefore the hypothesis H5 is accepted for Outcome 2. The result in Table 9 is consistent with EDT as well as with the literature, assuring the role of FP in company performance (Ball, 2006; Zeff, 2007). This result implies that countries adopting IFRS usually enjoy a very active FP that helps spread financial awareness regarding Islamic finance in those countries adopting IFRS. This also implies that an increase in news items and reports concerning Islamic finance can help in the adoption of IFRS as an accounting standard in IBI.

The third predictor which is statistically significant for Outcome 2 is the CSC. The CSC has a margin of -0.2716354, and is statistically significant at the 5% level of significance. This implies that the existence of a CSC in a country decreases the probability of adopting IFRS standards by 27.16%. This result is also consistent with EDT, as the theory suggests that enforcement mechanisms in any country are linked to accounting quality, and therefore hypothesis H7 is accepted for Outcome 2. Literature regarding the determinants of accounting standards adoption examines the existence of capital market as another environmental variable; however, the existence of capital market can also be considered an enforcement body in a country, as it plays a role in enforcing accounting regulations for listed companies

in the market. Zeghal and Mhedhbi (2006) and Zehri and Chouaibi (2013) examine the existence of capital market as a determinant for the adoption of IAS in different countries. The results of the study by Zeghal and Mhedhbi (2006) reveal that there is an association between the adoption of IFRS and the existence of capital market. Zehri and Chouaibi's (2013) result does not demonstrate any association between IFRS adoption and the existence of capital market. Research by Delcours and Huff (2015) is the only study which includes the governance system along with other environmental variables such as growth, education, political stability, culture, and the legal system. Their results suggest that quality of the governance system and strength of investor protection significantly influence both developing and developed countries' voluntary adoption of IFRS. Their results are also consistent with the results presented in Table 9 – CSC is considered a body of the governance system for the IFIs in a country. Therefore, it can be concluded that the result is consistent with prior research.

The negative sign of CSC coefficient suggests that CSC does not exist in the majority of countries adopting IFRS. Thus, it is reasonable to conclude that the existence of CSC in a country does not encourage the adoption of IFRS.

As discussed, there are multiple variables affecting the adoption of IFRS in the IBI. The marginal effect analysis enables the identification of the variables with the greatest influence on IFRS adoption. Comparing the margins of the three significant variables, PS (0.1258142), FP (0.0003095) and CSC (-0.2716354) for Outcome 2 (IFRS adoption), and considering the discussion above for the three variables, it is very clear that the margin, the variance, and the p value of the PS variable confirm it as the main variable affecting the choice of Outcome 2 over the other two significant variables (FP and CSC).

6.4.3 Local Standards Adoption

For Outcome 3, there are two predictors which have significant influence. The LE predictor has a margin of -0.0147216 at the 10% level of significance, meaning that one unit increase in the LE predictor will decrease the probability of using local standards in IBI. This result suggests that an increase in the level of education by one unit will result in a decrease in the probability of adopting local standards by 1.47%. This also implies that an advanced level of education in any country will influence the adoption of local standards negatively. The negative sign for the coefficient suggests that increasing the level of education will not lead to

the adoption of local standards. It is worth noting here that this variable is not associated with adoption for Outcome 1 or Outcome 2, but it is associated with Outcome 3 only. Even if there is a negative association with this variable for Outcome 3, it is still possible to conclude that this result is consistent with EDT since the association is there. This result is also consistent with prior research (e.g. Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013, Zehri & Abdelbaki, 2013) which found that advanced levels of education lead to IFRS adoption. The result can also be understood in another way, whereby low levels of education in countries adopting local standards leads to a negative association.

The CSC predictor has a positive coefficient of 0.4188346 at the 1% level of significance. This suggests that the existence of a CSC increases the probability of using local standards in the IBI. This result is also consistent with EDT, as it suggests that enforcement mechanisms in the country have a role in the adoption process. The result above is also consistent with the prior literature which investigated the role of the legal system (existence of capital market) in the adoption decision. As discussed in the IFRS adoption above, two studies investigated the existence of capital market with conflicting results (Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). Antonio and Mukhlisin (2013) conducted another study investigating the determinants of adopting accounting standards in IFIs. The study compares between the determinants of adopting accounting standards in the UK and Indonesia. The results of the study reveal that the main determinant in the implementation of accounting standards for IFIs are mainly influenced by institutional settings in the UK, and accounting needs in Indonesia. One of the factors Antonio and Mukhlisin (2013) discussed as a possible determinant is the direction of Sharia in Islamic institutions. Their results did not confirm the role of Sharia in the adoption decision, but only confirmed that the need for accounting standards is a driver for adopting accounting standards.

In addition, Table 9 shows that the CSC predictor has a margin of 0.4188346, a variance of 3.18, and a p value of 0.001; as the LE predictor has a margin of -0.0147216, a variance of 1.9, and a p value of 0.058, this shows that the CSC predictor has a greater influence over Outcome 3 than the LE predictor. This result implies that the existence of CSC in the country probably plays a main role in the adoption of local standards by IFIs in the country, to an even greater degree than educational level.

Table 10: Summary of Results

Hypotheses	Outcome 1		Outcome 2		Outcome 3	
	RRR	M.E	RRR	M.E	RRR	M.E
H1: EEO						
H2: ECO						
H3: PS			Accepted	Accepted		
H4: LE					Accepted	Accepted
H5: FP	Accepted	Accepted	Accepted	Accepted		
H6: SGR						
H7: CSC			Accepted	Accepted	Accepted	Accepted

Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)
 Variables definitions and measurements are the same as summarised in Table 4
 RRR: Relative Risk Ratio
 M.E: Marginal Effect

To summarise, it can be noted that each outcome is affected positively and negatively by different predictors. It is also possible that a single predictor can affect one outcome positively and another negatively, whilst not affecting the third outcome at all. For example, as shown in Table 9, the CSC margin is not significant for Outcome 1 at all, whilst being negatively significant for Outcome 2 and positively significant for Outcome 3. This is also the case for the FP predictor, as it positively influences Outcome 2, whilst negatively influencing Outcome 1 and having no significant influence over Outcome 3. Table 9 also shows that there is no single predictor which affects all three outcomes in the same way.

The three outcomes have varying quantities of predictors which have influence. Outcome 1 is only influenced by the FP indicator; Outcome 2 is influenced by the PS, FP, and CSC indicators; and Outcome 3 is influenced by the LE and CSC indicators. This shows that different environments will have different influences on the adoption decision of accounting standards in the IBI.

Relating the results of the RRR and the marginal effect analyses to the type of the environmental factors introduced by EDT reveals that it is mostly the internal environmental variables, such as the PS, FP, and LE variables, as well as the enforcement mechanisms, such as the CSC variable, that are more likely to influence the outcomes. In contrast, none of the three outcomes show that it can be influenced by the EEO, which is an external environmental variable.

Unexpectedly, there are some variables which show insignificance such as EEO, ECO and SGR as EDT. Compared to prior literature, openness to economy and economic growth are factors usually found to be associated with the adoption process in a country (see Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013). However, in this research, the result is not consistent with previous results. This inconsistency can be caused by a number of reasons, including differences in: a) sample size, b) context of the study, c) measurements of the tested variables, and d) timing of the study. From Table 10, it can be seen that the results of the calculated marginal effects are not too dissimilar from the interpretations of the RRR. This verification increases the validity of the results in both sections.

CHAPTER SEVEN: THE CONSEQUENCES ANALYSIS AND FINDINGS

7.1 OVERVIEW

This chapter consists of two main sections which will present the analysis and the findings of the consequences objective in the thesis. The first section covers tables and illustrations for dependent and independent variables as well as discussion about the models applied. The second section will cover the statistical summaries, discussions around the correlation, multicollinearity, and the multinomial regression analysis for the consequences.

7.2 VARIABLES AND MODELS FOR THE CONSEQUENCES

This section is covering many topics for the consequences including: dependent variables, explanatory variables, regression models and control variables for the applied models.

7.2.1 Dependent Variables

For the purpose of investigating the consequences of adopting one set of standards but not another, both the disclosure score for corporate governance (CG) reporting and the Corporate Social Responsibility (CSR) reporting are taken into account for each country. The sources of each country's disclosure scores for both CG and CSR are the Islamic finance development indicator reports issued by the Zawya Company. Detailed items included in the calculation of disclosure scores are identified in Appendix C. However, the following discussion illustrates the categories of items included to calculate the scores for both CG and CSR disclosure. Also, the CG and the CSR disclosure score for each country is presented in the tables below.

Table 11: GCGD Score and CSRD Score in the Sample Countries (AAOIFI Adoption)

Country	Adoption	Year	GCGD Index	CSRD Index
Bahrain	AAOIFI	2012	52.063	5.19
		2013	46.731	4.12
		2014	44.08333	5.47826
Jordan	AAOIFI	2012	39.57143	4.71429
		2013	31.71429	4.16667
		2014	40.375	4.14286
Lebanon	AAOIFI	2012	33	3
		2013	0	3
		2014	0	0
Mauritius	AAOIFI	2012	0	0
		2013	43	2
		2014	0	0
Oman	AAOIFI	2012	20	2
		2013	56.286	6.571
		2014	53.286	7.571
Qatar	AAOIFI	2012	42.556	5.11111
		2013	35.16667	4.18182
		2014	39.2	5.5
Sudan	AAOIFI	2012	31.25	1.75
		2013	28	1
		2014	28.6	2.75
Syrian Arab Republic	AAOIFI	2012	41	3.5
		2013	48.33333	4.33333
		2014	0	3
Tunisia	AAOIFI	2012	0	0
		2013	18	0
		2014	0	0
West Bank and Gaza	AAOIFI	2012	43	4.667
		2013	44.333	3.333
		2014	45.5	5
Average			30.1683	3.202678

Table 11, 12 and 13 provides the disclosure scores for all 30 countries adopting AAOIFI/IFRS/local standards over a three-year period. The scores indicate that countries adopting AAOIFI and local standards have more GCGD than those adopting IFRS standards. The average GCGD scores for the countries adopting AAOIFI and local standards are 30.1683 and 33.70536, respectively, compared to 20.6629 for countries adopting IFRS. For CSRD, the countries adopting AAOIFI and local standards also disclose more, showing scores of 3.202678 and 3.247223 compared to 1.870349 for countries adopting IFRS.

Table 12 :GCGD Score and CSRD Score in the Sample Countries (IFRS Adoption)

Country	Adoption	Year	GCGD Index	CSRD Index
Albania	IFRS	2012	32	2
		2013	32	2
		2014	0	0
Bosnia and Herzegovina	IFRS	2012	0	0
		2013	0	0
		2014	0	0
Kenya	IFRS	2012	0	0
		2013	0	0
		2014	0	0
Kuwait	IFRS	2012	28.55	3
		2013	28.56667	2.23077
		2014	0	2.84615
Malaysia	IFRS	2012	49.10526	3.18579
		2013	46.2	3.96154
		2014	46.82143	6.07407
Nigeria	IFRS	2012	0	0
		2013	0	0
		2014	0	0
Saudi Arabia	IFRS	2012	34.056	2.91667
		2013	33.2449	2.42553
		2014	35.46341	4.35
South Africa	IFRS	2012	42	3.67
		2013	46	1.5
		2014	51	4
Thailand	IFRS	2012	0	0
		2013	0	0
		2014	0	0
United Arab Emirates	IFRS	2012	40.22727	4.09091
		2013	40.65217	3.61905
		2014	34	4.24
Average			20.6629	1.870349

Table 11, 12, and 13 lists the average CSRD score over three years (2012, 2013 and 2014) for countries adopting IFRS and countries adopting AAOIFI; here, it can be seen that countries adopting AAOIFI disclose more than countries who adopt IFRS. The average CSRD score in countries adopting IFRS is 1.870 while the average for countries adopting AAOIFI is almost triple (3.202).

Table 13 :GCGD Score and CSRD Score in the Sample Countries (LOCAL Adoption)

Country	Adoption	Year	GCGD Index	CSRD Index
Bangladesh	LOCAL	2012	48.706	5.18
		2013	51.35714	5.46154
		2014	51.35714	5.46154
Brunei Darussalam	LOCAL	2012	50	5
		2013	40	5
		2014	0	0
Egypt, Arab Rep.	LOCAL	2012	42.33333	3.33333
		2013	41.33333	2.66667
		2014	33	4.66667
Indonesia	LOCAL	2012	52.28571	6.28571
		2013	52.1	5.5
		2014	35.84615	5.08333
Iran, Islamic Rep.	LOCAL	2012	43	4
		2013	29	3
		2014	26.85714	3.25
Iraq	LOCAL	2012	0	0
		2013	0	0
		2014	12	0
Maldives	LOCAL	2012	0	0
		2013	39.5	1.5
		2014	50	6
Pakistan	LOCAL	2012	42.87	1.89
		2013	42.02083	2.48936
		2014	43.76087	4.06522
Turkey	LOCAL	2012	45	3.5
		2013	45	3.75
		2014	47.3333	4.33333
Yemen, Rep.	LOCAL	2012	30	3
		2013	16.5	3
		2014	0	0
Average			33.70536	3.247223

Source: Islamic finance indicators (Zawya)

Corporate Governance Disclosure Score (CGDS)

As illustrated in the Islamic finance development reports, the metrics for the CGDS include many items which are grouped under specific categories.

The first category is disclosure related to financial statements, and it includes 36 items covering almost everything related to financial statements, such as figures, policies, related parties, board members, directors, and performance. The second category is management

discussion and analysis, which includes four items related to remuneration committee, reports on management discussion and analysis, and the number of people employed. The third category is Sharia reporting practices, and it includes 18 items related to the Sharia advisory board, disclosure of earnings and expenditure prohibited by Sharia, restricted assets, and information about senior managers, board of directors and shareholders. The fourth category includes items about segment reporting. The fifth category includes 11 items related to risk management reporting including items about the risk management philosophy, policy and committee, and also about the credit rating system, market risk, and information about gross loan position. The score for each country is calculated individually and illustrated in the Islamic finance development indicator web page, where the exact score for each country can be found. The score items are collected from the annual reports of IFIs as well as other reports published by the institutions. Both Islamic institutions as well as Islamic windows are taken into account when the disclosure score is calculated for each country.

Corporate Social Responsibility Disclosure Score (CSRDS)

The annual Islamic finance development reports also include the CSRDS for each country that operates Islamic finance. The CSR assessment covers IFIS in the country including Islamic banks and Islamic windows. The assessment was conducted using both the IFIs annual reports and CSR reports. The CSR assessment includes both mandatory disclosure and voluntary disclosure. The CSR mandatory assessment includes: policy for screening, policy for dealing with clients, policy for earnings and expenditure prohibited by Sharia, employee welfare, and *Zakah*. The voluntary disclosure assessment items categories include: policy for *Qard Hasan*, social, development and environment based investments, par excellence customer service, and policy for SMEs and social savings, policy for charitable activities, and policy for *Waqf* management.

7.2.2 Explanatory Variables

The explanatory variables in Table 4 are classified into external, internal, and enforcement variables. This classification approach gives the variables explicit recognition in relation to the adoption process of accounting standards. The variables tested in this paper are based on Environmental Determinism Theory (EDT), and the measurement used for some variables is chosen to represent the Islamic finance industry in the country. For example, the level of

education in a country is measured using the number of institutions in the country teaching Islamic finance courses. In addition, the financial press variable is measured using the number of news items and articles published about Islamic finance in each country. Other country level variables such as political stability, economic development and external economic openness are measured at country level using the measurements and sources illustrated in Table 4. Similar to other studies (e.g. Arpan and Radebaugh, 1985; Belkaoui, 1983, 1985; Mueller, 1963; Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013), the current study attempts to demonstrate that environmental factors are more likely associated with accounting quality in general and accounting standards outcomes in particular.

In addition to the continuous explanatory variables suggested by EDT, this research also included discrete variables related to the enforcement mechanism in each country which is possibly related to the adoption of accounting standards in the country, since IBI should be compliant with Sharia. These two variables are the existence of Sharia Governance regulations, (SGR) and the existence of a centralised Sharia committee (CSC) in the countries where Islamic banks operate. The data concerning these two variables are available from the Zawya website. The role of the enforcement mechanism to improve accounting quality in countries is discussed in previous literature, such as Cooke and Wallace (1990). However, the role of these two enforcement variables (SGR and CSC) is studied in this research for the first time in relation to the adoption of accounting standards in the Islamic banking industry. The table below gives a summary of the countries with a centralised Sharia committee and Sharia regulations. The tables below illustrate the existence of the SGR and CSC in the sample size countries.

Table 14 : Sharia Regulations and Centralised Sharia Committee in Countries Adopting (AAOIFI)

Country	Accounting Standards	Sharia Regulations	Centralised Committee
Bahrain	AAOIFI	Yes	Yes
Jordan	AAOIFI		
Lebanon	AAOIFI		
Mauritius	AAOIFI	Yes	Yes
Oman	AAOIFI	Yes	
Qatar	AAOIFI	Yes	Yes
Sudan	AAOIFI	Yes	Yes
Syrian Arab Republic	AAOIFI	Yes	Yes
Tunisia	AAOIFI		
West Bank and Gaza	AAOIFI		

Source: *Islamic finance indicators (Zawya)*

Table 15 : Sharia Regulations and Centralised Sharia Committee in Countries Adopting (IFRS)

Country	Accounting Standards	Sharia Regulations	Centralised Committee
Albania	IFRS		
Bosnia and Herzegovina	IFRS		
Kenya	IFRS		
Kuwait	IFRS	Yes	Yes
Malaysia	IFRS	Yes	Yes
Nigeria	IFRS	Yes	Yes
Saudi Arabia	IFRS		
South Africa	IFRS		
Thailand	IFRS		
United Arab Emirates	IFRS	Yes	Yes

Source: *Islamic finance indicators (Zawya)*

Table 16 : Sharia Regulations and Centralised Sharia Committee in Countries Adopting (LOCAL)

Country	Accounting Standards	Sharia Regulations	Centralised Committee
Bangladesh	LOCAL		
Brunei Darussalam	LOCAL	Yes	Yes
Egypt, Arab Rep.	LOCAL		
Indonesia	LOCAL	Yes	Yes
Iran, Islamic Rep.	LOCAL		
Iraq	LOCAL		
Maldives	LOCAL	Yes	Yes
Pakistan	LOCAL	Yes	Yes
Turkey	LOCAL		
Yemen, Rep.	LOCAL		

Source: *Islamic finance indicators (Zawya)*

From Table 14, 15 and 16, it is clear that countries adopting AAOIFI have more CSC than countries in the other groups. Five countries in the AAOIFI group (Bahrain, Mauritius, Qatar, Sudan and Syria) have CSC compared to only four IFRS countries (Kuwait, Malaysia, Nigeria and United Arab Emirates) and four countries in the local standards group (Brunei, Indonesia, Maldives and Pakistan). This result is consistent with El-Halaby and Hussainey's (2015) conclusion that CSR is affected by the existing Sharia auditing department (SAD) inside the bank. SAD is one form of the Sharia governance system that currently exists in the IFI to ensure compliance with Sharia in financial and legal transactions, as is the case in CSC.

7.2.3 Regression Model for Consequences of Accounting Standards Adoption

The two models designed to test the hypotheses (H8 & H9) for the possible consequences of adopting different standards are explained in this section. The dependent variables in these two models represent CG disclosure in the country in Model 1, while they represent CSR disclosure in Model 2. The independent variable in the model is the adoption variable, and this represents the different types of accounting standards adopted in the IBI (AAOIFI, IFRS, or local). Other variables (external of economic openness, economic growth, political stability, level of education, financial press, Sharia governance role in the country, and centralised Sharia committee) are included in the model as control variables; hence, the literature concerning MNL regression illustrated that these variables are possible determinants for accounting standards adoption and accounting quality in the country.

Model 3

Model 3 is designed to examine how the score of corporate governance disclosure can vary between the countries adopting different accounting standards (AAOIFI, IFRS and local standards) in IBI, controlling for all other possible variables which could affect the disclosure score.

$$\begin{aligned} \text{CGDscore} = & \beta_0 + \beta_1 \text{Adoption}_i + \beta_2 \text{EEO}_i + \beta_3 \text{ECO}_i + \beta_4 \text{PS}_i + \beta_5 \text{LE}_i \\ & + \beta_6 \text{FP}_i + \beta_7 \text{SGR}_i + \beta_8 \text{CSC}_i + \varepsilon_i \end{aligned}$$

Where:

CGDscore is the score of the disclosed items related to corporate governance in the country adjusted to the population of the country; **Adoption** is a nominal variable that is equal to 1 if the country adopts AAOIFI, 2 if the country adopts IFRS, and 3 if the country adopts local standards in the IBI; **EEO** is % of export to GDP + % of imports to GDP – it is measured annually at the country level; **ECO** is Growth Domestic Product per Capita in (\$) – it is measured annually at the country level; **PS** Political Stability score measured between 2.5 and -2.5 from the world governance indicators; **LE** number of Islamic Institutions offering training in the country; **FP** is the number of exclusive and regional Islamic finance news items and articles; **SGR** is a dummy variable where 1 is the existence of Sharia Governance Regulation, otherwise 0; **CSC** is a dummy variable where 1 is the existence of a centralised Sharia committee, otherwise 0; and ε is the error term.

Model 4

Model 4 is designed to examine how the score of CSR disclosure can vary between the countries adopting different accounting standards (AAOIFI, IFRS and local standards) in IBI, controlling for all other possible variables which could affect the disclosure score.

$$\text{CSRscore} = \beta_0 + \beta_1 \text{Adoption}_i + \beta_2 \text{EEO}_i + \beta_3 \text{ECO}_i + \beta_4 \text{PS}_i + \beta_5 \text{LE}_i \\ + \beta_6 \text{FP}_i + \beta_7 \text{SGR}_i + \beta_8 \text{CSC}_i + \varepsilon_i$$

Where:

CGDscore is the score of the disclosed items related to corporate governance in the country adjusted to the population of the country; **Adoption** is a nominal variable that is equal to 1 if the country adopts AAOIFI, 2 if the country adopts IFRS, and 3 if the country adopts local standards in the IBI; **EEO** is % of export to GDP + % of imports to GDP – it is measured annually at the country level; **ECO** is Growth Domestic Product per Capita in (\$) – it is measured annually at the country level; **PS** Political Stability score measured between 2.5 and -2.5 from the world governance indicators; **LE** number of Islamic Institutions offering training in the country; **FP** is the number of exclusive and regional Islamic finance news items and articles; **SGR** is a dummy variable where 1 is the existence of Sharia Governance Regulation, otherwise 0; **CSC** is a dummy variable where 1 is the existence of a centralised Sharia Committee, otherwise 0; and ε is the error term.

7.2.4 Controlling for Institutional Factors in the Model

Financial reporting standards and disclosure are part of the institutional framework of each country. Hence, the institutional system of a country is significantly interrelated, making it very difficult to study the actual effect of disclosure and financial reporting standards without controlling for all the other possible effects from the institutional environment. For example, it is obvious that countries with an equity market can provide more disclosure and more efficient enforcement mechanisms for investor protection (La Porta et al., 2006). Despite the challenges involved in these international studies, it is clear that cross country studies have an important role in advancing research on the role of institutions (Leuz & Wysocki, 2016). The general conclusion from all studies support that of La Porta et al. (1997, 1998), where disclosure is used as proxy to transparency or other proxies in consideration of controlling for the institutional variables, and this emphasises that there is a significant association between disclosure and different institutional factors. Therefore, in the current research, the important institutional factors in the country are controlled for. These institutional factors include:

education level, economic growth, political stability, and financial press and enforcement mechanisms in the countries. Reviewing the international studies also reveals the important role of enforcement as an institutional factor (e.g. Bhattacharya & Daouk, 2002; Coffee, 2007; Cumming et al., 2011; Frost & Pownall, 1994; Hope, 2003; Jackson & Roe, 2009; La Porta et al., 2006).

7.3 Findings and Discussion on Consequences

This section presents a discussion of the statistical summaries, correlation, multicollinearity and the multinomial regression analysis used in the research, the descriptive statistics of the variables, results of the models, and a discussion of the results.

7.3.1 Descriptive Analysis

Table 17 represents the descriptive statistics of the independent variables. Panel A displays the descriptive statistics of the continuous variables in the model, which include external economic openness, stage of economic development, political system, level of education and financial press. Panel B presents the frequencies of discrete variables.

Table 17 :Sample Descriptive Statistics for Continuous Variables

Panel A: Descriptive Statistics for Continuous Variables						
Adoption	Variable	N	Mean	SD	min	max
AAOIFI	CGDS	30	25.84923	19.75773	0	52.063
	CSRDS	30	2.731278	2.002395	0	5.5
	EEO	20	96.4432	35.5026	21.65651	133.5484
	PS	30	-0.86166	1.299965	-2.75742	1.210541
	ECO	25	1.32352	3.927479	-7.09576	11.08503
	LE	30	6.6	5.727128	0	21
	FP	30	306.8333	405.0693	0	1609
IFRS	CGDS	30	20.6629	20.37495	0	51
	CSRDS	30	1.870349	1.863537	0	6.07407
	EEO	28	98.88012	46.68173	30.2	185.5995
	PS	30	-0.39448	0.840843	-2.10576	0.8922639
	ECO	29	1.935306	1.838666	-3.43745	6.076476
	LE	30	14.13333	21.99174	0	99
	FP	30	783.1333	1168.991	13	4216
LOCAL	CGDS	30	32.15536	19.89253	0	52.28571
	CSRDS	30	3.047223	2.187112	0	6.28571
	EEO	25	83.19413	56.82001	31.16821	219.2552
	PS	30	-0.99125	1.066748	-2.68628	1.267537
	ECO	30	1.841595	3.928445	-9.20013	9.281366
	LE	30	6.3	7.134907	0	24
	FP	30	292.8667	444.6324	30	2447
TOTAL	CGDS	90	26.2225	20.34058	0	52.28571
	CSRDS	90	2.549617	2.060787	0	6.28571
	EEO	73	92.84055	47.70829	21.65651	219.2552
	PS	90	-0.74913	1.103738	-2.75742	1.267537
	ECO	84	1.719759	3.325924	-9.20013	11.08503
	LE	90	9.011111	14.07643	0	99
	FP	90	460.9444	784.6522	0	4216
	SGR	90	0.433333	0.498312	0	1
	CSC	90	0.3	0.460825	0	1
Panel B: Descriptive Statistics for Discrete Variables						
	Dummies	0 (%)	1 (%)			
AAOIFI	SGR	15 (50%)	15 (50%)			
	CSC	24 (80%)	6 (20%)			
IFRS	SGR	18 (60%)	12 (40%)			
	CSC	21 (70%)	9 (30%)			
LOCAL	SGR	18 (60%)	12 (40%)			
	CSC	18 (60%)	12 (40%)			
<i>Table 4 for Variables' Codes, Definitions and Data Sources</i>						
General Corporate Governance Disclosure Score (GCGDS), CSR Disclosure Score (CSRDS), External Economic Openness (EEO), Stage of Economic Development (ECO), Political Systems (PS), Level of Education (LE), Financial Press (FP), Sharia Governance Regulation (SGR), Centralised Sharia Committee (CSC).						

In Table 17, the data in Panel A shows that the first two variables in each group (AAOIFI, IFRS, local) are the two dependent variables in the analysis: 1) Corporate Governance Disclosure Score (CGD) and 2) Corporate Social Responsibility Disclosure Score (CSRD). In

the first group (AAOIFI), the mean for the CGDs in this group is 25.84. The maximum score for CGDs is 52.063, with the minimum being 0. In the second group (IFRS), the mean for the CGDs is 20.66, which is five points less than the CGDs in the AAOIFI group. The maximum points for the IFRS group is 51, and the minimum is 0. In the local group, the mean of the CGDs is 32.15 which is the highest across all groups. The maximum for the CGDs in the local group is 52.28, and the minimum is 0. The standard deviation is 19.75, 20.37 and 19.89253 for AAOIFI, IFRS and local groups respectively, indicating that most countries have CGDs higher than the mean of their group.

The CSR score for the AAOIFI group is 2.73: the maximum is 5.5 and the minimum is 0. The CSR score for the IFRS group is 1.87: the maximum is 6.07 and the minimum is 0. Unlike the other two groups, the mean for CSR in the local group is higher, as it scores 3.047 compared to 2.73 for AAOIFI and 1.87 for the IFRS group. The maximum is 6.28 and the minimum is 0. The standard deviation of the CSR score for the AAOIFI, IFRS and local groups respectively is 2, 1.86 and 2.18, indicating that most countries have a CSR score higher than the reported mean. Furthermore, when the results for CGDs and CSRs are read together, it becomes clear that both scores are higher in the local group compared to the AAOIFI and IFRS groups. This is a possible indicator that disclosure in the countries adopting local standards in their IBI emphasises a greater need for disclosure than in the countries adopting AAOIFI and IFRS standards in their IBI. Further confirmation on this matter will follow in the analysis section.

With regard to the other explanatory and control variables, it can be seen from Panel A that variation in the mean, minimum, and maximum value exists between all continuous explanatory variables. The External Economic Openness (EEO) means across the AAOIFI, IFRS and local groups are 96.44m, 98.88m and 83.19m, respectively. The mean of the EEO indicates that countries adopting IFRS are more open to economies compared to countries adopting AAOIFI and local standards. The mean of the EEO, as in Table 3, also indicates that the EEO in countries using local standards is more than ten times less compared to the mean of EEO in the AAOIFI and IFRS groups. The minimum score for EEO is 21.65m and the maximum is 219.25m.

The political stability (PS) variable has a negative mean in all three groups. The PS mean is 0.86 in the AAOIFI group, -0.39 in the IFRS group, and -0.99 in the local group. The mean

results indicate that countries adopting IFRS are more politically stable than countries in the other two groups. The min PS score is -2.757 and the maximum is 1.26.

The Economic Growth (ECO) mean of the countries in each group are 1.32, 1.93 and 1.84, respectively, for countries using AAOIFI, IFRS and local standards. It is again clear that the countries adopting IFRS and local standards enjoy more economic growth than countries using AAOIFI. The minimum value of the ECO is -9.20, as in the local group, while the maximum value is 11.08 for the AAOIFI group, as indicated in Table 3.

The Level of Education (LE) in the three groups is: 6.6, 14.12 and 6.3 for countries adopting AAOIFI, IFRS and local standards, respectively. From the mean of the LE, the conclusion can be drawn that countries adopting IFRS have almost twice the number of institutions that offer Islamic finance courses compared to countries adopting AAOIFI and local standards. The minimum value of the LE is 0, while the maximum is 99, as indicated in the IFRS group.

The Financial Press (FP) shows the most variation among the independent variables, as the minimum in the FP is 0 news items and articles (in the AAOIFI group) while the maximum is 4216 (the IFRS group). The mean FP for the three groups are: 306.83, 783.13 and 292.86 for AAOIFI, IFRS, and local standards, respectively. The mean figures indicate that the AAOIFI group has the lowest number of articles and news items relating to Islamic finance per year. In contrast, the group of countries adopting IFRS has the highest number of news items and articles per year.

Panel B illustrates the descriptive statistics of the discrete variables, where 1 indicates the existence of either the governance regulations or the existence of a centralised Sharia committee in the country, while 0 indicates the non-existence of either. The results show interesting variation in the two variables, as one would expect that either both would exist together or none at all. Interestingly, the existence of Sharia governance regulations does not necessarily mean that a centralised Sharia committee also exists in the same country. For example, in countries adopting local and IFRS standards, four countries have Sharia governance regulations, while in countries who have adopted AAOIFI, five have the same governance regulations. The existence of Sharia regulations in a country does not automatically lead to a centralised Sharia committee. Panel B data shows that out of ten countries using AAOIFI, only two have a Sharia committee. In the local and IFRS standards adoption groups, a mere four countries from each group have a centralised Sharia committee.

Analysis of the above statistics regarding the variables reveals quite clearly that quite a substantial amount of variation exists between each of the groups adopting different accounting standards. This variation in the descriptive statistics of the study's variables illuminate the fact that the environment differs rather widely between countries. Thus, the choice of different accounting standards in each country can be related to the differing environmental variables of these countries.

7.3.2 Assumptions of the OLS Model

Multiple regression is a widely used multivariate technique among the statistical analysis techniques due to its broad applicability for many purposes. As Hair et al. (2006) explain, the two main purposes for using multiple regression in research are the prediction and the explanation. Prediction involves how one or more independent variables can predict the dependent variable. On the other hand, the explanation examines the regression coefficients and tries to form a conclusion about the effect of the independent variables. It is also the case that some studies are designed in such a way that the multiple regression answers the prediction as well as the explanation. However, the model must be defined in order to investigate the research problem, otherwise measurement errors can occur. Measurement errors can be defined as "the degree to which the variable is an accurate and consistent measure of the concept being studied" (Hair et al., 2006, p.193). In other words, measurement errors can happen when the dependent variable does not accurately represent the item which needs to be predicted, and therefore an acceptable level of predictability cannot be achieved for the variable. Another main concern in the regression model is specification error, as this represents the possibility of including irrelevant variables as independent variables, or failing to include a relevant variable in the model (Hair et al., 2006).

When using the regression model, it is important to be aware of the effect sample size can have on generalisability. If the sample size is insufficient, the results of the regression cannot be generalised. Hair et al. (2006) state that the cut-off point for the ratio should be always more than or equal to 5:1 (five observations for each independent variable in the model), with the recommended ratio being between 15 and 20 observations for each independent variable. Since generalisation relies on the degree of freedom, which increases along with sample size, a bigger sample will give better generalisability. It is always recommended to increase the sample size whenever possible in order to allow better generalisability through increased degree of freedom (Hair et al., 2006).

Most of the tests, including the regression and analysis techniques used through the different suggested models in the literature, are actually parametric tests based on the assumption that the data are also parametric. To verify whether the data are parametric or not, it must meet the characteristics of being parametric by achieving assumptions including linearity, normality, homogeneity, and independence, and must meet the model specification. Analysing data that fails to meet the assumptions of the parametric data are likely to generate incorrect results. The sections below set out how to check whether data are parametric, starting with identifying the outliers and the influence of the data. Further sections discuss how to identify the linearity of the phenomenon measured, normality of the error term distribution, homogeneity (constant variance of the error terms), independence of the error terms, errors in variables, and model specifications.

Outliers

The Institute for Digital Research and Education (IDRE) website defines an outlier as “an observation with large residual. In other words, it is an observation whose dependent variable value is unusual given its values on the predictor variables. An outlier may indicate a sample peculiarity or may indicate a data entry error or other problem” (IDRE, 2016). There are two main methods to test for outliers in the data before commencing analysis: the leverage method and the studentized residual of the error term, both of which can help identify the outliers in the model.

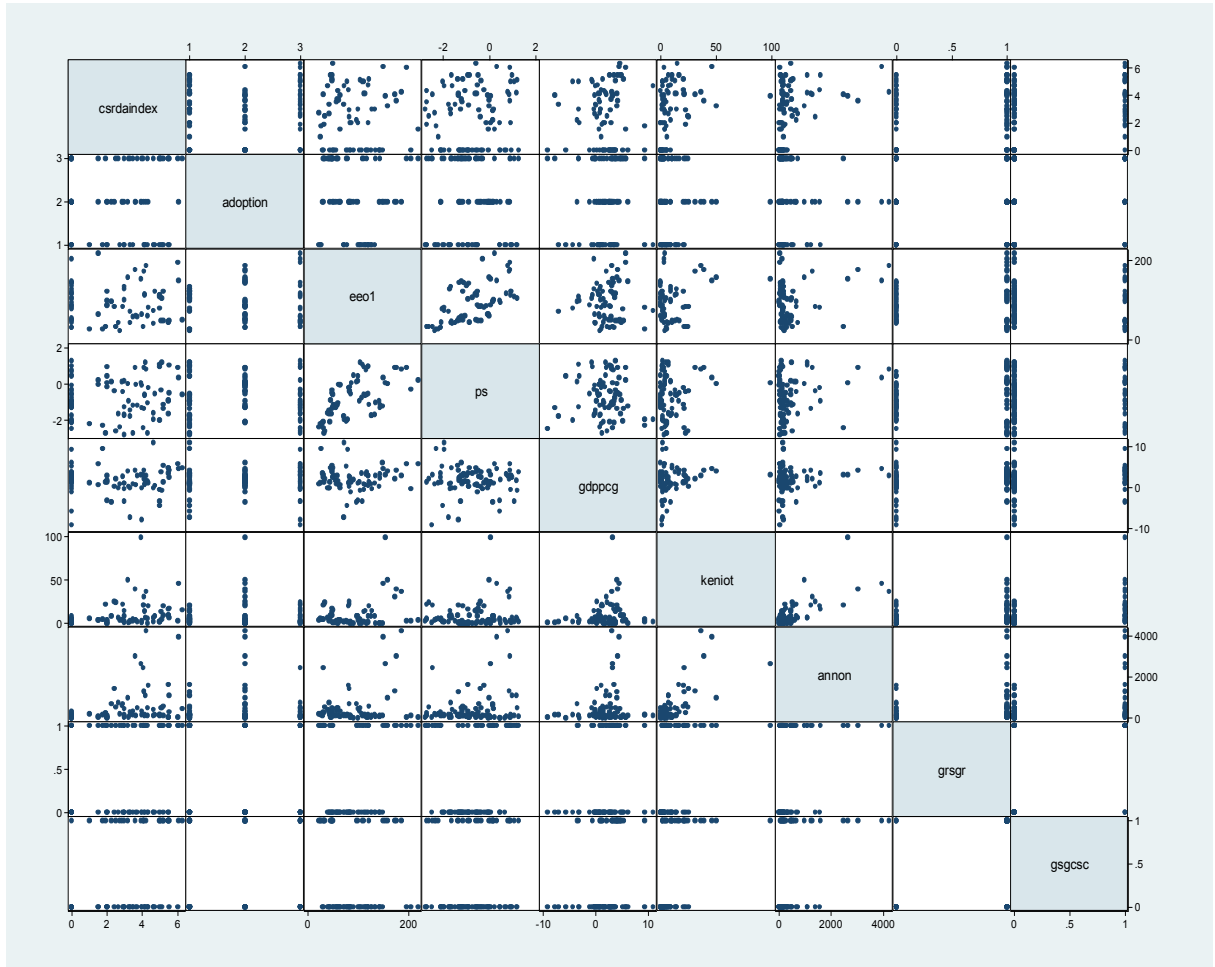


Figure 2: Plot of all independent variables

The graphs of the CGDscore show potential problems, as in every plot there are data points which are located far away from the majority of data points. Because of this, further analysis of the data is needed to identify the potential outliers. The scatterplot with country labels gives a clearer picture about the distribution of the variables in the suggested regression model, as illustrated in Figure 5.

Stem-and-leaf plot for r (Studentized residuals)

r rounded to nearest multiple of .01
plot in units of .01

```

-2** | 01
-1** | 90
-1** | 74,70,67,63
-1** | 40
-1** | 39,33,26,23
-1** | 18,12,10
-0** | 93,90,80
-0** | 66,64,63,60
-0** | 56,53,51,48,45,43,43
-0** | 35,29,29
-0** | 10,07,05
0**  | 05,13,14
0**  | 21,23,25,28,30,31,37,37,37
0**  | 42,45,45,48,50,51,52,56,58
0**  | 73,75,75,76,78
0**  | 88,93,95
1**  | 00,06,08,17
1**  | 24,29,31
1**  |
1**  |
1**  |
2**  | 05
2**  |
2**  |
2**  | 61
2**  |
3**  |
3**  |
3**  | 42

```

Figure 3: Steam leaf of r

The steam leaf of the studentized residual of the data highlights several observations which are possible outliers in the data. Figure 4 below presents a table of countries which have unusual residual, and those residuals will be investigated further to verify whether or not they are outliers. The cut-off points for the residual to be considered an outlier are when r is greater than or equal to (\geq) 2.5, or when r is less than or equal to (\leq) -2.5. The r results presented below show that r for West Bank of Gaza (2.61) is slightly higher than the cut-off point for r to be considered an outlier. However, the r for Maldives is 3.42, indicating the possibility of this country being an outlier. However, it is always recommended to use at least two methods

before concluding anything in this regard; the data were checked after these results were obtained, and no errors were found.

```
. list r country if abs(r) > 2.5
```

	r	country
72.	2.60619	West Bank and Gaza
73.	3.420178	Maldives
74.	.	Oman
75.	.	Brunei Darussalam
76.	.	Iran, Islamic Rep.
77.	.	Iraq
78.	.	Bosnia and Herzegovina
79.	.	Iran, Islamic Rep.
80.	.	Bahrain
81.	.	Kuwait
82.	.	Qatar
83.	.	Oman
84.	.	Syrian Arab Republic
85.	.	Syrian Arab Republic
86.	.	Syrian Arab Republic
87.	.	Tunisia
88.	.	Qatar
89.	.	Iran, Islamic Rep.
90.	.	Bahrain

Figure 4: List of countries where $r \geq 2.5$

Leverage

Calculating the leverage is another way to identify possible outliers in the data. The formula to identify the cut-off point for leverage to be considered an outlier is: $(2 \cdot V + 2/n)$. Applying this formula to our analysis gave us $2 \cdot 8 + 2/90 = 0.2$, therefore any country with leverage more than 0.2 is considered an outlier. Using 0.2 as the cut-off point to identify the outlier in the data reveals that six countries are potential outliers, depending on the leverage method. These countries are Malaysia, Maldives, Sudan, United Arab Emirates, Pakistan, and West Bank and Gaza.

When comparing the residual result with the leverage results when identifying the outliers in the data, it was noticed that each method identified a different number of countries. One way to rectify the results of the two methods is to plot the leverage and the residual result in one plot which can help in identifying the outliers more clearly. The diagram below is the leverage residual plot, and from the diagram it is very clear that both methods identified

different countries as outliers. While the normalised residual square identified West Bank and Gaza as a possible outlier, the leverage method identified Malaysia and UAE as potential outliers.

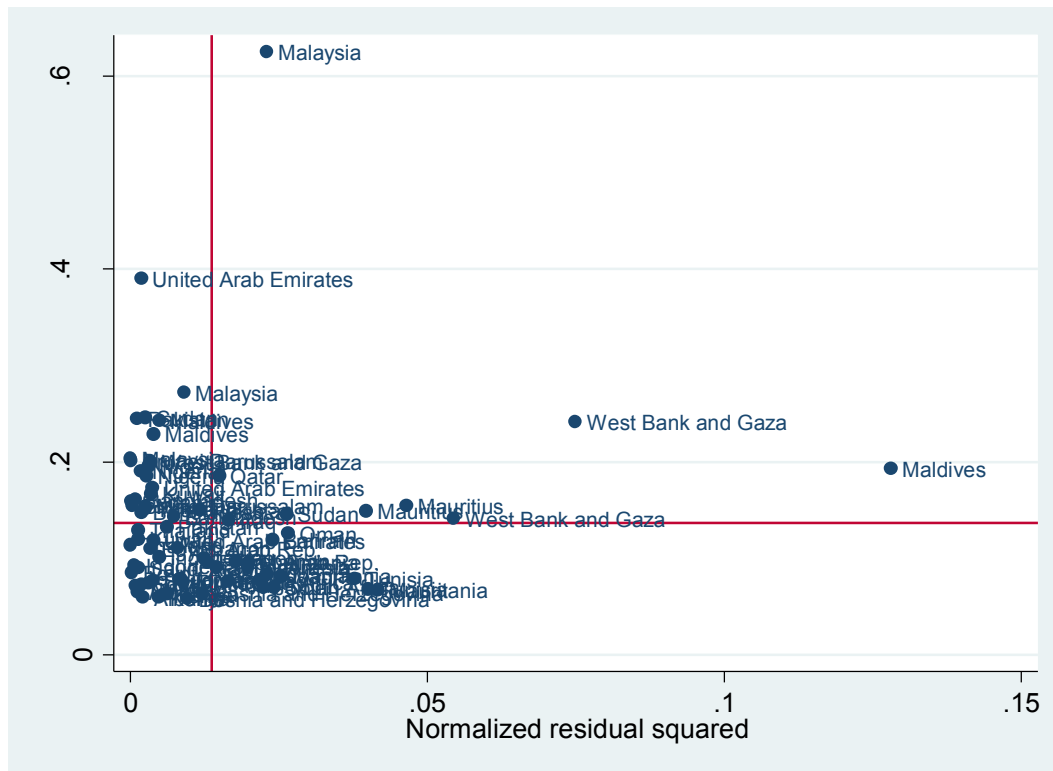


Figure 5: Leverage residual plot

Normality of the Error Term Distribution

Testing for normality is an essential step in analysing both dependent and independent variables. The simplest way to test for the normality of independent variables is the residual histogram. This means of testing for normality is very difficult in smaller samples, so an alternative way of checking the normality is the use of normal probability plots (Hair et al., 2006) such as the Kernel density, p norm and q norm, as “...normal distribution makes a straight diagonal line and the plotted residuals are compared with the diagonal” (Hair et al, 2006, p.208).

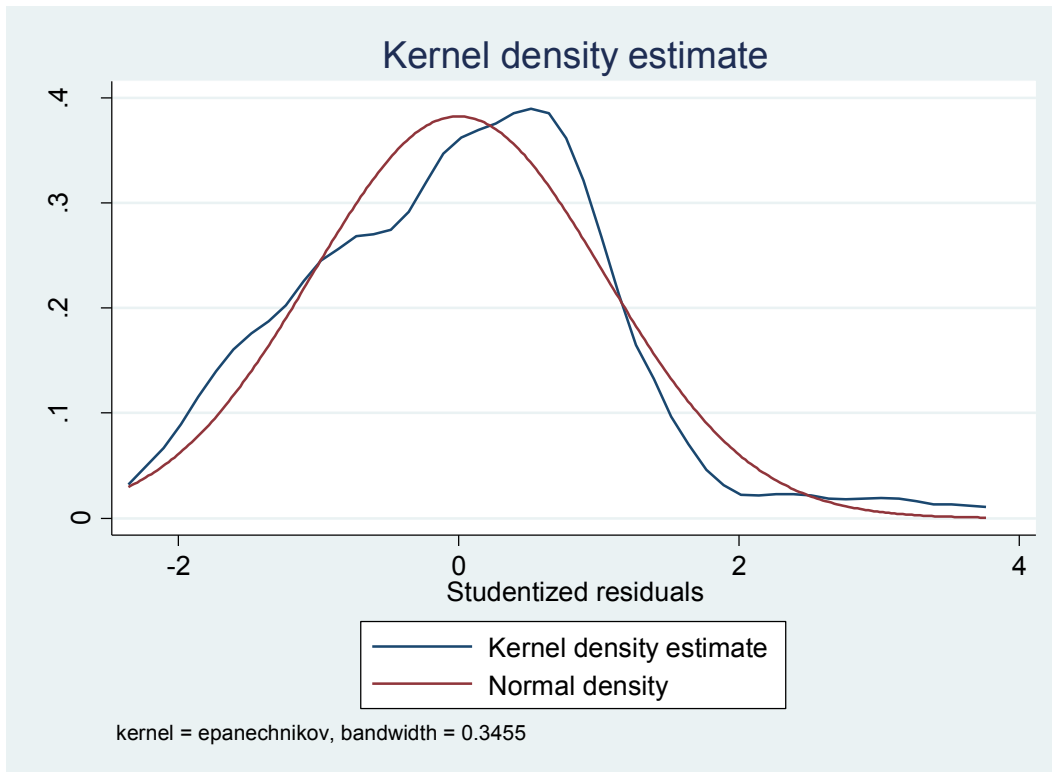


Figure 6: Kernel density estimate for normality

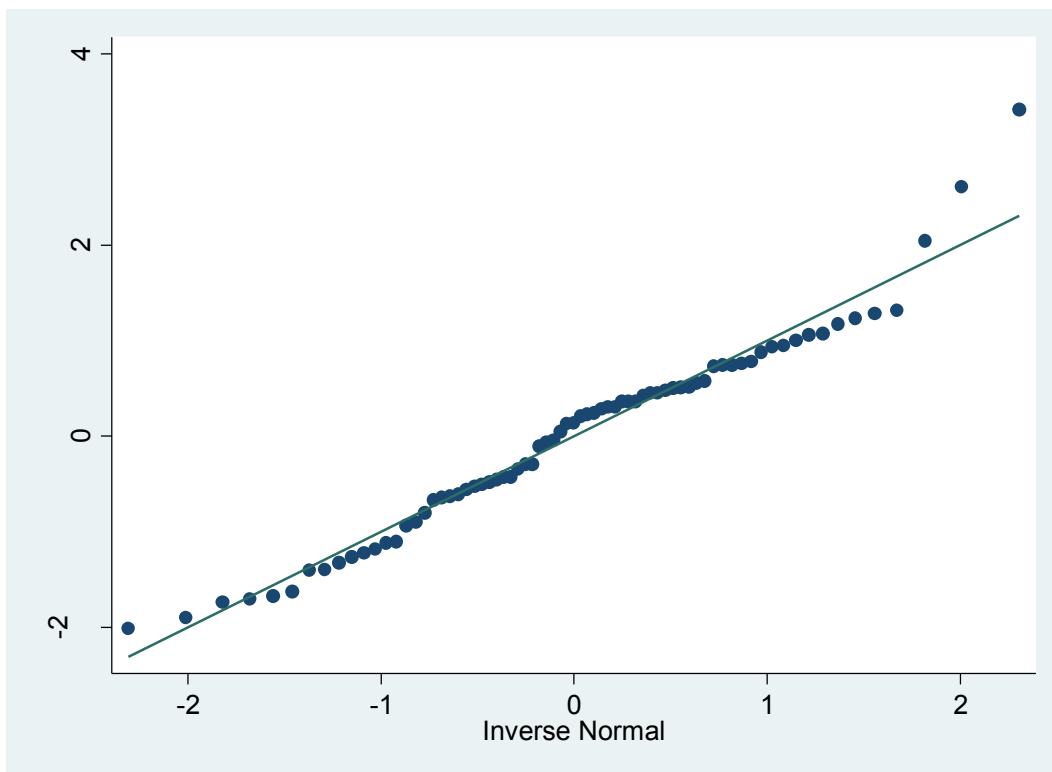


Figure 7: P norm graph to test for normality

Shapiro-Wilk W test for normal data

Variable	Obs	W	V	z	Prob>z
r	73	0.97056	1.875	1.370	0.08528

Figure 8: Shapiro-Wilk test for normality

The Shapiro-Wilk ‘W test’ examines the normality of data in the regression model. The hypothesis of the test is based on the assumption that the distribution is normal. As can be seen in from the table above, the p value is very small (0.085), indicating that the r is not normally distributed – thus, the data is not normally distributed. This suggests the need to run the regression analysis, taking into consideration the need to correct the abnormal distribution of data. Robust regression can take care of such a regression assumption violation (IDRE, 2016); the robust regression was conducted instead of the simple pool OLS. The Shapiro-Wilk W test was generated following the robust regression, and the results show that the test must assume that r is normally distributed.

. swilk r

Shapiro-Wilk W test for normal data

Variable	Obs	W	V	z	Prob>z
r	73	0.97443	1.629	1.063	0.14380

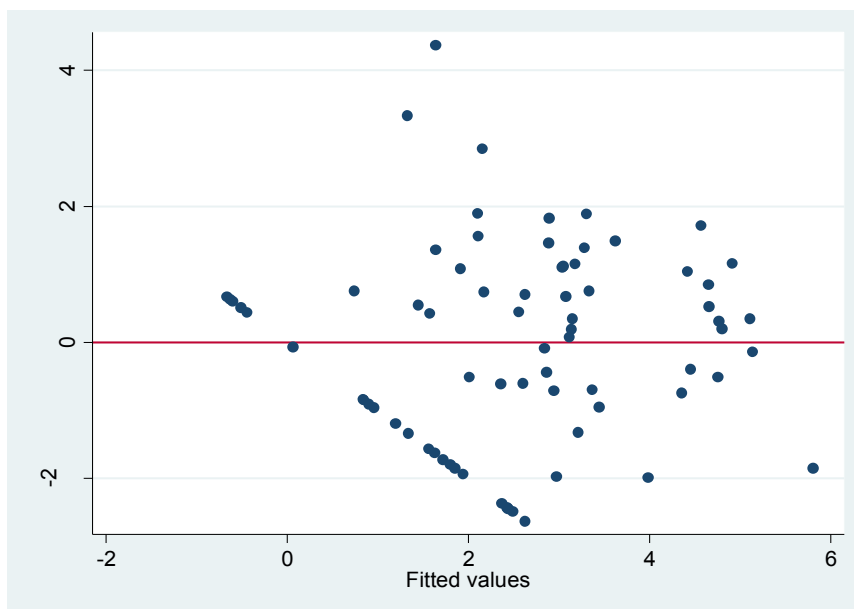
Figure 9: Shapiro-Wilk test for normality after running robust regression

Homogeneity of Variance (Residual)

One of the main assumptions of the least square regression is the homogeneity of the variance of residuals. If the variance of the residuals is non-constant then the residual variance is said to be “heteroscedastic”. The unequal variance (heteroscedasticity) is a violation of the assumption which is very common. The heteroscedasticity test is important in the cross-sectional analysis as it analyses the relationship between the dependent variable and the cross-section error term. In the cross-sectional analysis, the existence of heteroscedasticity leads to

unequal variance circumstances which, according to Hair et al. (2006), can cause the dispersion of the values of the dependent variable if not constant across the values of the independent variables. In other words, the existence of heteroscedasticity can limit the explanation of the regressor to the dependent variable as well as the variance of the independent variable, if not equally explained by each of the independent variable. This leads to correct estimation of the standard error and hence the result of the hypothesis testing will be biased. Heteroscedasticity can be identified through the residual plots as well as statistical tests (Hair et al., 2006). Statistical tests such as White's test can be used as well as graphical methods to identify heteroscedasticity. One graphical method involves plotting the residual versus the predicted values, which can then be tested in Stata using the 'rvfplot' command. If heteroscedasticity exists, there are two possible remedies, as recommended by Hair et al. (2006). First, the weighted least square method can be employed if the violation attributed to a single independent variable. Second, the transformation of the variables can also be used to exhibit homoscedasticity. Therefore, to avoid this problem and to control for heteroscedasticity, robust standard error is used in the analysis for both OLS models (CGDs and CSRDs).

Figure 10: Residual and fitted data plot to test for heteroscedasticity



Cameron & Trivedi's decomposition of IM-test

Source	chi2	df	p
Heteroskedasticity	67.59	49	0.0403
Skewness	10.53	9	0.3096
Kurtosis	0.02	1	0.8851
Total	78.14	59	0.0484

Figure 11: White's test

```
. estat hettest

Breusch-Pagan / Cook-Weisberg test for heteroskedasticity
Ho: Constant variance
Variables: fitted values of csrdaindex

chi2(1)      =    0.45
Prob > chi2  =    0.5006
```

Figure 12: Breusch-Pagan/Cook-Weisberg test for heteroscedasticity

Both tests test the null hypothesis that the variance of residual is homogenous. If the p value is very small, the null hypothesis can be rejected and the hypothesis that the variance is not homogenous can thus be accepted. These two tests are very sensitive to the normality of the data, therefore it is recommended that heteroscedasticity be checked through plots combined with these two tests in order to ascertain whether any correction is needed for heteroscedasticity. The results from the Breusch-Pagan / Cook-Weisberg test ⁵ for heteroscedasticity shows that the p value is large enough to accept the null hypothesis (that the variance is homogenous). In contrast, a small p value in the White's test indicates the existence of heteroscedasticity. As robust regression has the feature of dealing with heteroscedasticity, then there is no concern that this might affect the regression result.

Linearity

In linear regression, there is an assumption that the relationship between the dependent variables and predictors is linear. If this assumption is violated, the linear regression will try apply a straight line to data that does not follow a straight line. Linearity is the degree to which the change in the dependent variable is associated with the independent variable. In

⁵ Other tests, such as Cameron & Trivedi's decomposition of IM-test, are also known as White's tests

addition, the regression coefficient is constant across the range of values of the independent variable (Hair et al., 2006). The linearity of the model can be easily examined through the residual plots. In other words, to plot the standardised residuals against each of the predictor variables in the regression model. If linearity does not exist, then corrective actions can be taken such as transforming the data values (e.g. logarithm and square roots, etc.) of one or more independent variables to achieve linearity. The following steps should be followed to correct for such deviation:

- Check the normality of the predictor variable, if not normally distributed
- Carry out transformation for the variable (using the log or square root)
- Run the regression again, placing the transformed variable in the regression model
- Check the linearity of the transformed variable.

Other actions involve including the nonlinear relationships in the regression model such as through creating polynomial terms, or using specialised methods such as nonlinear regression specifically designed to accommodate the nonlinearity effects of independent variables.

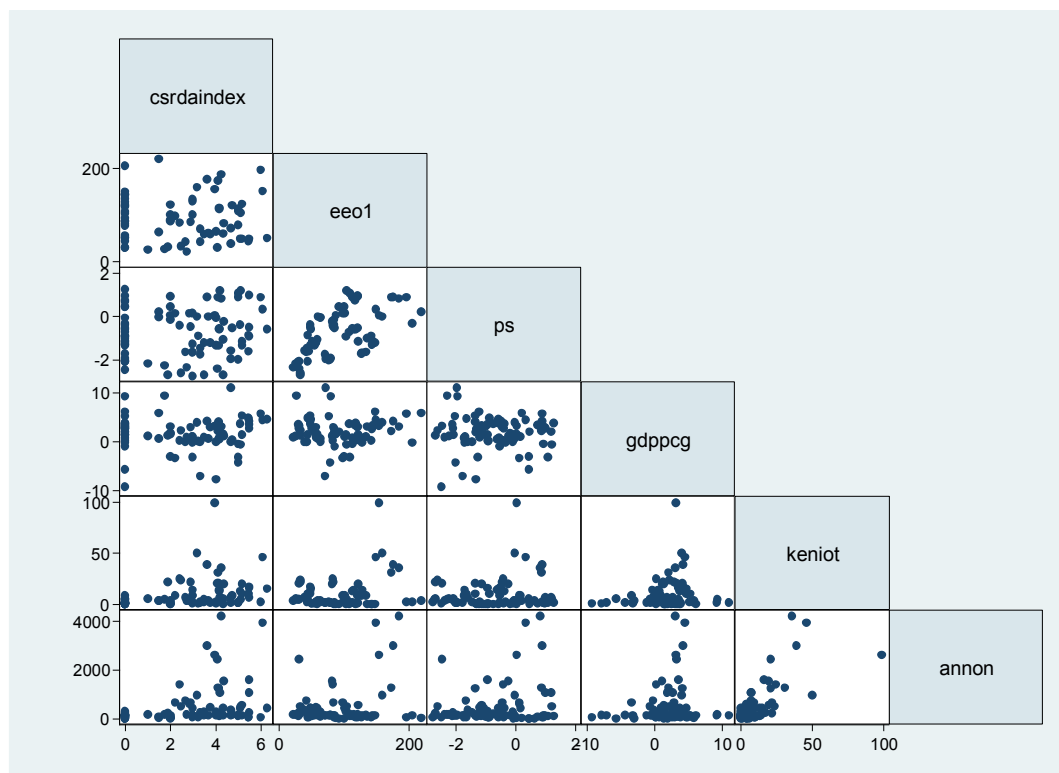


Figure 13: **Half plot for checking linearity**

In the scatterplot above, the nonlinearity cannot be of concern since the identified outliers will be dealt with through the robust regression. Other than the outliers appearing in the graph above which have previously been identified, there is no reason to reject this assumption. Therefore, it can be reasonably concluded that the linearity assumption is valid for continuous variables in the model.

Model specifications

Model specification errors can occur when one or more variables are omitted from the model or unrelated variables are included in the model. If relevant variables are omitted from the model, the common variance they share with the included variables may be wrongly attributed to those variables, and the error term is inflated. Conversely, if irrelevant variables are included in the model, the common variance they share with included variables may be wrongly attributed to them. Model specification errors can substantially affect the estimate of regression coefficients.

There are different methods for detecting specification errors. The link test command is one way to detect model specification errors in single-equation models. This test is based on the idea that if the model is well specified, then no other independent variable should be significant, except by chance. Link tests create two new variables: the variable of prediction, `_hat`; and the variable of squared prediction, `_hatsq`. The model then refits using these two variables as predictors. `_hat` should be significant, as it is the predicted value. However, the `_hatsq` should not be significant, because if the model is correctly specified then the squared prediction should not have much explanatory power. Therefore, the p value of the `_hatsq` is what will indicate if the model specification is correct or not.

```
. linktest
```

Source	SS	df	MS			
Model	161.550993	2	80.7754966	Number of obs =	73	
Residual	147.830119	70	2.11185884	F(2, 70) =	38.25	
Total	309.381112	72	4.29695989	Prob > F =	0.0000	
				R-squared =	0.5222	
				Adj R-squared =	0.5085	
				Root MSE =	1.4532	

csrdaindex	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]	
<code>_hat</code>	.8254558	.3078144	2.68	0.009	.2115393	1.439372
<code>_hatsq</code>	.0358041	.0586014	0.61	0.543	-.0810726	.1526809
<code>_cons</code>	.1334108	.4026493	0.33	0.741	-.6696479	.9364696

Figure 14: Link test for the model specification

The above link test for `_hatsq` is not significant. This result indicates that the link test failed to reject the hypothesis that the model is specified correctly. Therefore, it is possible to conclude that there no specification error exists in the model.

```
. ovtest
```

```
Ramsey RESET test using powers of the fitted values of csrdaindex
```

```
Ho: model has no omitted variables
```

```
F(3, 60) = 1.56
```

```
Prob > F = 0.2078
```

Figure 15: Ramsey reset test for the model specification

Another test which works in a similar way to the link test is the `ovtest`. Here, new variables are created based on the prediction and added to the model. The results of the model show that the null hypothesis (that the model specification is correct) cannot be rejected, as the *p* value of the `ovtest` is not significant. Therefore, no further test needs to be carried out after the addition of the robust command to control for the other violation of the assumptions.

Independence (Autocorrelation): Independence or Error Terms

In the regression analysis, it is assumed that each predicted value is independent; in other words, each predicted value is unrelated to any other prediction and is not sequenced by any variable. This assumption emphasises “that the errors associated with one observation are not correlated with the errors of any other observation” (IDRE, 2016). This is also known as autocorrelation. One possible way that this assumption is violated is when data are collected on the same variable over time, as usually some of the data are sequenced by time and the residual plot can show any relationship between residual and time. In such cases, data transformation or specially formulated regression models can address this violation (Hair et al., 2006). When data are collected over time (time series data), then the test for autocorrelation should not be neglected. One way to test for autocorrelation is to use the Durbin-Watson test. However, this test is not appropriate for the present study as the data panel data rather than time series data.

Correlation & Multicollinearity

Multicollinearity appears when two or more independent variables are correlated with each other (Hair et al., 2006). It is very important to determine any multicollinearity in the data before the multivariate analysis is conducted, to identify the relationship between the independent and dependent variables (Hair et al., 2006). For this purpose, two tests are conducted to verify the possibility of multicollinearity in the data. The tests include the analysis of the correlation coefficients as in Tables 18 and 19 and analysis of the variance analysis factor (VIF) in Table 20.

Table 18 : Pearson Correlation for GCGDS

	GCGDS	ADOPT	EEO	ECO	PS	LE	FP	SGR	CSC
GCGDS	1								
ADOPT	0.1273	1							
EEO	-0.1098	-0.1158	1						
ECO	0.0148	0.0605	0.0374	1					
PS	0.0447	-0.0482	0.5912***	-0.0124	1				
LE	0.3784***	-0.0087	0.2557**	0.1588	0.1394	1			
FP	0.3198***	-0.0073	0.2745**	0.1552	0.2359**	0.7337***	1		
SGR	0.2437	-0.0824	0.1535	0.2216**	0.1826*	0.3597***	0.3587***	1	
CSC	0.4161***	0.1782*	-0.0859	0.223**	0.0803	0.5191***	0.4431***	0.6018***	1

Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)
 Variables definitions and measurements are the same as summarised in Table 4
 *, ** and *** indicate significance at .1, .05, and .01 respectively

Using the correlation coefficients to identify any multicollinearity, a conclusion can be drawn about the fit of the independent variables. According to Hair et al. (2006), the high coefficient of correlation matrix can be 0.9 or higher. Using this role and analysing the correlation coefficients in the matrix in Table 6 and Table 7 for the GCG disclosure and CSR disclosure scores, it can be concluded that there is no multicollinearity among the independent variables. The highest correlation coefficient is 0.7337 and all other coefficients are considerably lower than this. In fact, most of the correlation coefficients in the matrix score below 0.5, with the exception of three coefficients: 0.608 correlating SGR and CSC, 0.7337 correlating LE and FP, and 0.5912 correlating EEO and PS. Besides those three variables, all other variables have a correlation coefficient of less than 0.5. As most of the variables' correlation coefficients are less than 0.5, there is no possibility of extreme multicollinearity.

Table 19 :Pearson Correlation for CSRDS

	CSRDS	ADOPT	EEO	ECO	PS	LE	FP	SGR	CSC
CSRDS	1								
ADOPT	0.0629	1							
EEO	-0.0434	-0.1158	1						
ECO	0.0225	0.0605	0.0374	1					
PS	0.1163	-0.0482	0.5912*	-0.0124	1				
LE	0.3614*	-0.0087	0.2557**	0.1588	0.1394	1			
FP	0.3729*	-0.0073	0.2745**	0.1552	0.2359**	0.7337*	1		
SGR	0.2685**	-0.0824	0.1535	0.2216**	0.1826*	0.3597*	0.3587*	1	
CSC	0.4273*	0.1782*	-0.0859	0.223**	0.0803	0.5191*	0.4431*	0.6018*	1

Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)
Variables definitions and measurements are the same as summarised in Table 4
*,** and *** indicate significance at .1, .05, and .01 respectively

However, the correlation coefficients can identify the relationship between only two variables, and according to Hair et al. (2006), this does not guarantee the existence of multicollinearity between variables. Therefore, a VIF test must also be conducted to identify the possibility of any multicollinearity between all variables together. VIF measures the multicollinearity by inverting the tolerance value. Tolerance is calculated by 1.0 minus R-squared of the regression that is analysed without the selected independent variable. VIF is calculated by dividing 1 with the tolerance value. This means that high VIF values indicate high multicollinearity. The VIF values presented in the model are listed in Table 20. Column I relates to the model that tests the determinants of accounting standards adoption, and column II relates to the model that tests the consequences of adopting accounting standards. The results presented in Table 20 are lower than three for all variables. The average VIF for all variables in column II is 1.98. This indicates that there is no multicollinearity between the independent variables in the models, as according to Hair et al. (2006), a VIF value higher than 10 indicates multicollinearity.

Table 20 :VIF for Explanatory Variables

ADOPT	VIF
IFRS	1.79
Local	1.66
EEO	1.9
ECO	1.11
PS	1.82
LE	2.7
FP	2.41
1. CSC	2.53
1. SGR	1.88
Average	1.98

Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3) Variables definitions and measurements are the same as summarised in Table 4
*, ** and *** indicate significance at .1, .05, and .01 respectively.

7.3.3 Multivariate analysis

In this section, the results of the multivariate analysis are discussed. Tables 21 and 22 present the results of the analysis for the CG disclosure model and the CSR disclosure model.

Corporate Governance Disclosure including the CSRD has two main approaches, as previously discussed in the literature; one approach investigates the determinants of disclosure (e.g. Aribi & Gao, 2012; El-Halaby & Hussainey, 2015), and the second approach discusses the effects of improving disclosure (see for example Leuz & Wysocki [2016] who discuss in detail the possible effects of improving disclosure at micro and macro level). From the reviewed literature in this paper, it is possible to conclude that improving disclosure in a country can significantly impact its economy by improving market liquidity (Daske et al., 2008; Christensen et al., 2013; Hail & Leuz, 2007).

In the current research, the focus is to find out the association between the adoption of accounting standards in IBI and the disclosure scores in the country. Tables 21 and 22 above confirm that this association exists. This association confirmation is consistent with ED theory (Cooke & Wallace, 1990). In their study, Cooke and Wallace (1990) confirm that disclosure can be impacted by many other accounting and non-accounting variables in a country. As illustrated in Tables 21 and 22, there are many factors which can potentially affect disclosure; some are external, such as the openness to the economy, while others are internal, such as political stability, level of education, and the financial press in the country. Other variables are related to the enforcement mechanisms in the country, and the results

show that these factors are significantly associated with the disclosure score. This is also consistent with the institutions of accounting framework devised by Pope and McLeay (2001), which states that adoption of accounting standards is one of the factors which impacts the accounting quality of a country.

There are two types of research that confirm such a link. Several studies investigate how the application of one accounting standard can affect disclosure in financial statements (e.g. Fields et al., 2001; Holthausen & Leftwich, 1983; Kothari, 2001; Watts & Zimmerman, 1986). These studies confirm that there is a possible link between accounting standards and disclosure practices. Other studies investigate the link between disclosure and institutions; for example, Atanassova (2008) found that after switching to IFRS, the Bulgarian banks improved the quality of their disclosure. Verriest et al. (2010) compared adoptions of IFRS to GAAP, and found that disclosure was improved as long as the firm had a strong corporate governance policies. The analysis and discussion below add new results to the literature in the IBI context.

Corporate governance Analysis

After reviewing many definitions of corporate governance, Brickley and Zimmerman (2010) suggest using a broad one: “we find the following very broad definition particularly useful: corporate governance is the system of laws, regulations, institutions, markets, contracts, and corporate policies and procedures (such as the internal control system, policy manuals, and budgets) that direct and influence the actions of the top-level decision makers in the corporation (shareholders, boards, and executives)” (p.236).

Table 21 : Regression Result for GCGDS & CSRDS when Adopting AAOIFI/Local

	Column 1	Column 2
ADOPT	GCGDS	CSRDS
AAOIFI	13.29015 (2.41)***	1.81812 (3.47)***
LOCAL	17.29371 (3.96)***	2.027268 (4.98)***
EEO	-0.1490357 (-2.61)***	-0.01328 (2.77)***
ECO	-0.5668895 (-0.65)	-0.0612 (-0.7)
PS	7.712245 (2.96)***	0.904575 (3.89)***
LE	0.4410758 (2.36)***	0.034198 (1.74)*
FP	0.0021902 (1.03)	0.000518 (2.2)**
1. CSC	13.61567 (2.78)***	1.631346 (3.05)***
1. SGR	-6.950385 (-1.42)	-1.13895 (2.32)***
_cons	31.71373 (4.02)	2.766543 (4.7)
N	73	73
F	13.4	21.14
Prob > F	0.000	0.000
R-squared	0.4528	0.5196
Adj R-squared	.3746	.45100
Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3) Variables definitions and measurements are the same as summarised in Table 4 **, ** and *** indicate significance at .1, .05, and .01 respectively.		

Table 21 shows the results of two models estimating the relationship between CGDs and CSRDS, and the possible factors affecting those two disclosure scores. The two models estimated by the robust OLS method are clustered by country. Column 1 represents the results for corporate governance disclosure score in relation to the possible associated factors. The results show the existence of association between countries adopting AAOIFI in relation to countries adopting IFRS standards and the CGDs in the country. As the positive coefficient of AAOIFI countries (13.29015) is significant at the 1% level of significance and a t value of 2.41, H8 (accounting standards adopted in the country can improve CG disclosure) is supported. Similarly, the results show that countries adopting local standards also have positive coefficient (17.29371) at the 1% level of significance and with a t value of 3.96, indicating the existence of an association between the countries adopting local standards in

relation to countries adopting IFRS with the CGDs in the country. This result is supported by H8 and also consistent with previous studies such as North (1990), who noted that accounting is an institution that helps to facilitate more complex transactions in an economy.

This result suggests that adopting accounting standards is associated with a country's disclosure practices. The adoption of one set of accounting standards can either improve or worsen the disclosure practices in a country as a whole.

Hence, improving disclosure practices in a country can have an impact on the economy at the macro level as well as the micro level (Leuz & Wysocki, 2016). It is also possible to conclude that the adoption of certain accounting standards can also improve the economy of the country (Mueller, 1986). These two conclusions regarding standards adoption and disclosure can also be true for adopting accounting standards in IBI; hence, it is possible to conclude that accounting standards adopted in IBI are linked to disclosure improvement, leading to many favourable economic consequences in the market. Examples of these favourable consequences include reducing information asymmetry (Bushman et al., 2004), increasing transparency (Baydoun et al., 2013), reducing the cost of capital (Botosan, 1997; Sengupta & Zhang, 2015), increasing market liquidity (Helay et al., 1999), as well as other capital market effects (Leuz & Wysocki, 2016).

Baydoun et al. (2013) emphasise the need for local standards in the Gulf countries, and argue that the absence of local accounting standards in these countries affects corporate governance disclosure leading to a lack of transparency in the country. This result is consistent with the current study as there is an association between accounting standards adoption and disclosure in the chosen countries, leading to better transparency. The results are also in accordance with EDT, as accounting standards are an important institution that can affect accounting quality.

Table 22 shows that in countries adopting IFRS, there is a negative association with GCGD compared to those adopting AAOIFI. The data in column 1 of Table 22 shows that the adoption of IFRS is negatively associated with GCGD with a 1% significance of association, a coefficient of -13.29015, and a t value of -2.41. The negative sign of IFRS adoption compared with AAOIFI adoption can be justified by the average GCGD score for countries adopting IFRS compared to the GCGD scores of countries adopting AAOIFI. The average GCGDs in Table 18 show that countries who adopt AAOIFI disclose more corporate governance items than countries adopting IFRS. This result indicates that the adoption of

Table 22 : Regression Result for GCGDS & CSRDS when Adopting IFRS/Local

ADOPT	Column 1	Column 2
	GCGDS	CSRDS
IFRS	-13.29015	-1.81812
	(-2.41)***	(-3.47)***
Local	4.003559	0.209147
	(0.69)	(0.34)
EEO	-0.1490357	-0.01328
	(-2.61)***	(2.77)***
ECO	-0.5668895	-0.0612
	(-0.65)	(-0.7)
PS	7.712245	0.904575
	(2.96)***	(3.89)***
LE	0.4410758	0.034198
	(2.36)***	(1.74)*
FP	0.0021902	0.000518
	(1.03)	(2.2)**
1. CSC	13.61567	1.631346
	(2.78)***	(3.05)***
1. SGR	-6.950385	-1.13895
	(-1.42)	(2.32)***
_cons	45.00388	4.584663
	(4.79)	(5.93)
N	73	73
F	13.4	21.14
Prob > F	0.000	0.000
R-squared	0.4528	0.5196
Adj R-squared	.3746	.45100
Dependent variable is Adoption of AAOIFI coded (1) IFRS coded (2) and Local coded (3)		
Variables definitions and measurements are the same as summarised in Table 4		
*, ** and *** indicate significance at .1, .05, .01 respectively		

AAOIFI accounting standards can increase corporate governance disclosure to a greater extent than IFRS in IBI. Literature investigating compliance with corporate governance in Islamic banks does not generally compare between those banks adopting AAOIFI, IFRS or local standards, but instead measure how much the banks disclose compared to the designed checklist (see Abdullah et al., (2015), or investigate the differences in corporate governance for IFIs across countries (e.g. Baydoun et al., 2013; Grassa & Matoussi, 2014).

Tables 21 and 22 confirm that there is an association between disclosure and adoption of accounting standards in IBI. However, it was not clear which set of accounting standards promotes disclosure more, on average.

The results in Tables 21, 22 and 11, 12 and 13 (scores for CG and CSR disclosre at country level) are considered to be an addition to the literature of corporate governance for Islamic

banks and are consistent with the findings of Grassa and Matoussi (2014). The results confirm that culture, economic, and social contexts are linked to the corporate governance system in Islamic banks and countries by extension.

The results shown in the above tables show that an association does exist between the adoption of accounting standards and disclosure of corporate governance in Islamic banks. In addition, the same tables also report an association between corporate governance disclosure and other factors such as enforcement regulations/bodies, or internal factors such as political stability or level of education in the country. This result is considered an addition to the corporate governance literature as well as providing the first empirical examination of this specific topic. This research suggests that corporate governance disclosure is linked to many other accounting and non-accounting variables, which need to be considered when working to enhance corporate governance disclosure or the corporate governance system in Islamic banks either at the bank or country level.

Surprisingly, the second variable showing as a significant coefficient is the EEO, as the coefficient is negative for this variable, indicating that CGDS is associated negatively with the openness of economy in the country. Considering that this variable is introduced in the model as control variable, it appears that EEO has an association at the 1% level of significance with disclosure scores in IBI. A negative sign in this model for the EEO variable is not expected. However, in IBI, this result can be justified as the main purpose of disclosing information in this industry; not to globalise, but to be compliant with Sharia (AAOIFI, 2010). Therefore, there are countries which do not strive for globalisation yet still disclose more in order to be Sharia compliant. On the other hand, some countries are more globalised but do not disclose as much as other countries in IBI. This result also indicates that even emerged economy countries can have higher disclosure for Sharia purposes as well as for preferred economic consequences at both the macro and micro level. One example of these countries is Oman, where the highest disclosure score of 56.286 was recorded in 2013 for GCGD, and 7.571 for CSRD in 2014. The disclosure score in Oman confirms that disclosure is driven by other factors in IBI, such as the Sharia compliance regulations in the country. Aribi and Gao (2012) confirm that the CSRD disclosure in IFI is related to SSB requirements, which means it is related to religion or Sharia requirements to a greater extent than any other determinants. The results confirm that even in countries with less openness to economy, levels of disclosure can still be high.

The third variable that shows significance in the model is political stability (PS). The positive coefficient of PS scored 7.712245 with a t value of 2.96, significant at the 1% level of significance. This indicates a very strong positive association between political stability in the country and the CG disclosure score. In other words, political stability can be a factor associated with disclosure score changes in IBI (Solomons, 1978). The significant association between disclosure score and political stability addresses the importance of non-accounting institutions' impact on the accounting quality of a country. In addition, political stability will ensure many businesses survive and grow, and corporations often prefer to operate in countries with stricter financial reporting regimes to enjoy better financing from different finance organisations (Leuz & Wysocki, 2016). Thus, many companies go for cross listing, especially those from emerging economies.

Soderstrom and Sun (2007) emphasise that the legal and political systems in any country are the main determinants for accounting quality in the country. For example, they explain that legal and political systems can affect earnings quality indirectly through ownership structures. This suggests that there is a link between the disclosure score of governance and political stability as an institutional factor in the country. This result is consistent with EDT, which emphasises the role of political stability in accounting quality.

The fourth variable associated with CGDs is level of education (LE), as the positive coefficient of 0.4410758 with a t value of 2.36 is associated at the 1% level of significance with CGDs. This result presents that a country's LE is one possible factor affecting the CGD practices in the country.

Level of education has been investigated before in the literature as a main determinant for the accounting quality in a country (see for example La Porta, 1998-2007). Douppnik and Salter (1995) also consider LE in their framework as important factor which can affect the accounting quality of a country. Furthermore, Schultz and Lopez (2001) investigate the impact of national influence on judgements made by accountants in France, Germany, and the United States. Level of education in these studies by La Porta (1998-2007), Douppnik and Salter (1995) and Schultz and Lopez (2001) is regarded as one of the main institutional environment variables that can affect accounting quality. The results shown in Tables 21 and 22 indicate the significance of LE in countries allowing Islamic finance as a possible factor associated with the disclosure score. This implies that increasing the number of institutions offering Islamic finance courses in a country can have an impact on accounting quality in

general, and disclosure particularly. Increasing the number of institutions offering Islamic finance courses will help to provide well-educated human resources who can practice the principles of Islamic finance along with the financial principles. Well-trained employees in the Islamic finance field can also help to apply disclosure policies along with Sharia accounting principles. A study carried out by Al Akra et al. (2009) highlights the importance of the education system in Jordan, and the quality of accounting education in the adoption of certain accounting standards. EDT further supports this result, as it clearly indicates that the level of education in a country impacts accounting quality.

The fifth variable with significant results in the model is the existence of a centralised Sharia committee. The positive coefficient of the CSC variable (13.61567) with a t value of 2.78 indicates that the existence of a Sharia committee in a country is associated with a CG disclosure score 13.61 times higher than countries without a CSC. This result suggests there is an important link between CSC and the encouragement of disclosure practices in IBI.

Results obtained by Abdullah et al. (2015) show that the mean of voluntary disclosure is less than 40%. This indicates that the stronger the corporate governance regulation, the greater the voluntary disclosure of the bank. In other words, the existence of corporate governance and its application in Islamic banks are associated with the volume of disclosure. In their paper, the authors emphasise the role of the Sharia Supervisory Board (SSB) as an important element that strengthens Sharia governance in Islamic banks. The SSB is a main governance body which every Islamic bank must have. An SSB requires at least three Islamic scholars who specialise in Sharia in general, but they should also be qualified in Islamic jurisprudence (AAOIFI, 2007).

Investors and depositors rely heavily on the SSB to make sure that they invest in accordance with Sharia. This result is consistent with the findings in Tables 15 and 16, which show that the GCGD is associated with the existence of Sharia governance regulations in the country. This implies that the Sharia enforcement bodies required by the Sharia governance regulations take important roles in improving disclosure practices in Islamic banks. It also highlights the importance of other committees besides Sharia enforcement bodies, such as audit and financial committees, in Islamic banks to further improve disclosure practices. Moreover, there is a need for enforcement bodies to have some degree of monitoring power to ensure all legal and financial transactions are conducted according to Sharia, as well as the power to enforce penalties when the regulations are not followed. Effective enforcement regulations are

required to generate hopeful outcomes as a result of having enforcement regulations and enforcement bodies (Nobes & Parker, 2012). Another main role for Sharia governance bodies like the Sharia Supervisory Board (SSB) is to provide consultation to the IFIs (Grassa, 2013).

Corporate Social Responsibilities Disclosure (CSR)

The CSR regression results are presented in column 2 in Tables 21 and 22. The results are similar to the CGDs regression, in that the AAOIFI and local standards adoption are more positively associated with CSR than IFRS. Table 21, column 2 shows that AAOIFI and local coefficients (t values) are 1.818 (3.47) and 2.02 (4.98), respectively. These values represent the possible association between accounting institutions' adoption of AAOIFI and local standards in IBI and the disclosure score for CSR in the country. Both coefficients are significant at the 1% level of significance; it is also clear from the t values that there is a strong association between adoption and disclosure score. This result is consistent with H9, which states that there is an association between adoption of accounting standards and CSR score. This is also in agreement with Belkaoui (1983). In addition, El-Halaby and Hussainey (2015) found that bank size, accounting standards, the existence of a Sharia auditing department, GDP growth, and auditor type are all positively associated with CSR. Van der Laan Smith et al. (2014) found that firms in countries with shareholder orientation, such as the UK and Australia, experienced a significant increase in CSR after the adoption of IFRS. The findings of Van der Laan Smith et al. (2014) suggest that the mandatory adoption of accounting standards can affect the CSR disclosure of firms considering institutional environments. Besar et al. (2009) also came to the same conclusion regarding the effect accounting standards adoption has on CSR practices.

The results in column 2 of Tables 21 and 22 demonstrate that accounting standards are associated with CSR, which is consistent with the findings of El-Halaby and Hussainey (2015), Van der Laan Smith et al. (2014), and Besar et al. (2009) whose results all confirm the association between accounting standards adoption and CSR score in the Islamic banks investigated. It is also consistent with EDT, which suggests that the accounting quality of a country is determined by many factors including the type of accounting standards adopted.

Column 2 of Table 16 presents the association between IFRS adoption, AAOIFI adoption and CSR score. The coefficient of -1.818 with a t value of -3.47 suggests that there is a

significant negative association between CSR score and adoption of IFRS in comparison to AAOIFI.

In terms of CSR score for countries adopting local standards, column 2 in Table 22 does not show any association between the two variables. This is likely to be because the average CSR score for countries adopting AAOIFI and local standards are almost the same. This can be seen in Table 11 and 12, where the CSR score for AAOIFI is 3.202 and for local standards is 3.247.

The second variable in the regression model for CSR showing an association with disclosure is EEO. The results show that the coefficient is significant at the 1% level of significance, with a t value of 2.77. The negative coefficient of EEO suggests that the relationship between the adoption of accounting standards and disclosure score for CSR in IBI is negative. This result reveals that most countries disclosing more in CSR do not enjoy improved export and import activities. This can be understood to mean that in the IBI industry, the main aim of CSR disclosure is Sharia compliance rather than globalisation.

The results of a study by Aribi and Gao (2012) confirm the role of the Sharia governance system as main determinants for disclosure practices in IFIs. Their results demonstrate that the CSR score of a country is associated with their Sharia governance system, and they emphasise the role of SSB as main determinants for CSR considering the importance of Sharia compliance in the IFI.

El-Halaby and Hussainey (2015) found GDP growth to be one of the country level factors associated with CSR. In their study, the authors investigated economic growth as a control variable when investigating the association between CSR in Islamic banks and bank level characteristics. The results of the research shows that GDP is a significant factor associated with CSR score. El-Halaby and Hussainey's (2015) result disagrees with the result of the current study, as the analysis in Tables 21 and 22 does not show any association between CSR and economic growth. The two results are inconsistent with each other, however it is worth bearing in mind that this study is conducted at country level while theirs was carried out at bank level.

Political stability is the third variable which shows a positive significant coefficient with CSRs. PS's coefficient of 0.904575 and t value of 3.89 is also significant at the 1% level of

significance, and a positive association indicates that an increase in political stability is potentially linked to an increase in CSRD.

This result is consistent with EDT, as it highlights political stability as an important internal factor that can affect the accounting quality of a country. The result also correlates with existing literature; Belkaoui (1983, 1985) argues that democracy in the political system encourages democracy in accounting. Therefore, it is possible to conclude that accounting quality is linked with the political system as well. Purjalali and Meek (1995) confirm the role of the political environment in changing the accounting system in Iran, as the Iranian revolution 1979 was a major factor in changing the country's finance and accounting systems. This further suggests that, for IFIs, political stability is an important institutional factor associated with accounting quality in general and disclosure practices in particular.

The fifth variable indicating an association between CSRD and other institutional factors is the level of education in the country. LE has a positive coefficient of 0.034198 and t value of 1.74, and is significant at a 10% level of significance. This institutional variable shows a weak positive association between CSRD and the level of education in a country. In other words, the increase in LE is associated with a 0.034 increase in CSRD. This result is consistent with EDT, as level of education is one institutional factor that can affect the disclosure score and accounting quality in the country in general (Cooke & Wallace, 1990).

El-Halaby and Hussainey (2015) also controlled for the level of education in their study, and found that there is no association between the level of education and CSRD. This is inconsistent with the results presented in Tables 21 and 22 of the present research, where analysis shows that there is an association between the level of education and CSRD at the country level. The inconsistency of the results between this study and El-Halaby and Hussainey's (2015) is most likely due to the different measures used in the two studies; this study uses the number of institutions offering Islamic finance courses in a country to measure the level of education, unlike El-Halaby and Hussainey (2015) who use the literacy rate as a measure for the level of education.

The association between CSRD and the level of education in the country can imply a number of things, such as the important roles colleges, universities and institutions have in positively affecting disclosure practices in Islamic banks. This is especially true if a country's education

includes courses in applying accounting standards, auditing Islamic banks, or supervising for Shari compliance.

The sixth variable in the CSRD regression model which shows an association between the dependent and independent variable is financial press (FP). In contrast to the CGD model, this variable is significant in the CSRD model at a 5% level of significance. The FP coefficient is positive and shows that the news items and articles in a country are potentially associated with CSRD. The FP coefficient of 0.000518 and a t value of 2.2 is very small; however, if it is calculated for the average Islamic news items and articles concerning Islamic banking over a year, then it can be a powerful institution variable affecting CSRDs in the country. The role of the media has been discussed before as a main corporate governance factor (see for example Dyck, 2002, 2003, 2007). The association between CSRD and financial press represents the importance of institutional environmental factors in accounting quality, as suggested by EDT (Cooke & Wallace, 1990). EDT confirms the importance of the financial press as an institutional factor which can affect the disclosure score of organisations. The importance of the institutional environment is also confirmed by Wysocki (2011) and Leuz and Wysocki (2016). The findings of the extant literature is consistent with the results presented in Tables 21 and 22 – it can thus be concluded that FP as control variable can affect CSRD in the country. This implies that the conferences, events, and news items concerning Islamic finance can increase awareness about the benefits of Islamic finance through the application of Sharia principles, including practicing social responsibilities towards society and disclosing each of these activities in the annual reports.

The other two variables in the CSRD model that show significance are the enforcement type of institutions; namely, the existence of a centralised Sharia committee (CSC) and the existence of the Sharia Governance Regulations (SGR) in the country. The two variables are associated at the 1% level of significance; however, CSC is associated positively with CSRD, unlike the SGR variable which is associated negatively with CSRD.

Further, Aribi and Gao (2012) emphasise that Islam can be used as an important determinant for CSR in general, as well as CSRD. Hence, corporate governance in Islam such as the SSB guides disclosure practices in Islamic IFIs. This conclusion is in agreement with the association found in Tables 21 and 22 between CSRD and CSC, as CSC and SSB are both part of the current governance system allowing Islamic finance to ensure Sharia compliance. On the other hand, Besar et al. (2009) argue that Sharia committees only satisfy the very

minimum requirements of Sharia compliance activities, and recommend installing a Sharia audit department to achieve the required CSR. In general, the studies of El-Halaby and Hussainey (2015) and Aribi and Gao (2012) confirm the importance of a Sharia governance system at country level, such as the CSC, or at bank level, such as the SAD or SSB, to both comply with Sharia and disclose more CSR items.

The existence of a SGR in the country is associated negatively with CSR; the results present the coefficient of the SGR at -1.13895, with a t value of (2.32). The negative sign shows that the existence of SGR in a country reduces CSR. However, this result can be read another way – as can be seen in Table 11, 12, 13, the disclosure score for the countries without Sharia regulation is still high compared to the average, as in Jordan, Lebanon, Saudi Arabia and Bangladesh. The CSR score for these countries in 2012 were: Jordan (4.714), Lebanon (3), Saudi Arabia (2.91667) and Bangladesh (5.18).

This indicates that even if the SGR does not exist at country level for IFIs, the Islamic banks and other IFIs still have Sharia governance regulations at bank level. This result also suggests that CSR is influenced by other institutional environment variables whether Sharia governance regulations exist or not.

After reviewing the results in column 1 and column 2 in Tables 21 and 22, as well as taking into account the results above, the conclusion can be made that the adoption of one set of accounting standards is linked to the disclosure practices in a country. The results can be generalised, as the analysis shows that this is true for countries adopting AAOIFI, local, and IFRS standards. This points to the conclusion that disclosure is associated to the adopted standards regardless of the type of standards available.

CHAPTER EIGHT: CONCLUSION

8.1 Overview

This study investigated two main objectives in the Islamic banking industry, which is still very young as a global industry and still growing. The two objectives are the determinants and consequences of adopting accounting standards in IBI. There are three types of accounting standards typically used in this industry, namely AAOIFI, IFRS, and local standards. This section presents a summary of the study's findings, where the results of the first and second objective are summarised. This chapter also discusses the different implications of the study and who it will impact in the short term as well as the long term. In addition, this section summarises the limitations of the study, and gives new ideas and insights for future research considering the use of different theories, research methodology, and different standards used in IBI.

8.2 Summary of the Findings

It is abundantly clear that all three sets of accounting standards are influenced by some of the variables applied in this study. These variables consist of internal environmental factors, such as the level of education or financial press, and enforcement mechanisms, such as the centralised Sharia committee.

The main objective of this study was not to determine the direction of the relationships, but merely to establish the presence of such relationships between the predictors and the outcomes; with this in mind, the following conclusions can be drawn: AAOIFI adoption is predominantly determined by the financial press, which implies that a change in the financial press is more likely to influence the adoption of AAOIFI in a country; IFRS adoption is predominantly influenced by three environmental factors: political stability, financial press, and the existence of a centralised Sharia committee; the adoption of local standards is predominantly influenced by two environmental factors: the level of education, and the existence of a centralised Sharia committee. These results confirm EDT in the context of

Islamic banking, as environmental factors significantly affect the adoption of accounting standards.

Given that all of the significant determinants of accounting standards are either internal environmental factors or enforcement mechanisms, this implies that the internal social environment of the countries as well as enforcement mechanisms can influence the strategic decision of adopting accounting standards. The results also imply that accounting is not universal, and it is dependent on its environment. Therefore, to achieve higher quality of accounting standards, more effort is required from governments to impose the most appropriate accounting standards for their country (Cooke & Wallace, 1990). This can be achieved by increasing available training and courses in Islamic finance, as well as increasing the scope of the financial press related to Islamic finance. Another strategy to improve accounting quality through adopting the most appropriate accounting standards is to establish effective enforcement mechanisms, such as corporate governance regulations and supervisory regulations.

In regard to the outcomes of adopting different accounting standards in IBI, the disclosure score of a country is associated with both accounting and non-accounting institutions. Those institutions are either internal factors, such as level of education and financial press, or they are enforcement mechanisms, such as a centralised Sharia committee. Moreover, the adoption of certain accounting standards is also associated with the disclosure score in the country. This result, as previously discussed by Wysocki (2011), indicates that both accounting and non-accounting institutions are interdependent. The main objective of this study was not to investigate the direction of the relation, only to identify the presence of an association between the predictors of accounting and non-accounting institutions and the outcomes (CG and CSR disclosure) in IBI; therefore, the following conclusions can be drawn from the results of the analysis.

CG disclosure is significantly associated with the adoption of accounting standards in a country. CSR disclosure also exhibits an association with all other non-accounting variables in the model, including external economic openness, political stability, level of education, financial press, and enforcement mechanisms (e.g. centralised Sharia committee and the existence of Sharia governance in the country). The results also indicate that CG disclosure is associated with other non-accounting institutions as well, mainly external economic openness (EEO), political stability (PS), level of education (LE), and enforcement mechanisms in the

country such as a centralised Sharia committee. CSR disclosure also shows a strong association with the adopted accounting standards, whether AAOIFI, IFRS or local standards.

The results of this study highlight the role of environmental institutions in the country in relation to accounting quality in general, and in the accounting standards adoption decision and disclosure practices. The results also indicate that EDT shows the same results in the IBI context. In other words, both accounting and non-accounting institutions are linked to the accounting practices of a country, whether in terms of adoption decision or disclosure practices. It is not possible to falsify EDT using these results either, thus it can be confirmed that EDT is valid in the context of Islamic banking.

In regard to analysing the results, even though the study is conducted at country level where some of the country differences are controlled for such as: GDP, openness to economy and it is very important not to ignore the possible influence of other different variables in the result. The discussion below highlights some possible factors which possible led the result to be as presented in the previous chapters. All these variables can play a role in explaining the different results between countries adopting AAOIFI, IFRS and LOCAL standards. It also can explain the differences of the CG and the CSR disclosure scores reported for the different countries adopting AAOIFI, IFRS and Local. Referring to Tables, 11,12,13 the CG scores and the CSR scores are varying where IFRS countries are recording the less scores for CG with (20.6629) and (1.870349) for the CSR. While AAOIFI countries have an average CG score of (30.1683) and (3.202678) for CSR. Countries with LOCAL accounting standards scored the top average CG score of (33.70536) and CSR average score of (3.247223).

A) The role of other human and non-human factors

In the previous explanation about EDT it was highlighted that the EDT in its final version suggest also that there is a role for the human variables as possible influence (Haniffa and Cooke, 2002). The different variables of human and non-human factors, as introduced by Haniffa and Cooke (2002), represent the corporate characteristics of the firm as well as its management attitude.

B) The role of the culture

The role of culture in explaining the differences in the accounting practices is debatable. It is also debate able how to measure culture in countries and whether developed and developing

countries can use the same measure for culture. For example Nobes, (1998) admit that culture is a possible factor which can work as a background to drive changes in the other causes factors for the difference (e.g. finance system) in accounting system. However, he agree with (Gernon and Wallace, 1995; Baydoun and Willett, 1995) that using culture as direct variable for causes of accounting system differences is problematic as the mechanism of the effects are not clear.

It is true also that culture in each country can be affected by the colonial or former colonial therefore culture changes can be explained by another factor which is the colonial history. Taking the colonial history and the culture of country in consideration this lead Nobes, 1998 to classify the countries in two groups: the culturally self-sufficient (CS) and the culturally dominated (CD). Nobes identified the culture of the developed countries as more CS while the culture in the developing countries as more (CD). After the classification of culture in both developing countries as well as the developed countries Nobes, 1998 suggests that researchers should concentrates in using related business culture instead of the general culture in the country. This according to Nobes, (1998) does emphasise that this factor is less important in explaining the international accounting system differences in developed countries. However in developing countries, Nobes, (1998) confirm that this factor can be important as the environment in the developing countries is totally different.

The culture factor in this study is captured by the discussion of the enforcement mechanisms for the financial reporting practices in the countries as in (Gernon and Wallace, 1995; Baydoun and Willett, 1995 and Nobes, 1998). Nobes, 1998 confirm that other factors such as political system, stage of economic development and religion can be of significant to explain the differences in countries other than the developed countries. For example (Gambling and Abdel-Karim, 1991; Hamid et al., 1993) confirm also that religion is one of the factors related to the differences in the accounting systems.

C) The adoption is for labelling purposes

In addition, the differences appearing if the country is adopting the accounting standard fully in practice or it is adopting it for labelling purposes only. Studying the Malaysian adoption of IFRS in IFIs reveal that after the adoption the IFIs still need a lot of guidance and clarification how IFRS can be applied to a Sharia compliance business. The effort to issue this guidance and the effort to adjust the IFIs financial accounts after they are produced in

IFRS to match the regulatory agencies in the country such as the (Central banks) make (Mukhlisin, 2016) suggests that some adoptions are for labelling purposes.

8.3 Research Implications

There are two possible approaches this research can take: practical and theoretical implications.

In terms of the theoretical implications, this study raises several implications related to testing the EDT theory applied in the research. To the researcher's best knowledge, this study is the first to apply EDT in an Islamic context. In addition, this research is the first to attempt to falsify the theory in order to confirm or reject it. The research hypothesis was designed to test the reality in the Islamic environment across the sampled countries. This research investigated enforcement mechanisms as determinants for the adoption of accounting standards in IBI; for the first time in Islamic finance literature, an association was found between Sharia enforcement mechanisms and strategic decisions made in a country, such as the adoption of accounting standards in the IBI. In addition, this research is also one of only a few attempting to investigate the direct link between accounting standards adoption and improvement in a country's corporate governance disclosure, as well as the CSR disclosure as a whole. Regarding the methodology, the use of MNL to compare between the determinants of the accounting standards adoption and the consequences of this adoption helped to accomplish the comparison objective using the same model. This implies that using the right statistical tool in the analysis can contribute to the study and explain the research objectives as planned. MNL has been used previously in accounting literature; however, it has been used here for the first time to investigate the determinants of accounting standards adoption.

With regard to the practical implications, this research can benefit a wide range of stakeholders across many countries. The first organisation to benefit from the research is AAOIFI, as this research provides information regarding the countries which have adopted AAOIFI standards. This information is not currently available within the AAOIFI organisation, as confirmed by the company's financial assistant, Mr. Khaled Al-Sheik, during our interview in August 2015. This study also discusses the determinants of AAOIFI standards adoption, and such information can be used by AAOIFI to market their standards to other countries. It can also be of help in developing a plan to initiate and introduce AAOIFI

standards as an option to improve disclosure, transparency and reduce information asymmetry among IFIs.

Identification of the determinants and consequences of using specific accounting standards is also beneficial to new IFIs, as this information gives the IFIs the ability to compare between the available options. The case is true for all IFIs that wish to change their accounting regime, as this research highlights the possible link between the adoption of accounting standards and disclosure score. This can also help IFIs in countries allowing voluntary adoption of different accounting regimes in their Islamic financial institutions, as they can evaluate and choose according to their specific needs.

Increasing disclosure impacts many areas at both the macro and micro level in a country, as discussed in section 4.5. The existence of this association is also important to many entities in the country such as Islamic banks, governments, investors, creditors and scholars.

8.3.1 Islamic Banks

Islamic banks will be affected differently depending on which accounting regime they decide to adopt. For example, their cost of capital, value relevance and information asymmetry may be affected, a fact which has been proven by research in these areas.

According to economic theory, there is a link between a firm's disclosure of more information and their cost of capital. Increased disclosure potentially reduces information asymmetry through reducing reverse selection. Reverse selection occurs, as explained by Leuz and Wysocky (2011, p.28), when "...uninformed or less informed investors have to worry about trading with privately or better informed investors. As a result, uninformed investors either price protect or exit the market to minimize possible losses from trading with informed counterparties. These actions reduce the liquidity of share markets, i.e., ability to quickly buy or sell shares at low cost and with little price impact. Corporate disclosure and reporting can mitigate the adverse selection problem and increase market liquidity by levelling the playing field among investors" (see also Verrecchia, 2001).

Another possible effect of increased disclosure, as suggested by economic theory, is that increased disclosure can reduce information asymmetries between shareholders and their firms as well as the potential buyers and sellers of the firm's shares. Reducing information asymmetries possibly reduces issuing capital at discount, which in turn lowers the cost of

issuing capital (Leuz & Verrecchia, 2000). Firms typically issue capital at discount to overcome the reluctance of potential investors to hold firms' shares in illiquid market. According to Leuz and Verrecchia (2000), discounting results in fewer proceeds to the firm which leads to the higher cost of capital.

8.3.2 Governments

Other than Islamic banks, governments can also find the association between accounting standards adoption and disclosure score for the Islamic banks a core issue. This is especially true if the government has an interest in changing the accounting regime in IBI. If governments are fully informed about the associations between certain accounting standards and increased disclosure in the country, they are then able to make better decisions regarding the selection of the most appropriate standards for their country. Most governments aim to increase investors' protections, especially the emerging market countries.

Governments also tend to look to increase market liquidity, and this research can help the government to see how the accounting standards could possibly affect (increase or decrease) market liquidity in the country. Similar studies have investigated the possible effects of adoption on market liquidity, such as Daske et al. (2013), who reported that mandatory adoption in countries seriously adopting IFRS (actually applying IFRS) as opposed to label adopters (not fully applying IFRS) do experience an increase in liquidity.

8.3.3 Investors

Existing investors may also benefit from this study, as they are able to evaluate whether their current investments are in countries which disclose more information or less. This can help them to decide whether or not to continue their investment in the same environment. Potential investors also have an interest in which countries disclose more information than others, as this can help them decide the best place to direct their investment. Comparing disclosure scores between countries with different accounting regimes can help them identify where to invest, considering the need for higher levels of disclosure. More disclosure can also lead to more understanding of financial statements which improve the decision usefulness as a result (Scott, 2012).

8.3.4 Creditors

Creditors can have a very high level of interest in which accounting regimes lead to increased disclosure, as this information can be used to make lending decisions for Islamic banks. Kosi (2010) investigated the link between changing accounting regime and credit relevance in 14 European countries. The studied countries include: Austria, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and UK. He concluded that there was an increased credit relevance of profitability for mandatory adopters from countries with strong creditor protection.

8.4 Research limitations and suggestion for future research

8.4.1 Limitations

One limitation of this study is that it has a small sample size (10 countries adopting each standard), which has restricted the model from investigate more environmental variables. Other variables, such as the existence of industry framework, the existence of accounting regulations, culture, and colonial history, were not considered in this study either due to multicollinearity or data unavailability. Another limitation of this study is the availability of disclosure scores at country level over the long term. Zawya only offers this information for the last four years, which consequently meant that the study was restricted to a three-year period. These limitations can be an area of interest for future research, as more information will be available in the coming years relating to Islamic finance at the country level.

8.4.2 Future Research

Conducting the Research using Other Theories

This research can be conducted in several ways using several other theories, for example using isomorphism theory. The application of isomorphism theory can enable other researchers to give noble contributions, as this theory suggests that the professionals in the industry should have a role in the adoption process. Collecting information about the role of the professionals in the industry, and including an investigation of their role in the adoption of the standards, is something worth considering for future research.

Another theory which could be considered for examining the determinants and consequences of accounting standard adoption is institutional theory; future researchers could consider other accounting and non-accounting institutions to investigate this research topic. There are many factors which could be investigated as determinants of adopting accounting standards in IBI. Many of these factors are discussed in the literature (see e.g. Pope & McLeay, 2011).

Conducting the Research using Different Methodology

Different research methods may be used to investigate the same topic at country level, as suggested by Wysocki (2010) who suggests the use of structure equation modelling when conducting the study at the country level. Another suggestion for future research is the use of the K-means to investigate the differences between the countries' institutional factors (Wysocki, 2010). In addition, this research may be conducted using a different research approach. Adopting the inductive approach in future research could help gain a deeper insight into the determinants and consequences of accounting standards adoption in IBI, as this approach allows the researcher to collect more data and design the hypothesis to build a theory instead of merely testing a certain theory, as is the case in this research.

Conducting the Research to Examine Determinants and Consequences of Other Standards (Sharia and Governance)

This research can be also conducted to examine the determinants and consequences of adopting other standards in IBI (e.g. Governance). The determinants and consequences of adopting Sharia and Governance standards have not yet been investigated. Researchers may consider researching this to enrich the literature and the Islamic finance sector with any results which may emerge from such research. As mentioned previously, researching this can help introduce new insights for improvements for many stakeholders in the industry, as well as the countries in which Islamic finance operates.

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List of Appendices

Appendix A: List of main literature for determinants of accounting standards

Authors	Country	Year	Sample	Research Instrument	Determinants examined	Industry	Findings
Panel (A) Empirical Evidence							
Trembley (1989)	U.S	Fiscal year 1986	53 Software Specialized firms		<ul style="list-style-type: none"> • Size= net sales • IBTDN= change in earning • DEBT=long term debt to total assets • Audit opinion • Ownership 	Software Specialized firms	Adoption choices usually determined by the company size and auditor's opinion
Dumontier and Raffournier (1998)	Switzerland	1994	133 nonfinancial firms	Logistic Model	<ul style="list-style-type: none"> • Size • Listing status • Internationality • Ownership structure • Leverage • Capital intensity • Profitability • Auditors reputation 	Non-financial listed companies	Absence of significant relationship between voluntary adoption of IASs, debt ratio and firm performance
Leuz and Verrechia (2000)	Germany	1998	Listed companies in DAX 100 index	Logistic regression	<ul style="list-style-type: none"> • Firm size • Financing needs • Financial performance 	German firms that have switched from German to international reporting (IAS or U.S GAAP)	Results shows that firm size, financing needs and financial performance significantly explain the decision of adopting the IAS.
Omneya,	Egypt	Year	72 non-		<ul style="list-style-type: none"> • Language 	Non-financial	Lower

Abd Elsalam, and Weetman (2003)		end 1995	financial listed local companies			effect	listed companies	compliance and lower disclosure level when the translation to Arabic of the requirement s is not available
Zeghal and Mhedhbi (2006)	Developing countries	2003	Compared between 32 developing countries adopted the IFRS and 32 developing countries have not adopted them	Logistic regression		<ul style="list-style-type: none"> • Culture • Economic growth • Exist of capital market • Educational level • The degree of external economic openness 		The developing countries with the highest literacy rates, with a capital market and Anglo American culture most likely to adopt the IAS.
Affes and Callimaci (2007)	Germany & Australia		106 German and Australian firms			<ul style="list-style-type: none"> • Firm size • Debt 		Early adoption increase with firm size and has little significant relationship with Debt
Tarca (2004)	UK, France, Germany, Japan, Australia	1999- 2000	150 largest companies(by market capitalization) in each country Total sample in all countries are = 506 companies	Binary logistic regression model used Dependent variable is the choice of US GAAP or IAS. Independent are firm attributes(Prop ortion of foreign revenue, size,		To determine to what extent which companies' use voluntary international standards (IAS/ USGAAP)	Different listed companies	Firms listed in USA regulated markets more likely to choose US GAAP. Companies traded in OTC market often select IAS

leverage,
country, stock
exchange
listing and
industry group

Zehri and Chouaibi, (2013)	Developing countries	2008-2011	74 developing countries (32 developing countries adopted IFRS and 32 countries did not adopt IFRS.	Logistic Model	<ul style="list-style-type: none"> • Culture • Economic growth • Exist of capital market • Educational level • The degree of external economic openness • Legal system • Political system 		Developing countries with high economic growth along with legal system of common law and advance educational level are most likely to adopt IAS/IFRS
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Panel (B): Discussion papers

Authors	Country	Year	Sample	Research Instrument	Determinants examined	Industry	Findings
Al Akra et al. (2009)					<ul style="list-style-type: none"> • The political and economic influences • Legal system • Taxation • Cultural influence • Religion • Business ownership and organization • The education system • International factors 		political and economic factors through privatization contributed more to the development of the accounting practices
Antonio and Mukhlisin (2013)	UK and Indonesia			Ibn Khaldoun's Model in civilization	<ul style="list-style-type: none"> • The function of government • The direction 	The Islamic Finance Industry	The main determinant in the implementat

		of Shariah	ion of
		<ul style="list-style-type: none"> • The role of people • The use of wealth • The development of country • The promotion of justice 	accounting standards for Islamic financial are mainly contributed by institutional settings in UK and accounting needs in Indonesia
Briston (1978)	Indonesia		The adoption of the accounting standards in Indonesia is due to the needs of the country.
Cooke and Wallace (1990)	21 countries (12 developed and 9 developing)		Factors influencing the IAS disclosure are related to internal and external environmental factors.
Chamisa (2000)	Zimbabwe	<ul style="list-style-type: none"> • The accounting needs • Size of public and private sector • Existence of capital market • The underlying environment 	

Appendix B: list of the main variables and measurements investigated in the literature

Macroeconomic / country level determinants	Measurement	(Zehri and Chouaibi, 2013)	(Zeghal and Mhedhbi, 2006)	and Ding et al.(2007)	La Porta et al. (1998) or (1997)	Abd-El salam and Weetman, 2003
Culture	Dummy value=1 for the culture e.g Anglo-Saxon culture Dummy value = 0 otherwise	x	x			
Economic growth	The annual average growth rate of GDP / person GDP per capita / country's population	x	x		x	
Exist Capital market	Dummy value=1 if capital market exist Dummy value = 0 otherwise	x	x			
Advanced Educational level	The general literacy rate in the country	x	x			
Open to exterior world	The average rate of gross foreign direct investment / GDP	x	x			
Legal system	Dummy value=1 if country is civil/code law Dummy value = 0 otherwise	x		x	x	
Political system	Gistel index	x				
Ownership concentration	The average percentage of common shares owned by the three largest shareholders in the 10 largest non-financial domestic firms			x	x	

Importance of the accounting profession	The density of public accountants / auditors per 100,000 inhabitants		
Equity market development	<ol style="list-style-type: none"> 1) The ratio of the aggregate stock market capitalization held by minority shareholders to gross national products 2) The number of listed domestic firms relative to the population 3) The number of the IPOs relative to the population 	x	x
Language	Translating the standards to the local languages		x

Appendix C: List of disclosure items

GOVERNANCE DISCLOSURES

Financial Statements

- Disclosure of profit and loss account statement
- Disclosure of balance sheet statement
- Disclosure of cash flow statement
- Capital and its breakdown
- Deposits and its breakdown
- Other Liabilities and provisions breakdown
- Cash and balance breakdown
- Borrowing and its breakdown
- Investments and their breakdown
- Fixed assets and their breakdown
- Contingent liabilities and their breakdown
- Profit earned and their breakdown
- Other income and their breakdown

- Interest expenses and their breakdown

- Operating expenses and their breakdown
- Directors' fee and allowances
- Total Capital adequacy ratio

Management Discussions and analysis

- Information regarding remuneration committee
- Information on remuneration to all the directors/MD
- Report on Management Discussion and Analysis (MDA)

Sharia Reporting

- Disclosure of the role of sharia advisor or board in supervising the bank's activities
- Disclosure of earnings or expenditures prohibited by sharia
- Disclosure of restricted assets or assets pledged as security
- Other details of Annual report
- Basic organization structure/chart/description of corporate structure
- Date of establishment
- Official address/registered address/address for correspondence
- Web address of the bank/email address

- Tier 1 capital
- Tier 2 capital
- Risk-weighted capital assets
- Narrative statement of company's affairs
- Amount of dividend recommended
- Report on corporate governance
- Composition of Board of Directors
- Details of attendance of each director at BOD meeting
- Number of BOD meetings held and dates
- Classification of directors as executive or outsider
- Information on management/executive committee of the board
- Composition of Audit Committee
- Number of meetings held and date of audit committee
- Disclosure of materially significant related party transactions
- Disclosure of accounting treatment and policies
- Disclosure of information on the quarterly result/press release to website
- Disclosure of listing information on stock exchange
- Disclosure of market price data

- Disclosure of performance

- Discussion of material development in HR including number of people employed

- Information about branches
- List of shareholders owning 5% or more of the company
- Management's objectives and strategies vision/motto
- Details about the BOD (other than name/title)/background of the chairman/academic/professional/business experience
- Number of shares held by directors
- List of senior managers (not on the board of directors)/senior management structure
- Background of senior managers
- Directors' engagement/directorship of other companies

- Financial ratios and statistics

Segmental Reporting

- If the company operates in more than one business and/or geographic segment, then disclosure in report and detailed footnote for the segments

Risk Management Reporting

- Discussion of overall risk management philosophy and policy
- Information on risk management committee
- Information on assets-liability management committee
- Quantitative and qualitative information on gross loan position
- Disclosure of credit rating system/process

CORPORATE SOCIAL RESPONSIBILITY DISCLOSURES

Mandatory Disclosure

- **Policy for Screening Clients**

Disclosure of provisions for screening clients

- **Policy for Dealing with Clients**

Disclosure of provisions relating to dealing with clients in terms of late payments, insolvency, credit extension etc

- **Policy for Earning & Expenditure Prohibited by Sharia**

Disclosure of amount and description of impermissible or haram transactions

Voluntary Disclosure

- **Policy for Qard Hasan**

Disclosure of formal scheme operated by the bank for related parties to place their funds in use of Qard Hasan

- **Social, Development and Environment Based Investments**

Disclosure of social impact investments that help in assisting poor, needy, heavily indebted individuals and families. As well as, disclosure of development based

- Comparative financial statement

- Ageing schedule of past due loans and advances (NPA)
- Disclosure about risk management process (use of risk-mitigating tools such as collaterals, guarantees, netting agreement, managing concentrations)
- General descriptions of market risk
- Significant concentrations of foreign exchange exposure by currency
- Broken down by assets and liabilities
- Maturity information about deposits and other liabilities

- **Employee Welfare**

Disclosure of provisions showing equal opportunities for all employees, as well as expected behaviours from them

- **Zakah**

Disclosure of Zakah in financial statements in accordance with provisions of AAOIFI standard

investments that assist in growth of targets such as research, education or an infrastructure of a country. Also, investments that aid in protecting the environment

- **Par Excellence Customer Service**

Disclosure of code of conduct and active measures taken to develop customer service skills

- **Policy for SMEs and Social savings**

Disclosure of policies for micro and small business savings as well as community based programmes

- **Policy for Charitable Activities**

Disclosure of charity fund and activities

- **Policy for Waqf Management**

Disclosure of Waqf that is managed based on Sharia guidelines and rules

Appendix D: Countries applying Islamic finance

S.No.	Country Name	Islamic Finance Year	Where Islamic finance started in the country	Islamic Law name / year	Reference of Year when the Islamic finance start	Reference of using AAOIFI or IFRS	Acc. Standards	No. of IFIs	Acc. Standard as of the Law	Law for financial reporting	Financial Reporting Law year	Year of implementing F. R. law	Financial Reporting standard in practice	codes AAOIFI=1, IFRS=2, Local=3	Market Development
1	Afganistan		0						0	0		0	Both AAOIFI and IFRS	0	
2	Albania	1993	Arab-Albanian Islamic Bank established in 1993		The World Almanac of Islamism: 2014				Mandate IFRS	Article 4 of Albanian's law on Accounting and Financial Statements, No.9228	2008	Mandate IFRS from 1 January 2008	Mandate IFRS	2	
3	Algeria	1991	1991 Al-Baraka Bank		Rodney Wilson, Islamic Banking and Finance in North Africa, 2011 pp:26		Local		Local GAAP consistent with IFRS as written in the Annual report of Bangue Al Baraka D'Algerie	Bangue Al Baraka D'Algerie (from the financial report of this bank I find out that Algeria apply the Local Accounting standards which are very much consistent with the IFRS)	2013	0	Local GAAP consistent with IFRS as written in the Annual report of Bangue Al Baraka D'Algerie (http://www.albaraka-bank.com/ar/images/rapport%202014_arabe.pdf)	2	
4	Australia	1989	1989 launch of first Islamic finance firm, The Muslim community Cooperative	Australia Board of Taxation to review tax laws on Islamic finance, 2010	PWC, Islamic Finance, Greating value, 2012				The Australian Accounting Standards Board (AASB)	The Corporation Act, 2001	2005	The period beginning on or after 1 January 2005	Local Australian Accounting Standards Board (AASB) equivalent to IFRSs	3	Developed

			Australia limited													
5	Azerbaijan	1988	Universal bank established in 1988 now known as Kauther bank	The international bank of Azerbaijan	Islamic finance in the former Soviet Union, (Bekkin , 2008)					1988						
6	Bahrain	1979	establishing Islamic banks in 1979		Rodney Wilson, the development of Islamic finance in the GCC, 2009 pp 6		AAOIFI	57	AAOIFI FAS (Have special Law for Islamic banking)	The Islamic bank licensee must comply with AAOIFI FAS The central Bank of Bahrain (CBB Rulebook, Volume 2- Islamic Banks, Part A, Paragraph AU4.1.1	1988	0	Mandate AAOIFI FAS for Islamic banks	1	Frontier	
7	Bangladesh	1983	1983 Islamic Bank of Bangladesh		Islamic banking and finance: On its way to globalization (Khan & Bhatti, 2008)		IFRS	38	The Institute of chartered accounting in Bangladesh (ICAB) adopted IAS and IFRS as Bangladesh Financial Reporting Standards (BFRS)	Bangladesh bank issued Guidelines for conducting Islamic banking in November, 2009 Paragraph 3.4 in Appendix II.	2009	November, 2009	IAS and IFRS are adopted as BFRS , In practice Some banks are reporting compliance with both BFRS and AAOIFI	3	Frontier	
8	Bosnia and Herzegovina		Bosna Bank International Sarajevo		http://www.globalbankingandfinance.com/list-of-islamic-banks-in-			22	IFRS translated into Bosnian as of 31 December 2009	The law on Accounting of the federation of Bosnia and Herzegovina (Official Gazette No. 83/90)			The bank applied all IAS and IFRS translated into Bosnian as of 31	IFRS	2	Standalone

					bosnia-and-herzegovina/							December 2009.			
9	Botswana		Nothing found												Standalone
10	Brunei	1992	the government actually put an Islamic bank into operation in 1992	The tiny Sultanate of Brunei followed Malaysia's example in 1985 the Sultan decreed an Islamic banking option	Islamic Banking and finance in south east Asia ,(Venardos,2005)		IFRS	4	IAS/ IFRS	Brunei Darussalam Accounting Standards Council (BDASC) has issued Notice No. 1/2014, Accounting standards to comply with IAS, IFRS	2014	Effect from 1 January 2014	In Practice some banks such as Islam Brunei Darussalam report compliance with the Brunei GAAP	3	
11	Canada	2009	2009	Toronto Stock exchange (TSX) Shariah index launched	PWC, Islamic Finance, Creating value,2012						2009				Developed
12	Dememark		0												Developed
13	djibouti	2010	4 banks operate in Djibouti (Saba Islamic Bank started 2006,	An Islamic banking law introduced in 2011 and seven	http://www.reuters.com/article/2013/11/07/islamic-finance-djibouti-idUSL5N				http://www.pwc.com/us/en/cfodirect/assets/pdf/pwc-ifs-by-country-2015.pdf	2010	Islamic banks operate in the country however, the country is	http://www.banque-centrale.dj/institutions	3/4		

			Salaam African Bank, Dahabshil Bank International and Shoura Bank). The latter two were set up in 2010.	guidance notes from Djibouti's central bank	OIR1FJ20131107							not adopting IFRS and it was difficult to check the annual reports of the banks as they use French and also there is no websites for the banks			
14	Egypt	1976	1960s credit unions started/ Faisal Islamic bank 1976	law number 48 of 1977 was passed permitting the establishment of Islamic banks and their regulation by the Central Bank of Egypt	Rodney Wilson, Islamic Banking and Finance in North Africa, 2011 pp:23		IFRS	12	Egyptian Accounting Standards (EAS)	The Egyptian Financial Supervisory Authority (EFSA) has developed EAS based on IASs and IFRSs that exist in 2005	2005	For Islamic instruments such as Ijarah there are separate law (Law No. 5 of 1995)	Local GAAP (EAS) Abu Dhabi Islamic Bank Egypt and Al-Baraka Bank Egypt	3	Emerging
15	Ethiopia	2011	The first Islamic bank launched (Zam		PWC, Islamic Finance, Creating value,					http://www.pwc.com/us/en/cfodirect/assets/pdf/pwc-ifs-by-country-2015.pdf	2011	Zam Zam bank stopped its islamic banking			

			Zam Bank), 2011		2012						operation in 2012		
16	France	2009	2009	Central bank to issue Islamic banking licenses	PWC, Islamic Finance, Creating value, 2012					2009			Developed
17	Gambia	1994	The Arab Gambian Islamic Bank Limited (AGIB) was incorporated as a private limited liability company on 11 November 1994 and was granted a banking license by Central Bank of The Gambia in 12 September 1996.	the Financial Institution Act 1992 had to be amended to allow for the operation of an Islamic Bank in an entirely conventional banking society.	http://www.access.gambia.com/information/agib.html			http://www.agib.gm/index.php	1996	Checked the website of the Arab Gambian Islamic bank and could not find any annual reports. The country is not adopting IFRS also. Therefore it is assumed that local standards are applied in the annual reports		3	
18	Germany	2010	2010	first Islamic	PWC, Islamic					2010			Developed

				banking operation	Finance, Creating value, 2012										
19	Ghana		Ghana Islamic Microfinance bank,	No Year founded	ISLAMIC BANKING IN WEST AFRICAN SUB-REGION: A SURVEY (Abdullahi, 2013)										
20	Guinea	1983	The Islamic Bank of Guinea (BIG)—established in 1983		Islamic finance In Sub Saharan Africa (Gelbard et al. 2014) / ISLAMIC BANKING IN WEST AFRICAN SUB-REGION: A SURVEY (Abdullahi, 2013)					1983					Standalone
21	Hong Kong	2007	Launched of Hang Seng Islamic China	http://www.globalbankingandfinance.com/list-	PWC, Islamic Finance, Creating value, 201					2007					Developed

			Index fund 2007	of-islamic-banks-in-hong-kong/	2										
22	Indonesia	1992	the Bank Muamalat Indonesia which has been functioning since 1992	the Indonesian Government has implicitly allowed the Shari'ah banking operations in the Act No. 7 of 1992	Islamic Banking and finance in south east Asia ,(Vernardos,2005)	IFRS	78	The Indonesian Financial Accounting Standards (IFAS)	Accounting standards in Indonesia are set by the Indonesian accounting Standards Board operates under the Indonesian Institute of Accounting (IAI). For Islamic Institutions there are three more laws 1) Indonesian Financial Accounting standards (Indonesian FAS or PSAK).2) Standards of Shariah compliant transactions (PSAK Syariah) 3) Standards for entities without public accountability (ETAP)	2009	As part of the convergence process IAI amended the standards to reflect the IFRS in issuance as at 1 January 2009.	Local GAAP (Indonesian FAS)	3	Emerging	
23	Iran, Islamic Rep.	1983	1983	Law on Usary free banking, Tehran, 1983 (Separate Law)	Rodney Wilson, Islamic Banking and Finance in North Africa,2011 pp:22	Local	54	Iranian Accounting Standards (Some banks do not specify which accounting standards)	Banks applied the requirements of Central Bank of Iran (CBI). e.g. Income recognition (circular MB/772 dated July 2005 and classification of financial instruments (Circular MB/2828 of 24 February, 2007	1983	0	Local GAAP (Iranian Accounting Standards) but some banks do not specify which accounting standards such as Parsian Bank and Karafarin Bank	3		

24	Iraq	1992	1992 Iraq Islamic bank		https://www.iraqiislamicbank.com/Page.aspx?id=1#.VfmBv9JViko		IFRS	13	0	the law for Islamic banks No. 46 issued in 4th of November 2015 specify the use of local alw to report financial transactions first. However, in case the law is not clear in certain issues then use AAOIFI	1992	0	http://www.arabnak.com	3		
25	Japan	2009	Law passed allowing banks to conduct Islamic finance, 2009		PWC, Islamic Finance, Creating value, 2012						2009				Developed	
26	Jordan	1978	1978 establish ment of Jordan Islamic bank		http://www.jordanislamicbank.com/?427dacca3edd8203f5aceefbb76c6d2efc545ea3cf		AAOIFI	12	(In practice all banks comply with AAOIFI)	The companies Law No. 22 of 1997 (Article 75: Accounts preparation) where accounts of companies should be prepared in accordance with (General recognised international accounting principles). Also Amman stock exchange requires IFRS to be used by financial institutions. Article (14) of the Instructions of Issuing companies Disclosure, Accounting and	1997		The companies Law No. 22 of 1997	AAOIFI	1	Frontier

										Auditing Standards					
27	Kazakhstan	2003	Bank TuranAlam (BTA) started in 2003		Islamic finance in the former Soviet Union,(Bekkin , 2008)						2003				Frontier
28	Kenya	2005	Barclays launching Islamic banking products in December 2005	In 2010, through the Finance Act, the Kenyan authorities amended Section 45 of the Central Bank of Kenya Act to allow the Central Bank as the government's fiscal agent to recognize the payment of a return rather	Islamic finance In Sub Saharan Africa (Gelbard et al. 2014)		Local	0	0		2005	0	IFRS	2	Frontier

				than interest on government securities, thereby opening up the spectrum of Shari'ah compliant investments in the country (Ndung'u, 2011)										
29	Kuwait	1977	Kuwait passed legislation on 23 March 1977 to allow the establishment of KFH (Wilson, 2009)	Central Bank of Kuwait, Legislation, Safat, 2004, Section 10. (Not separate) (Wilson, 2011)	Rodney Wilson, Islamic Banking and Finance in North Africa, 2011 pp:22	IFRS	92	IFRS	The central bank of Kuwait (CBK), issued Instructions to Islamic banks No. 26, the Bases of preparing Closing Financial data of Islamic Banks, which reinforced a resolution by the ministry of the Commerce and Industry (Ministerial Resolution No. 18, 1990) to comply with IAS/IFRS.	1990	Ministry of the Commerce and Industry (Ministerial Resolution No. 18, 1990)	IFRS	2	Frontier
30	kyrgystan	2007	EkoBank and Islamic development bank		Islamic finance in the former Soviet					2007				

			signed a MOU to operate Islamic banking in the country in 2006 / EkoBank opened officially in 2007		Union,(Bekkin , 2008)									
31	Lebanon	2005	Lebanon Islamic bank first Islamic bank in Lebanon in early 2005 http://www.lebaneseislamicbank.com.lb/pages.asp?id=18	law of establishing the Islamic law in Lebanon , 2004	https://www.google.co.uk/#q=LAW+No+575+Establishing+Islamic+banks+in+Lebanon	AAOIFI	7	IFRS	Banque du Liban as a central bank request the banks and the financial institutions to comply with IFRS	2000	Banque du Liban, Basic Decision No.7737: Internal Control and Internal Audit in Banks and Financial Institutions, Article 3. December 2000	In practice Islamic banks comply with AAOIFI such as Blom Development Bank	1	Frontier
32	Libya	2012	Libyan Central bank approves new Islamic banking law, 2012		PWC, Islamic Finance, Creating value, 2012					2012				

33	Luxembourg	1978	The Islamic Banking System Holdings Limited Luxembourg was established in 1978 /In early 2009, the Luxembourg Deutsche Bank launched "Al Mi'yar"		http://www.ifcreview.com/restricted.aspx?articleid=2096&areaid=29#					1978				
34	Malaysia	1983	1983	Islamic Banking Act of Malaysia, Kuala Lumpur, 1983 (Separate Law)	Rodney Wilson, Islamic Banking and Finance in North Africa, 2011 pp:22		IFRS	76	Malaysian Financial Reporting Standards (MFRS)= IFRS (Compliance with MFRS constitutes compliance with IFRS)	The financial reporting Act, 1997 established the Malaysian Accounting Standards Board (MASB). MASB requires entities to apply the MFRS on or after 1 January, 2012 For Islamic Banking, Bank Negara Malaysia circulars (Financial Reporting and Financial reporting for Islamic Banking Institutions) Issued on 28 June, 2013 requires the use of MFRS for the	2012	On or after 1 January, 2012	Local GAAP (MFRS constitutes with IFRS ²	Emerging

										licensed person.					
35	Maldives	2011	Maldives Islamic Bank established in 2011	http://www.mma.gov.mv/laws/islamicbankingregulationEnglish.pdf	http://www.mma.gov.mv/finance?itm=6						2011		checked the Islamic banking regulation in English for the country and could not find anything related to using AAOIFI or IFRS for reporting the financial transactions	3	
36	Mali		Population is 90% Muslims but no interest in Islamic finance		ISLAMIC BANKING IN WEST AFRICAN SUB-REGION: A SURVEY (Abdullahi, 2013)										
37	Mauritania	1985	1985 Al-Baraka Bank		Rodney Wilson, Islamic Banking and Finance in North Africa, 2011 pp:27						1985				
38	Mauritius	2009	Credit Unions present since 1998 but the first Islamic bank services	In 2007, the Banking Act was amended to formally allow for	Islamic finance In Sub Saharan Africa (Gelbard et al. 2014)				AAOIFI FAS	The central bank, Bank of Mauritius, issued its (Guideline for Institutions Conducting Islamic Banking Business in 2008. Section 20 of the guideline requires Islamic banks and	2008	2008	IFRS	1	Frontier

			started by HSBC bank in 2009	Islamic banking activities						Institutions to Adopt AAOIFI FAS.				
39	Moroco	2013	Nothing found				Local							Frontier
40	Nigeria	1992	Habib Bank (now Bank PHB) was the first bank operating an Islamic banking window (in 1992)(Jaiz Bank as fully fledged Islamic bank established in 2012) (Gelbard et al. , 2014)	the Central bank Nigrian CBN issued a draft framework for the regulation and supervision of noninterest banks in Nigeria on March 4th, 2009 (Legal Services Department, CBN, 2009). Also, Nigrian Central bank release the framwork for non-interest	THE ISLAMIC FINANCE INDUSTRY IN NIGERIA: FROM HISTORY MYSTERY TO FUTURE REALITY By Said Adekunle Mikail, PH D, 2013, Thomson Reuters Also, http://www.zora.uzh.ch/94170/1/DaudaMomodu_Rev_2013-1.pdf		Local		1992	checked the acnnual report of Jaiz bank 2014 and it does not state any reporting to AAOIFI or IFRS even the country adopted the IFRS fully in 2012 but othe law for Islamic finance does not specify the use of IFRS in Islamic banks		3	Frontier	

				banking in 2011.											
41	Oman	2012	2012	Islamic banking regulatory framework, Central bank of Oman, 2011	http://www.cbo-oman.org/news/IBRF.pdf		AAOIFI	11	AAOIFI FAS	The Central Bank of Oman (CBO) issued its Islamic banking Regulatory Framework in December, 2012. The framework requires the fully-fledged Islamic banks, Islamic banking branches of foreign banks and Islamic windows of conventional domestic banks to apply AAOIFI FAS.	2012	December, 2012	AAOIFI	1	Frontier
42	Pakistan	1981	From January 1, 1981, separate interest-free counters started operations in all the nationalized commercial banks	SBP issued BCD Circular No. 13 of 1984 that called for elimination of Riba from the banking system and in January 1, 1985 all companies was directed to be only through interest-	http://www.bis.org/review/r070928e.pdf		IFRS	54	Islamic Financial Accounting Standards (IFAS) or Pakistan GAAP	The Securities and Exchange Commission of Pakistan (SECP) requires companies to comply with (IFAS) issued by the Institute of Chartered Accountants of Pakistan (ICAP). Such as IFAS 1, Murabaha, dated 24 August, 2005 and IFAS 2, Ijarah, dated 22 May 2007. Also the strategic Plan for Islamic banking Industry in Pakistan, 2014 – 2018, supports the issue of more Islamic accounting	1981	IFAS 1, Murabaha, 24 August, 2005 IFAS 2, Ijarah, 22 May 2007.	Local GAAP (Pakistan GAAP)	3	Frontier

				free modes						standards.					
43	Palestine	1994	The Islamic finance started after the launch of Palestinian Finance House Corporation - 1994		http://www.islamicfinance.com/ifn-country-analysis-palestine		Local	0	0		1994	0	http://www.arabnak.com	1	Standalone
44	Philippines		Amanah Islamic Bank					Philippines Financial Reporting Standards (PFRS) Local Based on IFRS but with several modifications (AOSSG, 2015)	The Central bank, Bangko Sentral ng Pilipinas, (BSP) has required all banks to comply with PFRS for annual financial statements beginning 1 January 2005. The Financial Reporting Standards Council (FRSC) part of the Philippines Institute of Certified Public Accountants (PICPA) adopted IFRS with modifications as PFRS		2005	Beginning 1 January 2005.	Local GAAP (PFRS)	3	Emerging
45	Poland		0												Emerging
46	Qatar	1982	establishing Islamic banks in 1982		Rodney Wilson, the development of Islamic finance in		AAOIFI	38	AAOIFI FAS	Qatar Central Bank (QCB) issued its Instructions to banks in November, 2011 required Islamic banks to Apply AAOIFI. Also	2011	November, 2011	Mainly AAOIFI but some banks report compliance to IFRS instead (Islamic Holding Group and Qatar Islamic	1	Emerging

					the GCC,2009 pp6					Circular No. 93/2012, Consolidated Financial Statements for Islamic banks, required all Islamic banks to comply for the year ended 31 December, 2012. All entities in Qatar Financial Centre (QFC) must comply with the rules of QFC Regulatory Authority (QFCRA) issued in April 2012. The QAFRA rules require all the Islamic Institutions to comply with AAOIFI.			Insurance)		
47	Saudi Arabia	1975	The Islamic Development bank opened in Jedah in 1975 (Wilson, 2009)	No specific law governing Islamic finance so far (Wilson, 2009)	Rodney Wilson, the development of Islamic finance in the GCC,2009 pp6		IFRS	99	IFRS	The Saudi Arabian Monetary Agency (SAMA) requires banks and insurance companies to comply with IFRS. As in (International Monetary Fund, Saudi Arabia: Report on the Observance of Codes (ROSC), June 2011	1975	0	IFRS	2	Emerging
48	Senegal	1983	Banque Islamique du Senegal (BIS) the biggest Islamic bank so	Issuing its first sovereign Islamic Bond, 2011	PWC, Islamic Finance, Creating value, 2012 / ISLAMIC BANKING IN WEST				0		1983	0	0		0

			far establishe d in 1983		AFRICAN SUB- REGION: A SURVEY (Abdullahi , 2013)										
49	Singapor e	2007	first Islamic bank establishe d, Islamic bank of Asia , 2007		PWC, Islamic Finance, Creating value.201 2					2007					Developed
50	Somalia	2009	the Salaam Somali Bank (launched in 2009)		http://shuraako.org/sites/default/files/documents/Somalia%20Banking%20Transfers.%20Challenges%20And%20Opportunities.pdf					2009					
51	South Africa	1989	In 1989, Al Baraka— part of the Saudi Arabian- based Dallah Al	finance minister introduce the legislation permitting Sukuk - 2011	PWC, Islamic Finance, Creating value, 2012		Local		IFRS	Article 11 (1) of the Bank Act 1990 and the Companies Act 71 of 2008, requires financial reporting to be in accordance with IFRS. Also, Section 8 of the Johannesburg	2008	Compani es Act 71 of 2008	IFRS	2	Emerging

			Baraka group—and the Islamic Bank were the first Islamic banks granted licenses by the South African Reserve Bank (Gelbard et al.,2014)						Securities Exchange listing requires compliance with IFRS					
52	South Korea	2011	Parliament expected to pass the law related to offering of tax waiver on foreign investors interest income from Sukuk issued - 2011		PWC, Islamic Finance, Creating value,2012					2011				Emerging
53	Sri Lanka		Amana Islamic Bank					Sri Lanka Accounting Standards (SLAS)	The Sri Lanka Accounting and Auditing Standards Act, N. 15 of 1995.	1995	The Sri Lanka Accounting and	Local GAAP (LKAS/SLFRS)	3	Frontier

										This law established the Sri Lanka Accounting and Auditing Standards Monitoring Boards which monitor the compliance with Sri Lanka Accounting Standards (SLAS) which are issued by the Institute of Chartered Accountants of Sri Lanka.		Auditing Standards Act, N. 15 of 1995.			
54	Sudan	1978	Faisal Islamic bank, Sudan ,1978	July 1, 1984 Governor instructed all the banks to convert to Islamic operation in two months	http://www.iby-bank.com/index.asp?CBT=1&BI=7&Sec=1	AAOIFI	44	0		Chapter V of the business banking Act, 2003 gives the governor of the Central Bank of Sudan the power to specify accounting standards for the bank.	1978	No specific act for Islamic Banks	Mainly AAOIFI, but There are some banks in Sudan prepare there consolidated financial statements based on IFRS but individual financial statements are in AAOIFI FAS such as Byblos Bank Africa (BBA) (AOSSG, 2016)	1	
55	Syrian Arab Republic	2006	In 2006 The syrian gov. permitted 3 Islamic banks (Al-Sham Bank, Al-Baraka Bank and Syrian International	The Syrian Parliament approved Islamic banking laws in 2005	Islamic banking and finance: On its way to globalization (Khan & Bhatti, 2008)	AAOIFI	6	AAOIFI	0		2006	0	Al Baraka Bank Syria (2013 and 2014) annual report are compile with the AAOIFI FAS	1	

			Islamic bank)											
56	Tanzania		0				Local	0	0		0	0	0	
57	Thailand		Islamic Bank of Thailand					THA IAS and THA FRS which are consistent with IAS and IFRS 2009	The responsibility for setting accounting standards resets with the Federation of Accounting Professions (FAP) as stated in section 7 of the Accounting Professions Act, B.E. 2547 (2004. FAP adopted the IAS and IFRS issued in 1 January 2009 as THA AS and THA FRS there is a plan also to update them to be in line with the IFRS Bound Volume 2012	2009	39814	Local GAAP (THA IAS and THA FRS which are consistent with IAS and IFRS 2009)	2	Emerging
58	Tunisia	1983	Al-Baraka Bank Tunis 1983 / May 2010 Establishment of Bank Al-Zaitona	Al-Baraka Bank Tunis 1983	Rodney Wilson, Islamic Banking and Finance in North Africa, 2011 pp:26		Local	Until 2014 there is no special law for Islamic institutions unless the Local law. However, the Arabic media discuss the plan to form a law for adopting AAOIFI for the Islamic banks in Tunisia	Al Baraka Bank Tunis 2013 & 2014 prepare there financial statements based in Institutions Law No. 112 dated 30th December, 1996 and the Ministerial decision dated 25 March 1999 in regard to the Accounting standards for banks and Financial Institutions (Specially Act NO. 21) http://www.albarakab	1983	0	http://raqaba.co.uk/	1	Frontier

										ank.com.tr/AccueilAR.aspx					
59	Turkey	1986	The Turkey Islamic Bank, 1986	Islamic Banking and finance in south east Asia ,(Ve nardos,2005 pp:65)	Local	4	IFRS + TUR FRS	There are two laws in Turkey: The Banking Regulation and Supervision Agency (BDDK) issued a Communique on the Financial Statements to be announced to Public by Banks as well as Explanations and Footnotes Thereof in 2007. Article 1 requiring banks to use Turkish Accounting Standards (TUR FAS) 2011 Article 5 require the enterprises which issue securities in the stock exchange market to use IFRS as adopted in the EU. Also, the Capital Market Board (CMB) issued a Communique on the Principles of Financial Reporting in the Capital markets (Serial Xi: No. 29) in 2011 Article 5 require the enterprises which issue securities in the stock exchange market to use IFRS as adopted in the EU.	2007	2007 and 2011	Local GAAP (TUR FRS) but the listed entities report under IFRS such as Al Barakah Turkish finance house	3	Emerging		

60	UAE	1975	the Emir of Dubai passed a decree on 12 March 1975 authorizing the establishment of Dubai Islamic Bank		Rodney Wilson, the development of Islamic finance in the GCC, 2009 pp		AAOIFI	73	IFRS	Central bank of UAE issued a Circular 20/99, Adoption of International Accounting Standards, in 1999 to banks.	1999	1999	IFRS	2	Emerging
61	Uganda	2012	Governor of the Bank of Uganda announces permits the licensing of financial institutions in Islamic banking - 2012	http://www.globalbankingandfinance.com/?s=list+of+Islamic+bank+in+Uganda	PWC, Islamic Finance, Creating value, 2012						2012				
62	UK	2010	UK Islamic finance Secretariat sets objectives to entrench London as a global gateway	Abolished double stamp duty for Islamic mortgages, 2003	PWC, Islamic Finance, Creating value, 2012	The first Islamic retail bank opened for business in the United Kingdom in	IFRS	18	IFRS as adopted by the EU	From July, 2012 the Financial Reporting Council (FRC) assumed responsibility for setting accounting standards within the meaning of section 464 of the UK Companies Act, 2006. The FRC issues two sets of	2012	July, 2012	IFRS	2	Developed

			for Islamic finance to lead to issuance of the first UK sovereign Sukuk - 2010			September 2004 (Vendore s ,2005 pp217)				standards that are to be applied by the companies in UK 1) Financial Reporting Standards (FRS) 2) Financial Reporting Standards for Smaller Entities (FRSSE). The companies Act allow the companies to prepare their accounts either in a) accordance with (section 396 (404) – Companies act individual (group) accounts) or b) in accordance with IAS.					
63	USA	1987	American House of Representatives established in 1987 (Khan & Bhatti, 2008)	The Dow Jones Islamic Market Indexes launched in 1999 (PWC, 2012)	PWC, Islamic Finance, Creating value, 2012				US GAAP	The companies in the US Securities and Exchange Commission SEC required to comply with US GAAP issued by the Financial Accounting Standards Board (FASB)	1999	0	Local GAAP	3	Developed
64	Yemen, Rep.	1995	the first Islamic bank launched (Islamic bank of Yemen), 1995	Islamic banking Law number 137, 1995 (Check this)	http://www.iby-bank.com/index.asp?CBT=1&BI=7&Sec=1		AAOIFI	10	IFRS or Accounting Standards for Islamic Financial Institutions	The Central Bank of Yemen (CBY) requires all banks to use IFRS in their published financial statements (Article 107 of the Tax By-Laws).	1995	(Check IFRS website)	Local GAAP (Accounting Standards for Islamic Financial Institutions)	3	

Note: For the countries where no Islamic bank law exist and the Islamic banks has to use the same accounting standards as the conventional banks this mean I have to check when the Islamic finance allowed in the country and therefore, apply the date when the Islamic finance started as the date for starting adopting the country accounting standards in the Islamic banking Industry (same law as the conventional banks in the country).