

Determinants of compliance with AAOIFI standards by Islamic banks

Compliance with AAOIFI standards

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Abstract

Purpose – The authors explore the level and determinants of compliance with Accounting and Auditing Organization for Islamic Financial Institution's (AAOIFI) financial and governance standards by Islamic banks (IBs).

Design/methodology/approach – The sample consists of 43 IBs across eight countries. The authors use ordinary least squares regression analyses to examine the impact of bank-specific characteristics and corporate governance (CG) mechanisms concerned with Board of Directors (BOD) and Sharia Supervisory Board (SSB) on the levels of compliance with AAOIFI standards.

Findings – The paper finds that the average compliance level based on AAOIFI standards concerning the SSB is 68 per cent; corporate social responsibility (CSR) is 27 per cent; and presentation of financial statements (FSs) is 73 per cent. The aggregate disclosure based on the three indices is 56 per cent. The analysis also shows that size, existing Sharia-auditing department, age and CG of SSB are the main determinants of compliance levels.

Originality/value – The determinants of compliance with AAOIFI standards for IBs around the world have not been explored before, and therefore, this paper is the first of its kind to this issue.

Keywords Determinants, Islamic banking, AAOIFI standards, Compliance and non-Compliance, Cross-country

Paper type Research paper

1. Introduction

We examine the determinants of compliance with Accounting and Auditing Organization for Islamic Financial Institution's (AAOIFI) standards by Islamic Banks (IBs).

The literature on compliance with AAOIFI explores the compliance level (Ullah, 2013; Vinnicombe, 2010; Ahmed and Khatun, 2013). However, the determinants of the compliance, considering both firm characteristics and board and Sharia Supervisory Board (SSB) characteristics, have not yet been empirically investigated. Our paper fills the research gap. Furthermore, the majority of prior research focuses on a single country (Hafij, 2013; Ahmed and Khatun, 2013) or is restricted to one category of AAOIFI standards, such as the presentation of financial statements (FSs) (Hafij, 2013) or corporate social responsibility (CSR) (Hassan and Harahap, 2010).

We contribute to existing literature in a number of ways. First, we consider majority of IBs that adopt AAOIFI. Second, we consider three AAOIFI standards related to Sharia, social and financial disclosures. Third, we are the first large-scale study that explores IBs' compliance with AAOIFI standards after 2010 (the updated version for AAOIFI which includes new financial and governance standards). Finally, we are the



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first to examine the impact of both country (i.e. culture) and bank characteristics on compliance with AAOIFI standards.

Our results indicate that the compliance level with AAOIFI Governance Standard Number 1 is 68 per cent; the compliance level with AAOIFI Governance Standard Number 7 is 27 per cent and compliance level with AAOIFI Accounting Standard Number 1 is 73 per cent. The empirical analysis shows that size; age; Sharia Auditing Department (SAD); uncertainty avoidance (UA) and corporate governance (CG) of SSB is significantly associated with levels of disclosure.

Our paper is organised as follows: Section 2 discusses issues related to compliance with AAOIFI standards. Section 3 reviews the literature and develops the hypotheses. Section 4 discusses the methodology. Section 5 discusses the descriptive analysis. Section 6 reports the findings. In Section 7, we discuss our findings. Section 8 concludes.

2. Compliance with Accounting and Auditing Organization for Islamic Financial Institution

AAOIFI formulates and issues accounting, auditing, governance, ethics and Sharia standards for IFIs. AAOIFI, as an independent international organisation, is supported by institutional members (200 members from 40 countries) including central banks, IFIs and other participants from the international Islamic banking and finance industry worldwide (AAOIFI, 2015). Currently, AAOIFI has published 88 standards including 26 accounting standards, 5 auditing standards, 7 governance standards, 2 ethics standards and 48 Sharia standards (AAOIFI, 2015). For the purpose of this study, compliance can be defined as “the degree to which IBs comply with the multitude of issues in the accounting and governance standards issued by the AAOIFT”. The following section explores the three AAOIFI standards of interest.

2.1 Accounting and Auditing Organization for Islamic Financial Institution and Sharia Supervisory Board

According to AAOIFI, a SSB is defined as “an independent body of specialised jurists in fiqh al mu’amalat (Islamic commercial jurisprudence)” (AAOIFI, 2010a, 2010b, 2010c, 2010d, 2010e). The purpose is to ensure IFIs are in compliance with Sharia principles. AAOIFI published Governance Standard Number 1, which specifies the composition of the board and the basic elements of its annual report.

2.2 Accounting and Auditing Organization for Islamic Financial Institution and corporate social responsibility

CSR for IFIs refers to “all activities carried out by an IFI to fulfil its religious, economic, legal, ethical and discretionary responsibilities as financial intermediaries for individuals and institutions” (AAOIFI, 2010a, 2010b, 2010c, 2010d, 2010e). AAOIFI issued Governance Standard Number 7 in 2010 to organise the activities related to CSR. The primary objective for this standard is to ensure that CSR activities and compliance of IFIs are communicated in a truthful, transparent and comprehensible manner to relevant stakeholders (AAOIFI, 2010a, 2010b, 2010c, 2010d, 2010e). The accountability for disclosure under this standard is divided between mandatory disclosure (such as earnings and expenditure prohibited by Sharia and *Zakat*) and recommended disclosure (such as *Qard Hasan*, charitable activities and *Waqf* management) (AAOIFI, 2010a, 2010b, 2010c, 2010d, 2010e).

2.3 Accounting and Auditing Organization for Islamic Financial Institution and the presentation and disclosure in the financial statements

In 1993, AAOIFI issued Accounting Standard Number 1 related to general presentation and disclosure in the FSs of IBs:

The objectives of financial reports is to provide information about the IFI's compliance with Islamic Sharia; information about IFI's economic resources and related obligations; information to assist in the determination of Zakat; IFI's discharge of its fiduciary and social accountabilities (AAOIFI, 2010a, 2010b, 2010c, 2010d, 2010e).

Based on this standard, the annual report contains seven basic statements in addition to basic information about the bank, significant accounting policies and other information.

3. Relevant literature and hypotheses development

We use both agency and signalling theories to identify the potential drivers of compliance with AAOIFI standards.

3.1 Firm-specific characteristics

3.1.1 Auditor. Auditors play an important role in the credibility of firms' financial information (Healy and Palepu, 2001). Chalmers and Godfrey (2004) stated that to maintain their reputation and avoid reputation costs, high-profile auditing companies are more likely to demand high levels of disclosure. The signalling theory suggests that the choice of an external auditor can serve as a signal of firm value. Generally, companies signal the quality of their financial reports by choosing large audit firms (Datar *et al.*, 1991). This expectation is consistent with agency theory, which holds that larger audit firms have a stronger incentive to impose more extensive disclosure standards because they have more to lose from damage to their reputations. The findings of Xiao *et al.* (2004) supported this proposition with a positive relationship between firms employing one of the Big 4 international auditing firms and their scopes of corporate disclosure. Guerreiro *et al.* (2008) and Hodgdon *et al.* (2009) examined corporate disclosure and found it to be positively related to auditor size. Therefore, we hypothesize that:

H1. The degree of disclosure is predicted to be higher in IBs audited by the Big 4 auditors than in IBs that are audited by non-Big 4 auditors

3.1.2 Age of bank. Older, well-established companies are likely to disclose much more information in their annual reports than younger companies because they are less likely to suffer any competitive disadvantage. In addition, the cost and the ease of gathering, processing and disseminating the required information may be a contributory factor (Owusu-Ansah, 1998). Many studies have shown that disclosure level is positively associated with company age (Cormier *et al.*, 2005; Hossain and Hammami, 2009), while others (Alsaeed, 2005) conclude that the age of the corporation has insignificant association with the level of disclosure. Therefore, we hypothesize that:

H2. Older IBs are expected to disclose more information than younger IBs.

3.1.3 Firm size. According to the agency theory, larger firms need to disclose more information to different user groups which leads to a decline in agency costs and reduces information asymmetries (Inchausti, 1997). In prior disclosure studies, the association

between firm size and disclosure reporting is mixed. For example, while some studies found a positive association (Hassan *et al.*, 2006; Elshandidy *et al.*, 2013), others found an insignificant association (Rajab and Handley-Schachler, 2009). Firm size is a significant determinant of disclosure and accounting policy choice and a “discriminator for accounting quality” (Rahman *et al.*, 2002). Moreover, large firms face higher demand for information from customers, analysts and the general public (Cooke, 1989). This results in increased pressure to disclose information. Therefore, we hypothesize that:

H3. Large IBs are more likely to disclose more information than small IBs.

3.1.4 Profitability. Inchausti (1997) suggested that profitability is capable of influencing the extent to which companies disclose information items. Consistent with the signalling theory, management when in possession of “good news” because of better performance are more likely to disclose more detailed information to the stock market than that provided by companies in possession of “bad news” to avoid undervaluation of their shares. Ahmed and Courtis (1999) showed that the results of prior studies provide mixed evidence on the association between firm’s profitability and the level of corporate disclosure. Elshandidy *et al.* (2013) reported a positive association between both variables. Nonetheless, the agency theory expects that managers of firms with high profitability would tend to provide more corporate information to justify their present performance to the shareholders.

Therefore, we hypothesize that:

H4. Disclosure are expected to be higher for highly profitable IBs than low profit.

3.1.5 Internal Sharia Auditing Department (ISAD). Mercer (2004) argued that the SAD:

[...]serve as the first line of defence against disclosure errors, ferreting out unintentional errors caused by weaknesses in a company’s internal controls and intentional errors due to fraud.

The internal audit function plays a unique and critical role in CG by helping to ensure the reliability of financial reporting (Gramling *et al.*, 2004; Carcello *et al.*, 2005). The literature provides evidence that internal auditing has a positive impact on financial reporting oversight and level of disclosure. Schneider and Wilner (1990) found that the presence of internal auditors deters fraudulent financial reporting. Other studies establish links between internal auditing and firm performance (Gordon and Smith, 1992). Archambeault *et al.* (2008) highlighted the need for an internal audit to improve governance transparency. Wilson and Walsh (1996) provided a basis for predicting that an internal auditing department will increase investors’ confidence in financial reporting reliability and perceived oversight effectiveness. Therefore, we hypothesize that:

H5. The level of corporate disclosure is positively associated with ISAD inside IBs.

3.2 Corporate governance of Board of Directors characteristics

To develop our research hypotheses, we review prior research which suggests an association between corporate disclosure and certain CG mechanisms (La Porta *et al.*, 2002; Eng and Mak, 2003).

3.2.1 Number of blockholders. A blockholder is a shareholder with an exceptionally large amount of shares. Early research indicated a negative relation between blockholder ownership and disclosure (Schadewitz and Blevins, 1998; Hossain *et al.*, 1994), while Haniffa and Cooke (2002) found a positive association. Marston and Polei

(2004) argued that investors who own a large proportion of equity shares in a company can obtain information about the company from internal sources. Therefore, more closely held companies are more likely to disclose less information because their large investors can access internal sources of information. Therefore, we hypothesize that:

H6. IBs with high percentages of blockholder ownership have low levels of disclosures.

3.2.2 Institutional ownership. Agency theory predicts that ownership structure affects the level of corporate disclosure (Eng and Mak, 2003). The relationship between institutional ownership and disclosure has been examined in prior studies; however, the empirical evidence is mixed. Schadewitz and Blevins (1998) found a negative association, while Mangena and Pike (2005) found a positive association between the two variables. IBs with a concentrated ownership structure do not have to disseminate more corporate information, because the main shareholders can easily obtain it, as they usually have access to that information. Therefore, we hypothesize that:

H7. There is a negative relationship between disclosure and institutional ownership.

3.2.3 Foreign ownership. Based on the agency theory, Fama and Jensen (1983) suggested that as the number of shareholders increases and ownership becomes more dispersed, the demands for additional information increase. Recent studies have found an association between disclosure and foreign ownership. For instance, according to Xiao *et al.* (2004), higher foreign ownership not only encourages information disclosure but also motivates firms to create English web pages to facilitate the dissemination of financial information. The extent of foreign investor ownership is an important determinant of the demand for financial information (Soderstrom and Sun, 2007). Therefore, we hypothesize that:

H8. There is a positive relationship between disclosure for IBs and foreign ownership.

3.2.4 Duality in position. Role duality in position exists when the CEO (chief executive officer) is also the chairman of the board. Agency theory predicts that role duality creates individual power for the CEO that would affect the effective control exercised by the board. Fama and Jensen (1983) argue that independent directors can play a significant role in monitoring the performance of managers. The results of prior research provide mixed evidence on the association between duality in position and corporate disclosure. Some studies find a negative association between the two variables (Laksmanna, 2008; Gul and Leung, 2004). Other studies did not find any significant association (Cheng and Courtenay, 2006). Therefore, we hypothesize that:

H9. IBs with duality in position have a lower level of corporate disclosures.

3.2.5 Board independence. Fama (1980) argued that the Board of Directors (BOD), which is elected by the shareholders, is the central internal control mechanism for monitoring managers. Chau and Leung (2006) suggested that independent directors will increase the quality of monitoring over management, because “they are not affiliated with the company as officers or employees, and thus are independent representatives of the shareholders’ interests” (Pincus *et al.*, 1989, p.246). The presence of independent

directors on boards may improve the quality of FSs (Peasnell *et al.*, 2005). Prior research supported the positive association between disclosure and board independence (Chen and Jaggi, 2000). Therefore, we hypothesize that:

H10. IBs with higher proportions of independent non-executive directors on the board have higher levels of corporate disclosures.

3.3 Corporate governance of Sharia Supervisory Board characteristics

In the context of Islam, the model of CG for business organisations is derived from the Sharia rulings. For example, they have to design the system according to Sharia principles and provide stakeholders' rights protection. According to Grais and Pellegrini (2006), the unique attributes of IBs must be clarified to improve CG mechanisms. Therefore, SSB is the most important distinction between IBs and conventional banks (Farook *et al.*, 2011; Grais and Pellegrini, 2006). Previous studies have found that the existence of the SSB and its characteristics have increased the disclosure levels of IBs (Farook *et al.*, 2011).

3.3.1 Sharia Supervisory Board size. Empirical evidence suggested that board size can affect the level of disclosure (Akhatruddin *et al.*, 2009). The common number of SSB members in IBs is between three and five members based on AAOIFI Governance Standard Number 7. According to Chen and Jaggi (2000), a larger board size may decrease the possibility of information asymmetry. Agency theory predicts that larger boards incorporate a variety of expertise, which results in more effectiveness in the monitoring role of the boards (Singh *et al.*, 2004). Moreover, a higher number of board members may also reduce the uncertainty and the lack of information (Birnbaum, 1984). The board's size is likely to affect its ability to control and review all transactions to ensure their operations. With more members, the collective knowledge and experience of SSB will increase and lead to greater disclosure. Therefore, we hypothesize that:

H11. There is a positive relationship between size of SSB and disclosure levels.

3.3.2 Sharia Supervisory Board cross-memberships. Cross-memberships of SSB members may also influence the corporate disclosure of IBs (Farook *et al.*, 2011). There is evidence that cross-directorships increase information transparency through comparing the knowledge that is gained from other companies (Dahya *et al.*, 1996) and because decisions taken at one board may become part of the information for decisions at other boards (Haat *et al.*, 2008; Haniffa and Cooke, 2002). The cross-membership of SSB members is preferable because of their ensuing knowledge and credibility (Lorsch and MacIver, 1989). Furthermore, SSB members with cross-memberships will be able to adopt their tacit and explicit knowledge into their application of Sharia rulings in Islamic banking. Therefore, we hypothesize that:

H12. There is a positive relationship between SSB cross-membership and disclosure.

3.3.3 Sharia Supervisory Board reputation. An SSB is composed of Sharia scholars who have wide knowledge of Islamic commercial law but less experience of secular educational institutions. Hussain and Mallin (2003) showed that the determinants affecting the directors' appointments in Bahraini banks are pertinent skills, business practice and reputation. Sharia scholars have an excellent reputation in their community because of their universal knowledge of Islam and their credibility and significant role in

that community. For this reason, reputation can be used as a measure for business knowledge, and therefore, scholars who have a good reputation will be able to comprehend better the modern applications of the banking industry pertaining to disclosure. Farook *et al.* (2011) indicated that reputation is instrumental in measuring the disclosure level among IBs. The reputation of an SSB is measured based on SSB membership on AAOIFI committees, which is similar to the methodology of Farook *et al.* (2011). Therefore, we hypothesize that:

H13. There is a positive relationship between SSB reputation and disclosure levels.

3.4 Culture

When scholars compare the disclosure practice of firms from diverse countries, they should consider country systems. A spacious amount of literature (Hope, 2003) has been conducted on determinants that might explain differences in accounting practices. Among the many factors studied, cultural values is claimed to be most essential. The national culture is an institutional factor that influences both managers' choices and investors' preferences regarding financial reporting (Hope, 2003). Hofstede (2001) proposed six culture dimensions which are widely used in accounting research [1] (Doupnik and Tsakumis, 2004). Jaggi and Low (2000) argued that the cultural factors of a country have an indirect impact on financial disclosures. Wong (2012) suggested that UA is the most influential cultural dimension that may affect disclosure. Therefore, in this research, we just added UA in our model to see for what extent it has impacts on the disclosure level. This consists with prior research that used only this dimension (Khlif and Hussainey, 2014). Gray (1988) argued that the higher a country ranks in terms of UA, more likely it is to rank highly in terms of secrecy or rank lower in terms of disclosure. Therefore, we hypothesize that:

H14. There is a negative association between uncertainty avoidance and disclosure.

4. Research methodology

4.1 Sample selection

We choose all fully flagged IBs that adopted AAOIFI. Based on AAOIFI (2015), there are 141 associated members, but not all of these banks adopt AAOIFI. We choose banks that adopted AAOIFI in MENA countries (i.e. Bahrain, Yemen, Qatar, Syria, Palestine, Sudan, Oman and Jordan). The analysis was limited to 2013 because we did not find significant differences between past three years (2011-2013).

4.2 Construction of disclosure indices for assessing the validity and reliability

We construct Sharia, social and financial indices based on AAOIFI standards as follows. First, we adopt the disclosure requirements of AAOIFI Governance Standard Number 1, Accounting Standard Number 1 and Governance Standard Number 7. We review the last available editions for AAOIFI (2010a, 2010b, 2010c, 2010d, 2010e) and (2014). Second, we reviewed the literature that explores CSR, SSB and FS (Aribi and Gao, 2012; Maali *et al.*, 2006; Haniffa and Hudaib, 2007; Hassan and Harahap, 2010; Belal *et al.*, 2014; Ahmed and Khatun, 2013). This enables us to construct an initial index which includes 218 items required by AAOIFI standards. Then, to ensure the content validity of the index, it is reviewed independently by three other researchers. After receiving their comments and suggestions, any remaining ambiguities were discussed with a fourth experienced academic. The final index included 214 items as shown in Table I. To

ensure the reliability of the research instrument, the principal author and two independent researchers scored five randomly selected banks. Then, the findings of the three researchers were compared. Given that the final research instrument had been agreed by all investigators, differences in the compliance scores across the investigators were not significant. Based on this, one overall index and three sub-indices (Sharia, social and financial) were constructed. The scores for the overall index and sub-indices were calculated by assigning equal weightings to each item of disclosure, and the indices were derived by computing the ratio of actual scores awarded to the maximum possible score attainable for items that were applicable to each IB.

4.3 Model specification and variable measurement

We use ordinary least squares (OLS) where the dependent variable is compliance/disclosure score and the independent variables include the factors discussed above. Therefore, we use the following OLS transformed multiple regression model:

$$\begin{aligned} Disc_i = & \beta_0 + \beta_1 AUD + \beta_2 AGE + \beta_3 SIZE + \beta_4 PROF + \beta_5 SAD \\ & + \beta_6 BLOCK + \beta_7 INST + \beta_8 FORGN + \beta_9 DUAL + \beta_{10} B.INDEP \\ & + \beta_{11} SSBSIZ + \beta_{12} SSBREPU + \beta_{13} SSBCROSS + \beta_{14} UNCER + \varepsilon \end{aligned}$$

where Disc is the compliance indices, which measures the level of compliance of SSBR, CSRR, SF and aggregate disclosure for IB *i*; β_0 is the intercept; β_1 [...]. β_{14} are regression coefficients; and ε is error term. Variables definitions are shown in Table II. The disclosure score for each index is calculated as a ratio of the total items disclosed to 15 (maximum score for Sharia) for Model 1; 104 (maximum score for financial) for Model 2; 95 (maximum score for social) for Model 3 and 214 (maximum score for aggregate disclosure) for Model 4.

5. Results of disclosure and compliance levels

5.1 Level of compliance by banks and countries

Table III shows the compliance levels for each bank over 2013. It shows that Bahrain Islamic bank, Qatar first investment bank and Cham bank are the highest bank that complies with Sharia disclosure. Jordan Islamic bank is the highest one that discloses information about CSR, whereas a Qatar Islamic bank is highest bank related to financial disclosure.

Standards	Items suggested by the author	Items suggested by independent researcher	Items suggested by second independent researcher	Final index (after fourth person's advice)	Weight (%)
FSIFI.1	110	105	100	104	49
GSIFI.1	18	20	15	15	7
GSIFI.7	90	100	94	95	44
Total	218	225	209	214	100

Table I.

Ensuring validity of research instrument

Notes: The weight is calculated based on final items for each standard dividend into total items (214); for example: weight of FSIFI.1 = $104/214 \times 100 = 49\%$

Abbreviated name	Full name	Variable description	Predicted sign	Data source	Supporting from literature
<i>Dependent variables</i>					
SSB Disc	Sharia Supervisory Board disclosure	Sharia disclosure accountability level based on SSB report		Annual reports	
CSR Disc	Corporate Social Responsibility disclosure	Social disclosure accountability level based on CSR report		Annual reports	
FIN Disc	Financial disclosure	Financial disclosure accountability level based on FS and footnotes		Annual reports	
OVER Disc	Overall disclosure	SSBR Disclosure + CSRR Disclosure + FIN Disclosure		Annual reports	
<i>Independent variables</i>					
Firm-specific characteristics					
Auditor	Auditor	Dichotomous; 1 = Bank's financial statements were audited by Big Four auditor; otherwise: 0	+	Annual report	Datar <i>et al.</i> (1991), Xiao <i>et al.</i> (2004)
AGE	Age of bank	Age of Islamic bank based on establish date	+	Annual report	Cormier <i>et al.</i> (2005), Hossain and Hammami (2009)
SIZE	Size of the bank	Log for total assets	+	Banker database	Beretta and Bozzolan, 2004, Elshandidy <i>et al.</i> (2013)
PROF	Profitability of the bank	ROA (return on assets)	+	Banker database	Wallace <i>et al.</i> (1994), Hussainey and Al-Najjar (2011)
SAD	Sharia Auditing department	Dichotomous; 1 = Bank that has Sharia auditing department; otherwise: 0	+	Annual report	Besar <i>et al.</i> (2009), Gramling <i>et al.</i> (2004), Carcello <i>et al.</i> (2005), Archambeault <i>et al.</i> (2008)
<i>Corporate governance characteristics for BOD</i>					
BLOCK	Number of blockholders	Number of blockholders – shareholders whose ownership $\geq 5\%$ of total number of shares issued	-	Banker and Zawya database	Mitchell <i>et al.</i> (1995), Schadewitz and Blevins (1998), Hossain <i>et al.</i> (1994)

(continued)

Table II.
Summary of variable
names, description
and sources

Table II.

Abbreviated name	Full name	Variable description	Predicted sign	Data source	Supporting from literature
INST	Institutional ownership	Percent of shares owned by institutional shareholders	+	Banker and Zawya database	Eng and Mak (2003), Mangena and Pike (2005)
FORGN	Foreign ownership	Percent of shares owned by foreign shareholders	+	Banker and Zawya database	Hossain <i>et al.</i> (1994), Xiao <i>et al.</i> (2004)
DUAL	Duality in position	Dummy variable, 1 if company's CEO serves as a board chairman, otherwise: 0	-	Banker and Zawya database	Haniffa and Cooke (2002), Laksmana (2008), Eng and Mak (2003), Gul and Leung (2004)
BINDEP	Board independence	Ratio of the number of non-executive directors to the total number of the directors	+	Banker and Zawya database	Haniffa and Cooke (2002), Hussainey and Al-Nejjar (2011), Abdelsalam and Street (2007), Chen and Jaggi (2000)
<i>Corporate governance characteristics for SSB</i>					
SSBSIZE	The number of the SSB	Dichotomous 1 for banks with five or more members and 0 less than five	+	Annual reports and Website	Singh <i>et al.</i> (2004), Akhatruddin <i>et al.</i> (2009), Abdul Rahman and Bukair (2013)
SSBREPU	The SSB having at least one of them sit on the board of AAOIFI	Dichotomous: reputable SSB member: 1, otherwise: 0 (Reputable scholar is one that has a position in SSB of AAOIFI and at least one SSB memberships)	+	Annual reports and Website	Hussain and Mallin (2003), Farook <i>et al.</i> (2011), Abdul Rahman and Bukair (2013)
SSBCROSS	Cross-membership of SSB	Dichotomous: SSB member with a cross membership in more than one Islamic bank: 1, otherwise: 0	+	Annual reports and website	Farook <i>et al.</i> (2011), Haat <i>et al.</i> (2008), Haniffa and Cooke (2002), Abdul Rahman and Bukair (2013)
<i>Culture</i>					
UNCER	Uncertainty avoidance	Score for each country based on data of Green Hofstede center	-	Green Hofstede center	Khelif and Hussainey (2014), Wong (2012)

Notes: Following the collapse of Arthur Andersen in 2002, the Big Five became Big Four, namely: Price water, house Coopers, Deloitte Touche Tomatsu, Ernst and Young and KPMG (Bokpin, 2013); Firm profitability (PRF) is measured by return on assets which is a more powerful measure of performance as compared to return on equity; return on assets is used here as a measure of overall earnings power of the company (Bokpin, 2013); dichotomous is a concept used to describe a variable that consists of only two categories (0 and 1) (Field, 2009); uncertainty avoidance, which is the degree to which individuals in a country prefer structured over unstructured situations, from relatively flexible to extremely rigid, to cope with risk and innovation; a low uncertainty culture emphasises a higher level of standardisation (Hofstede, 1991, 2001)

Bank	Average compliance %			Total disclosure (%)	Bank	Average compliance %			Total disclosure (%)
	Sharia (%)	Social (%)	Financial (%)			Sharia (%)	Social (%)	Financial (%)	
Tadamon International Islamic Bank	40	13	85	46	Qatar Islamic Bank	60	36	88***	61
Saba Islamic Bank, Sana	86	16	87	63	Qinvest bank	46	17	80	48
Shamil Bank of Yemen & Bahrain	60	21	72	51	Faisal Islamic Bank Sudan	73	20	67	53
Al Baraka Islamic Bank	86	49	73	69	Al Shamal Islamic Bank	60	18	63	47
Khaleeji Commercial Bank	27	24	87	46	Animal Resources Bank	6	16	75	32
First Energy Bank	80	25	74	60	Saving & Social Development Bank	53	47	68	56
Arab Banking Corporation	93*	25	77	58	Farmer's Commercial Bank	66	20	61	49
Bahrain Islamic Bank	73	46	77	72	Al Salam Bank	53	18	65	45
Venture Capital Bank	73	21	62	52	Blue Nile Mahsreg Bank	6	17	61	28
Ithmaar Bank	73	12	83	56	Al Jazeera Sudamese Jordanian Bank	66	19	57	47
Gulf Finance House	80	21	86	62	Al-Nile bank	73	18	72	54
Al Salam Bank of Bahrain	80	18	72	57	Tadamon Islamic Bank	53	16	61	43
Bank Al-khair	80	19	77	59	United Capital Bank	73	17	64	51
Global Banking Corporation	73	22	78	58	Jordan Islamic Bank	80	60***	72	71
Seera Investment Bank BSC	60	12	63	45	Islamic International Arab Bank	60	46	83	63
International Investment Bank	80	13	62	52	Jordan Dubai Islamic bank	80	39	67	62
Citi Islamic Investment Bank	60	9	74	48	Syria International Islamic Bank	80	21	63	55
Investors Bank	60	7	62	43	Cham Bank	93*	23	81	66
Qatar International Islamic Bank	46	17	66	43	Arab Islamic Bank	80	41	84	62
Qatar First Investment Bank	93*	19	63	58	The Palestine Islamic Bank	60	42	79	67
Barwa Bank	66	15	66	49	Bank Nizwa	66	21	66	51
Masraf Al Rayan	60	16	66	47					

Notes: * The highest banks score for Sharia disclosure; ** the highest bank score for social; *** the highest bank score for financial disclosure level

Table III.
Disclosure and
compliance level by
bank

In terms of the comparison between disclosures types in each country, Table IV shows the disclosure levels for each country by number of banks and percentage based on average disclosure. The table indicates that Jordan disclosed 65 per cent, which is more than Bahrain (56 per cent). This is perhaps surprising, as compliance with AAOIFI is mandatory for IBs in Bahrain. Sudan is the lowest country for compliance with AAOIFI (46 per cent). Bahrain has the highest number of banks that have adopted AAOIFI (15 IBs) not only because Bahrain is the host nation for the AAOIFI, but also because it is a requirement of the Central Bank of Bahrain that all IFIs licensed must comply with AAOIFI (Vinnicombe, 2010).

5.2 Compliance levels with Accounting and Auditing Organization for Islamic Financial Institution standards

Table V shows the compliance levels with AAOIFI Governance Standards Number 1 and 5. It shows that the average compliance level for our selected banks is 68 per cent. The disclosure level concerning with SSB members is 70 per cent, whereas the disclosure level concerned with SSB reports is 66 per cent. Information about names of SSB has got the highest items (95 per cent), whereas 22 per cent only from our sample report that they comply with AAOIFI.

Table VI shows the compliance level with AAOIFI Governance Standard Number 7. It shows that the average compliance level for our selected banks is 27 per cent, which is beyond our expectations. The disclosure level related to universal-oriented CSR items is 30 per cent, while the disclosure level related to Islamic-oriented CSR items is 23 per cent. It also shows that screening and informing clients for compliance with Islamic principles has the highest score (42 per cent) and disclosure about *Waqf* management has the lowest score (2 per cent).

Table VII shows the compliance level with AAOIFI Financial Standard Number 1. It shows that the average compliance level is 73 per cent. The disclosure level for universal-oriented financial disclosure is 86 per cent. However, the disclosure level related to Sharia-oriented financial disclosure is 36 per cent. The table shows that the average disclosure level that is recommended by AAOIFI, as well as IFRS and GAAP, for universal FSs (Financial Position Statement, Income Statement, Cash Flow

Country	No. of banks	% banks from sample		Average compliance (%)			Total average compliance (%)	Ranking of country
		No. of banks	%	Sharia (%)	Social (%)	Financial (%)		
Yemen	3	7	62	17	81	53	5	
Bahrain	15	35	72	22	74	56	4	
Qatar	6	14	62	20	72	51	6	
Sudan	11	25	53	21	65	46	7	
Jordan	3	7	73	48**	74	65	1	
Syria	2	5	87*	22	72	60	3	
Palestine	2	5	70	42	82***	64	2	
Oman	1	2	66	21	66	51	6	
Average	43	100	68	27	73	56		

Table IV.
Level of compliance by country

Notes: *The highest country score for Sharia disclosure; **the highest country score for social; ***the highest country score for financial disclosure level

	Items and corresponding AAOIFI standards (Sharia-oriented disclosure)	Total items is 15	Disclosure (%)	Compliance with AAOIFI standards	
Sharia disclosure index	<i>Items related to SSB members (SSBM)</i>		70	155	
	Names of Sharia board members		95		
	Brief about each members in the Sharia board (Background and qualifications)		40		
	The role and responsibilities of the board		70		
	The authorities of the board		88		
	The Sharia auditing department in the bank		65		
	Is the website or annual report disclose the Fatwa for the SSB related to Islamic services		63		
	<i>Items related to SSB report (SSBR)</i>		66		
	SSB report assigned from the board members		85		
	Information about the bank's responsibilities of Zakat		65		
	Information about the bank's responsibilities of activities not comply with Sharia and how bank deal with it		65		
	Information about how profit distribution process in the bank comply with Islamic Sharia		70		
	Information about the independency of the SSB with charter		37		
	Information about opinion for the SSB about compliance with Sharia		90		
	The board discloses its opinion after reviewing all documents and all financial statements for the bank		74		
	Is the report shows that the bank comply with the AAOIFI's standards		22		
	Information about the date of report and name of bank		85		
	Average compliance level	15	68		

Table V.
Compliance level with AAOIFI Governance Standards Number 1 and 5 (SSB)

Statement and Statement of Changes in the Owner's Equity) is 88 per cent, but the disclosure level related to Sharia-oriented FSs (Statement of Changes in Restricted Investments, Statement of *Zakat* and Statement of *Qard Hasan*) is 33 per cent.

Table VIII summarises the information provided by the annual reports for our 43 selected banks and discloses information about the main Islamic services, such as *Murabaha* and *Musharakah*. It shows that *Murabaha* is the most popular service provided by IBs in the MENA region (91 per cent), then *Mudaraba* 79 per cent and *Ijara* 70 per cent. *Salam* is the lowest service presented (12 per cent).

Table IX shows the overall compliance levels for the four models based on disclosure related to universal and Sharia orientation. It shows that the levels of compliance related to Sharia accountability for SSBM and SSBR are mainly similar (70 and 66 per cent). The compliance for universal CSR is 30 per cent and for Sharia

Table VI.
Compliance level
with AAOIFI
Governance
Standard Number 7
(CSR)

	Items and corresponding AAOIFI standard	Items	Disclosure (%)
Social disclosure index	<i>Universal-oriented CSR disclosure</i>		30
	Employee welfare	12	30
	Internal environment preservation policy	9	17
	Par excellence customers services	5	35
	Micro and small business and social saving and investments and development	10	33
	Charitable activates	6	37
	Social responsibility	13	28
	<i>Sharia-oriented CSR disclosure</i>		23
	Late repayments and insolvent clients	10	12
	Qard Hassan	10	15
	Zakat	7	35
	Waqf management	5	2
	Earning and expenditure prohibited by Sharia	4	32
	Screening and informing clients for compliance with Sharia	4	42
Average compliance level	95	27	

CSR items is 23 per cent. Also, the compliance related to financial information common to international standards like IFRS is 86 per cent, whereas financial disclosure related to Sharia items is 36 per cent. Finally, compliance levels for items related to universal orientation are higher than information related to Sharia requirements. This result shows low compliance and disclosure level for social reporting of IBs. This result is matching with the results of [Maali et al. \(2006\)](#); [Hassan and Harahap \(2010\)](#) and [Farook et al. \(2011\)](#) that recommend the extent of CSRD by IBs falls far short of their expectation (13.3; 38 and 16.8 per cent). [Maali et al. \(2006\)](#) indicate that IBs are not completely fulfilling their social role in accordance with the prescriptions of Islam. Based on our result, we conclude that IBs are mainly shaped and focused on economic incentives more than social norms, which consistent with the results of [Aggarwal and Yousef \(2000\)](#). [Kuran \(2003\)](#) maintains that IBs appear to seek profit as aggressively as conventional banks. He argues that it is even unrealistic to suppose IBs' activities as well as CSRD to differ or be more socially accountable than conventional as they run in the equal global capitalistic situations.

6. Empirical results

6.1 Descriptive analysis

[Table X](#) reports the descriptive statistics. It shows that the average compliance level based on the AAOIFI standard for SSB requirements is 68 per cent, the compliance level for CSR is 27 per cent and the compliance level for financial accountability is 73 per cent. Finally, the overall compliance for our selected banks is 56 per cent. In all, 65 per cent of the selected banks are audited by the Big 4 firms namely: Ernst & Young, KPMG, PricewaterhouseCoopers and Deloitte Touche Tohmatsu, and 67 per cent of the banks have a SAD. The average overall age of IBs is 19 years. The average board size is four members. In all, 71 per cent of SSB

	Items and corresponding AAOIFI standard	Total items	Disclosure (%)
Financial disclosure index	<i>Universal-oriented financial disclosure</i>		86
	Comparative financial statements	1	100
	Basic information about the bank	11	83
	Disclosure of the currency used for accounting measurement	2	88
	Disclosure of significant accounting policies	7	82
	Disclosure of contingences	1	83
	Disclosure of accounting policy changes	10	75
	Disclosure about assets and liabilities' risk	3	82
	Presentation and disclosure in the financial position	20	88
	Presentation and disclosure in the income statement	12	89
	Disclosure in the statement of cash flows	6	88
	Statement of changes in the owner's equity	10	85
	<i>Sharia-oriented financial disclosure</i>		36
	Disclosure of earning or expenditure prohibited by Sharia	2	45
	Statement of changes in restricted investments	12	42
	Disclosure in the statement of sources and uses of funds of Zakat and Sadakat	4	23
	Disclosure in the statement of sources and uses of funds, loan fund (Al Qard Al Hasan Fund)	3	35
	Average compliance level	104	73

Table VII.
Compliance level
with AAOIFI
Financial Standard
Number 1 (Financial)

Main services provided	No.	Disclosure (%)
Murabaha	39	91
Mudaraba	34	79
Ijara	30	70
Zakat	26	60
Musharakah	23	53
Sukuk	21	49
Istisna'a	11	26
Salam	5	12

Table VIII.
Disclosure about
eight main Islamic
services presented

Category of compliance	SSBR (%)	CSR (%)	Financial (%)	Overall (%)
Average % of compliance	68	27	73	56
Universal-oriented compliance %	Related to SSBM 70	30	86	58
Sharia-oriented compliance %	Related to SSBR 66	23	36	42

Table IX.
Overall disclosure
levels

Notes: SSBM: Sharia Supervisory Board Members; SSBR: Sharia Supervisory Board Report

Variables	N	Minimum	Maximum	Mean	SD
<i>Disclosure levels</i>					
SSBR	43	0.06	0.93	0.678	0.19585
CSRR	43	0.08	0.60	0.273	0.12083
FIN	43	0.31	0.85	0.731	0.12888
OVER	43	0.21	0.74	0.560	0.09600
<i>Firm specific characteristics</i>					
AUDIT	43	0.00	1.00	0.6512	0.48224
AGE	43	3.00	49.00	19.255	12.16766
SIZE	43	1.23	4.33	2.8706	0.67019
PROFIT	43	-13.39	21.57	1.6814	4.66238
SAD	43	0.00	1.00	0.6744	0.47414
<i>BOD corporate governance</i>					
BLOOK	25	0.00	7.00	2.7200	1.88237
FORIGEN	24	0.00	1.00	0.6328	0.35791
INSTITU	24	0.00	1.00	0.5750	0.29427
DUALITY	30	0.00	1.00	0.0333	0.18257
B. INDIP	24	0.00	1.00	0.4925	0.31958
<i>SSB corporate governance</i>					
SSBSIZE	43	0.00	1.00	0.1163	0.32435
SSBREPU	42	0.00	1.00	0.5000	0.50606
SSBCROSS	42	0.00	1.00	0.5714	0.50087
<i>Culture</i>					
UNCER	43	60.00	80.00	71.2558	5.61076

Notes: This table provides descriptive statistics for all of the variables defined in Table I which are as follows: SSBR: Sharia Supervisory Board Report; CSRR: Corporate Social Responsibility Report; FIN: financial disclosure that located at financial statements; OVER: overall disclosure that contain SSBR; CSRR and FIN; AUD: size of Auditor; AGE: age of bank; SIZE: size of the bank based on total assets; PROF: profitability of the bank based on ROA; SAD: Sharia Auditing department inside the bank; BLOCK: number of blockholders; INST: institutional ownership; FORGN: foreign Ownership; DUAL: duality in position; B.INDEP: board independence; SSBSIZ: the number of Sharia supervisory board members; SSBREPU: the SSB having at least one of them sit on the board of AAOIFI; SSBBCROSS: the SSB having at least one of them sit on the other Islamic bank' SSB (Cross membership of SSB); UNCER: uncertainty avoidance

Table X.
Descriptive statistics

members have cross-membership with SSBs in other IBs (e.g. Sheikh Abdul Sattar Abu Ghuddah is a member of the SSBs of more than ten IBs). In all, 50 per cent of our SSB members are also members of AAOIFI committees and 57 per cent of our SSB are members in more than one IB (cross-membership). The average number of blockholders is three, mean institutional ownership is 58 per cent and the average foreign ownership is 63 per cent. The mean percentage of independent directors on the board is 49 per cent.

6.2 Regression results

Regression results are shown in Table XI. It shows the cross-sectional OLS regressions for the aggregated score of disclosures and three sub-categories (SSB, CSR and FS). For

the SSB score (Model 1), we find that the coefficient estimates variables related to CG of SSB are positive and significant at the 5 per cent level. This result supports *H11*, *H12* and *H13* that IBs which have SSBs with more than four members, as well as SSB members who have cross-membership with SSBs in other IBs and IBs with SSB members who are also members of AAOIFI committees disclose more Sharia information in their annual reports and websites. Furthermore, the coefficient estimates on SADs is positive and significant. This supports *H5*. Concerning Model 2, the table shows that CSR is positive and significant with SIZE of bank at the 5 per cent level. This result supports *H3*. Furthermore, the coefficient estimate on AGE is positive and significant, indicating that older IBs disclose more information about social activities, which supports *H2*. For Model 3, we find that the coefficient estimates on SIZE and SAD are positive and significant. Therefore, we partially accept *H3* and *H5*. Regarding aggregate compliance (Model 4), we find significant positive association between overall compliance and SIZE, AGE and SSB SIZE at the 10 per cent level. Therefore, *H2*, *H3* and *H11* are partially accepted. For culture, we find that UA has a negative association with Sharia as well as aggregate disclosure level at the 10 per cent level (Models 1 and 4). This result is consistent with that of [Elshandidy et al. \(2013\)](#), who found a negative association between UA and disclosure. These results, therefore, support the acceptance of *H14*.

7. Discussion

The insignificant associations between corporate disclosure and auditors are consistent with prior research ([Barako et al., 2006](#); [Owusu-Ansah, 1998](#); [Hossain et al., 1995](#)). Our analysis identifies a significant association between disclosure level and existing SAD. This finding is consistent with previous literature, which presents SAD as one of the main determinants of compliance with AAOIFI and shows that the internal audit function can enhance the disclosure quality ([Bailey et al., 2003](#); [Gramling et al., 2004](#); [Carcello et al., 2005](#)). Bank age is positively correlated with compliance. Empirically, we confirm the findings of [Cormier et al. \(2005\)](#) and [Hossain and Hammami \(2009\)](#), who reported a positive relationship between company age and corporate disclosure. The significant associations between corporate disclosure and bank size are consistent with prior empirical studies which identified company size as a determinant of disclosure level ([Ahmed and Courtis, 1999](#); [Street and Gray, 2001](#)). We found that profitability is not associated with disclosure level. This result supports the argument that providing full disclosure in any situation is important whether it is achieving a profit or not ([Haniffa, 2002](#)). Also, this result is consistent with the findings of other researchers who did not find association between profitability and disclosure ([Aras et al., 2010](#)).

The results do not support that CG attributes concerned with BOD have a significant effect on corporate disclosure. Based on our analysis, we found an insignificant link between duality in position and corporate disclosure. This result is supported by [Ho and Wong \(2001\)](#), [Arcay and Vazquez \(2005\)](#) and [Cheng and Courtenay \(2006\)](#). Related to institutional ownership, our outcome is consistent with [Eng and Mak \(2003\)](#), who found an insignificant relationship between the two variables. Our paper concludes an insignificant association between compliance levels and board independence, which is consistent with [Haniffa and Cooke \(2002\)](#) and [Ho and Wong \(2001\)](#), who did not find a relationship between the two variables. We find that the coefficient estimates on blockholders and foreign ownership have an insignificant association with corporate

Table XI.
Regression results

Categories	Variables	Model 1 Sharia disclosure			Model 2 Social disclosure			Model 3 Financial disclosure			Model 4 Aggregate disclosure			
		Beta	t	Significance	Beta	t	Significance	Beta	t	Significance	Beta	t	Significance	VIF
Constant		2.605	0.015		1.140	0.264		0.983	0.329		3.301	0.003		
Firm-specific characteristics	AUDIT	0.156	0.772	0.447	0.252	1.437	0.162	-0.054	-0.270	0.789	0.185	1.162	0.255	2.354
	AGE	0.000	0.001	0.999	0.522	3.770	0.001***	0.098	0.619	0.541	0.275	2.197	0.036*	1.466
	SIZE	-0.026	-0.152	0.881	0.277	1.824	0.079*	0.670	3.841	0.001***	0.393	2.856	0.008**	1.767
	PROFIT	0.016	0.105	0.917	0.054	0.399	0.693	0.106	0.679	0.503	0.083	0.677	0.504	1.417
	SAD	0.443	2.757	0.010**	-0.185	-0.997	0.328	0.283	1.762	0.089*	0.187	1.472	0.152	1.498
Culture	UNCER	-0.365	-1.710	0.098*				0.004	0.018	0.986	-0.317	-1.880	0.071*	2.648
	BLOOK	0.093	0.586	0.563	0.081	0.584	0.564	-0.061	-0.386	0.702	0.068	0.538	0.595	1.473
	FORIGEN	0.010	0.056	0.956	-0.225	-1.484	0.149	-0.130	-0.749	0.460	-0.145	-1.053	0.301	1.766
	INSTITU	-0.024	-0.140	0.889	0.062	0.417	0.680	0.138	0.807	0.427	0.060	0.447	0.658	1.696
Corporate governance of SSB	DUALITY	-0.020	-0.114	0.910	-0.249	-1.597	0.121	-0.145	-0.812	0.424	-0.189	-1.344	0.190	1.854
	B.INDIP	-0.008	-0.048	0.962	-0.174	-1.136	0.265	-0.197	-1.125	0.270	-0.162	-1.174	0.250	1.786
	SSBSIZE	0.288	1.841	0.076*	-0.016	-0.114	0.910	0.159	1.021	0.316	0.261	2.122	0.043*	1.417
	SSBREPU	0.560	1.788	0.085*	0.027	0.097	0.923	0.276	0.883	0.385	0.248	1.003	0.324	5.683
Model summary: R ²		0.831	2.209	0.035*	0.005	0.015	0.988	-0.240	-0.641	0.527	0.463	1.562	0.130	8.194
			0.517			0.634			0.518			0.700		
F-value			2.142			3.464			2.153			4.663		
p-value			0.042			0.002			0.041			0.000		

Notes: This table presents ordinary least squares (OLS) regressions on the factors that influence disclosures for banks that adopt AAOIFI. Based on our research, we formulated three models and aggregate model; Model 1 focus on compliance with Sharia AAOIFI disclosure requirements; Model 2 emphasises on compliance with social AAOIFI disclosure requirements; Model 3 emphasises on compliance with financial AAOIFI disclosure requirements; Model 4 gathers the three models (Sharia; social and financial); AUD: size of Auditor; AGE: Age of bank; SIZE: size of the bank based on total assets; PROF: profitability of the bank based on ROA; SAD: Sharia auditing department inside the bank; BLOCK: number of blockholders; INST: institutional ownership; FORGEN: foreign ownership; DUAL: duality in position; BINDEP: board independence; SSBISZ: the number of Sharia supervisory board members; SSBREPU: the SSB having at least one of them sit on the board of AAOIFI; SSBKROSS: the SSB having at least one of them sit on the other Islamic bank SSB (Cross membership of SSB); UNCER: uncertainty avoidance (culture). *** Correlation is significant at the 1% level; ** Correlation is significant at the 5% level; * Correlation is significant at the 10% level. The R² indicates that the corporate characteristics as well as CC selected for the purposes of this study explain at 52% (sharia model), 63% (social model) and 70% (aggregate model) the variation in banks' levels of compliance with AAOIFI disclosures requirements

disclosure. The insignificant sign on the number of blockholders is consistent with the research of [Samaha and Dahawy \(2011\)](#), who did not find association between the variables. The insignificant link between foreign ownership and disclosure is consistent with [Mangena and Tauringana \(2007\)](#).

The significant associations between disclosure and CG variables concerned with SSB are consistent with prior empirical disclosure reporting research ([Singh et al., 2004](#); [Abdul Rahman and Bukair, 2013](#); [Hussain and Mallin, 2003](#), [Farook et al., 2011](#); [Haat et al., 2008](#); [Haniffa and Cooke, 2002](#); [Abdul Rahman and Bukair, 2013](#)). [Gray \(1988\)](#) and [Salter and Niswander \(1995\)](#) showed that measures of national culture can help explain cross-country differences in accounting practices particularly with regard to disclosure level. The analysis shows that culture based on UA has a negative association with disclosure level (Sharia and aggregate). This result is supported by [Hope \(2003\)](#), who showed that cultural values are determinants of differences between disclosure levels. Consequently, the purpose to achieve international convergence for IFIs, a main goal of AAOIFI, should be expanded from merely adopting a single set of high-quality accounting standards to considering the cultural values of Islamic countries as well as other countries that have IBs or even Islamic windows around the world.

8. Conclusion

We measured to what extent IBs that adopt AAOIFI standards are consistent with AAOIFI requirements. We also associated variations in SSB, CSRR and FSs disclosure levels with variations in both firm characteristics and CG mechanisms related to BOD and SSB. The findings of this study illustrate a relatively low average level of compliance with AAOIFI disclosures related to social requirements (27 per cent). It also indicates a relatively high average level of compliance with AAOIFI disclosures related to Sharia and financial requirements. This approximates to 68 per cent for SSB and 73 per cent for financial disclosure level. We find that the CG mechanisms related to SSB have significantly high explanatory power over Sharia disclosure variations when compared with CG mechanisms related to BOD. This can be explained based on the fact that AAOIFI standards for our selected banks are mandatory, and BOD does not have a direct role in ensuring compliance with standards, whereas SSB has a significant role in preparing reports about the compliance level with Sharia. We find also that firm characteristics (age, size and SAD) have a significant impact on disclosure variations.

These results have theoretical and practical implications. They suggest that more attention should be paid to variables that may explain the variations in Sharia, social and financial disclosure, particularly those concerned with SSB. Our suggestion is consistent with a recent trend in the accounting literature ([Farook et al., 2011](#); [Abdul Rahman and Bukair, 2013](#)) for research to look more deeply at the SSB characteristics of CG. The practical implication of our results lies in our empirical evidence relevant to the importance and benefits of compliance with AAOIFI standards which has a significant impact on the image of IBs as well as approving Sharia compliance and serving the society, which represent the main competitive advantages for these banks. Our results suggest that more attention should be paid to the adoption of AAOIFI, particularly for IBs who are members without adopting. Looking more closely at the variations in compliance with AAOIFI and the disclosure levels between the IBs in each country is useful for clearly identifying the extent to which the regulatory approach relies on either regulations or mandatory and voluntary disclosure. Furthermore, AAOIFI should take

measures to make their standards mandatory for all their members as a first step to making it compulsory for all IFIs. When we measured the disclosure levels for each country, we found that Bahrain is located in the fourth place after Jordan, Syria and Palestine. Consequently, we recommend that the Central Bank of Bahrain further investigate this issue and explore the reasons and the scope for enhancing compliance with AAOIFI.

Our results related to compliance levels of banks with AAOIFI add significantly to Islamic accounting literature by emphasising the importance of widening this research scope to pay more attention to variations above the mandated requirements (AAOIFI adoption), which provide a minimum amount of information to all stakeholders. The results indicate that organising reporting by IBs that formally implement an accounting standard (AAOIFI) significantly improves the disclosure level for Sharia compliance by encouraging them to care about their SSB report. The results support the current trend in the regulations in Bahrain, Sudan and Jordan, which encourage the mandatory adoption of AAOIFI by IBs. The unweighted disclosure index is adapted to measure the compliance level with AAOIFI. However, this kind of disclosure index has an important limitation, as the number of disclosure items required by different standards varies considerably. As in our research, some standards require a large number of items (104 items) to be disclosed (Accounting Standard Number 1), whereas others require only a few items (15 items) to be disclosed (Governance Standard Number 1). This may become a significant problem when studies examine compliance with AAOIFI disclosures. An alternative method recommended for future research to avoid this problem is the “partial compliance un-weighted approach” which was used by [Street and Gray \(2001\)](#). Furthermore, our paper only focused on three AAOIFI standards, and further research may examine other standards.

Further research could consider other variables that might affect compliance levels such as gross domestic product, corruption index and audit committee, leverage, ownership structure and other culture dimensions. In this study, the sample is restricted to IBs in eight countries that adopted AAOIFI standards during 2013. Further studies could extend the sample to other countries that have IBs and extend the covered period. Future research could also investigate the level and determinants of compliance levels with AAOIFI standards for other financial institutions. Finally, additional research could be undertaken to examine the economic consequences of the compliance with AAOIFI standards.

Note

1. Hofstede six dimensions are power distance (PD), uncertainty avoidance (UA), individualism (IND), masculinity (MAS), long-term orientation (LTO) and Indulgence (INDU).

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