

The Convergence of the Divine and the Debit: A Comprehensive Analysis of the Interplay Between Islamic Fiqh and Modern Accounting Standards (2018–2025)

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ABSTRACT

Objective: This study investigates the epistemological and technical convergence between Islamic jurisprudence (Fiqh al-Muamalat) and modern accounting frameworks (IFRS and AAOIFI) from 2018 to 2025. **Method:** Adopting a qualitative systematic literature review (SLR), the research synthesizes data from academic journals, regulatory standards (FAS 30, 39, 44), and industry reports to analyze the reporting discrepancies in Islamic financial institutions. **Findings:** The analysis reveals a persistent "comparability paradox" where identical economic transactions are reported differently under IFRS (substance over form) versus AAOIFI (form over substance). Key divergences are identified in the treatment of Murabaha (sale vs. loan), Mudarabah (equity vs. liability), and lease accounting. Furthermore, the study highlights the emergence of new regulatory frontiers, including the standardization of Zakat calculation and the accounting for digital assets. **Implications:** The study concludes that while harmonization efforts are accelerating, distinct ontological roots necessitate a dual-reporting approach in many jurisdictions to satisfy both global investors and Shariah compliance requirements.

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I. INTRODUCTION

The global financial architecture, long dominated by the secular paradigms of Western capitalism, has witnessed the ascent of a formidable alternative in recent decades: Islamic finance. With industry assets breaching the US\$4.9 trillion mark in 2023 and projected to surpass US\$7.5 trillion by 2028 (LSEG, 2024; LSEG, 2025) 12, Islamic finance has graduated from a niche marketplace to a systemic component of the global economic order. This meteoric rise, driven by powerhouse economies such as Saudi Arabia, Malaysia, and Iran—which collectively account for 72% of global Islamic finance assets (LSEG, 2025) 1—has precipitated a profound intellectual and technical crisis in the realm of financial reporting. At the heart of this crisis lies a fundamental tension between the immutable laws of Fiqh al-Muamalat (Islamic commercial jurisprudence) and the evolving frameworks of modern accounting, primarily the International Financial Reporting Standards (IFRS) and the Generally Accepted Accounting Principles (GAAP).

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The intersection of accounting and Fiqh is not merely a technical exercise in bookkeeping; it is a philosophical confrontation between two distinct worldviews. Conventional accounting is predicated on economic rationalism, focusing on the "substance over form" of transactions to provide investors with information useful for predicting future cash flows (Velayutham, 2014).³ In contrast, Islamic accounting is rooted in the concept of Tawhid (the unity of God) and Khilafah (vicegerency), where the validity of a transaction depends heavily on its legal form and adherence to Shariah prohibitions against Riba (usury), Gharar (excessive uncertainty), and Maysir (gambling). If the legal form of an Islamic contract is compromised to fit a conventional accounting definition—for instance, treating a Murabaha sale as a secured loan—the transaction may be rendered void from a religious perspective (Djessas et al., 2025).⁴ Between 2018 and 2025, this tension has catalyzed a flurry of regulatory activity. The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) has aggressively modernized its Financial Accounting Standards (FAS) to bridge the gap with global practices while preserving Shariah integrity. Key developments include the overhaul of Zakat reporting through FAS 39 (AAOIFI, 2022) ⁵, the alignment of impairment models with global expected credit loss (ECL) norms via FAS 30 (AAOIFI, 2020) ⁶, and the nascent codification of digital asset accounting under FAS 44 (AAOIFI, 2025).⁷ Simultaneously, jurisdictions like Saudi Arabia have navigated the complex terrain of mandatory IFRS adoption, necessitating innovative "workarounds" to reconcile international compliance with domestic religious mandates (Chambers, 2025).

II. LITERATURE REVIEW

The Epistemological Divide: Theistic Agency vs. Economic Rationalism

The academic discourse during the review period has been heavily preoccupied with the ontological differences between conventional and Islamic accounting. Conventional accounting theory views the business entity as separate from its owners, operating with the primary objective of maximizing shareholder wealth. In contrast, literature reinforces the view that Islamic accounting is a "social construction" deeply embedded in religious values (Velayutham, 2014). Scholars argue that Islamic accounting cannot be decoupled from Maqasid al-Shari'ah (objectives of Islamic law), necessitating disclosures that conventional standards often deem irrelevant, such as the amount of Haram income or the social impact of Zakat distributions (Khan et al., 2021).

Recent studies have critiqued the "pragmatic approach" of adapting conventional standards for Islamic institutions. For example, treating Mudarabah investment accounts as liabilities under IFRS ignores the risk-sharing nature of the contract, effectively secularizing the instrument into a conventional deposit (IASB & AAOIFI, 2024). This "Anglicization" of Islamic accounting is viewed by purists as a threat to the industry's legitimacy, prompting calls for a return to a "constructive approach" where standards are derived directly from Fiqh sources.

The Regulatory Dichotomy: AAOIFI vs. IFRS

The literature reveals a fragmented global regulatory landscape. Research identifies a clear split between AAOIFI-centric jurisdictions (e.g., Bahrain) and IFRS-converged jurisdictions (e.g., Malaysia, Saudi Arabia).

1. AAOIFI-Centric: Research in these regions highlights the high degree of alignment between financial reporting and Shariah requirements, particularly in the treatment of leases where the lessor retains ownership risk (Djessas et al., 2025).
2. IFRS-Converged: In these jurisdictions, Islamic banks face "dual compliance" challenges, often requiring distinct internal ledgers to satisfy both the central bank (IFRS) and the Shariah board (Wolters Kluwer, 2024).

Shariah Governance and Financial Reporting Quality

A significant body of empirical research investigates the link between Shariah governance mechanisms and reporting quality. Studies utilizing Agency Theory suggest that robust Shariah Supervisory Boards (SSB) reduce information asymmetry (Al-Matari et al., 2022). Empirical evidence from Indonesia (2019–2023) indicates that while the Board of Directors positively influences financial performance, the efficacy of SSBs is often mediated by the quality of Corporate Social Responsibility (CSR) disclosures (Husaeni

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& Dewi, 2024). Furthermore, the adoption of AAOIFI standards has been statistically linked to lower levels of earnings management and higher reporting conservatism compared to IFRS adoption alone (Mejri et al., 2022)

III. METHODS

This report employs a qualitative systematic literature review (SLR) methodology to synthesize the state of knowledge regarding the intersection of Accounting and Fiqh. The research design involves the triangulation of data from three primary sources: academic scholarship, regulatory texts (AAOIFI and IASB standards), and industry performance reports.

Data Collection

The research material covers the period from 2018 to 2025. The selection criteria prioritized:

1. **Thematic Relevance:** Documents explicitly addressing the accounting treatment of Islamic financial instruments and the AAOIFI-IFRS comparison.
2. **Temporal Scope:** Recent updates including FAS 39 (Zakat), FAS 30 (Impairment), and FAS 44 (Digital Assets) were prioritized (AAOIFI, 2022; AAOIFI, 2025).
3. **Source Authority:** Data includes peer-reviewed articles from journals such as the Journal of Islamic Accounting and Business Research, official AAOIFI announcements, and reports from LSEG (LSEG, 2025).

IV. RESULTS AND DISCUSSION

The analysis reveals a complex landscape where theological mandates and financial engineering are in constant negotiation. The results are discussed under **four main thematic pillars**.

1. The Accounting Treatment of Sale-Based Contracts: Murabaha and Ijarah

Murabaha (Cost-Plus Sale): Under AAOIFI FAS 2, Murabaha is recognized as a sale. The asset must appear on the bank's books to ensure the bank assumes ownership risk (damun), justifying the profit (Djessas et al., 2025). Conversely, IFRS 9 focuses on cash flow characteristics. Since Murabaha results in fixed payments, IFRS views the "economic substance" as a financing arrangement. However, Murabaha often fails the "Solely Payments of Principal and Interest" (SPPI) test because the markup is technically profit, not interest. This potentially forces banks to use Fair Value Through Profit or Loss (FVTPL) measurement, creating volatility (Wolters Kluwer, 2024). To address this in mandatory IFRS jurisdictions like Saudi Arabia, banks utilize "Dual Tranche" structures—combining a long-term fixed Murabaha with a series of spot Murabahas—to manage the transition to Risk-Free Rates without violating the prohibition on Gharar (Chambers, 2025).

A sharp conflict exists regarding leasing. IFRS 16 treats most leases as finance leases, requiring the lessor to derecognize the asset and record a receivable. In contrast, AAOIFI FAS 8 requires the lessor to keep the asset on the balance sheet to validate the legitimacy of charging rent (Morshed & Szeles, 2020). If a bank derecognizes the asset per IFRS, it theoretically admits it does not own it, rendering the rental income Riba (Djessas et al., 2025).

2. The Equity-Liability Conundrum: Mudarabah

In Mudarabah (trust financing), capital providers share profits but bear all financial losses. IFRS Classification (IAS 32): Because account holders can typically withdraw funds on demand, IFRS classifies these funds as Financial Liabilities (IASB & AAOIFI, 2024).

1. AAOIFI Classification: AAOIFI recognizes the hybrid nature of these funds, classifying them as "Equity of Investment Account Holders" (EIAH), a mezzanine category between liability and equity (IASB & AAOIFI, 2024).
2. Risk Implications: A study of Indonesian Islamic banks (2008–2020) found that Mudarabah financing reduces risk only when it constitutes between 5.5% and 12.6% of the total portfolio; outside this range, it increases Non-Performing Financing (NPF) (Husaeni & Dewi, 2024).

3. Modernizing the Standards: Zakat and Impairment

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FAS 39: Financial Reporting for Zakat (Effective 2023): This standard harmonizes Zakat reporting, mandating specific calculation methods. It clarifies that the Zakat rate is 2.5% for the lunar year and 2.5775% for the solar year to account for the difference in days (AAOIFI, 2022). It supersedes FAS 9, requiring clearer separation between corporate Zakat liability and Zakat paid on behalf of shareholders.

FAS 30 vs. IFRS 9 (Impairment): FAS 30 was issued to align with the forward-looking Expected Credit Loss (ECL) model of IFRS 9 but with Shariah modifications. It bifurcates assets into "Receivables" (subject to credit risk/ECL) and "Investments" (subject to market risk impairment), preventing the application of default probabilities to equity-like partnership contracts (KPMG, 2017).

4. Emerging Frontiers: Digital Assets

As of 2025, the accounting for digital assets represents the newest frontier. AAOIFI issued FAS 44 "Determining Control of Assets and Business" to address digital asset recognition (AAOIFI, 2025). The core Fiqh debate concerns whether crypto qualifies as Mal (wealth). Research suggests that if crypto is held for investment, it should be treated similarly to equity (Fair Value), provided the underlying activity is Shariah-compliant (World Scientific, 2023).

V. CONCLUSION

The period from 2018 to 2025 serves as a testament to the resilience and adaptability of Islamic accounting. The exhaustive review of literature and standards demonstrates that the field has moved beyond the initial phase of "defensive distinction" toward a mature phase of "principled engagement."

First, the "Standards War" has not ended in a victory for either side but rather a stalemate of coexistence. While IFRS provides the global language of capital, AAOIFI provides the dialect of legitimacy. The value relevance studies confirm that the market values the specific information AAOIFI provides, particularly regarding Takaful and risk-sharing (Mejri et al., 2022). Second, the data conclusively links robust Shariah governance with superior financial reporting quality. The SSB acts as a vital check on agency costs, ensuring that the "Trust" (Amanah) aspect of Islamic finance is reflected in the numbers (Al-Matari et al., 2022). Third, the cases of Saudi Arabia and Malaysia illustrate that convergence requires constant innovation—such as the "dual tranche" Murabaha or "temporary Syirkah funds"—to prevent secular standards from invalidating religious contracts (Chambers, 2025).

Looking ahead, the integration of Maqasid al-Shari'ah into sustainability reporting represents the next great frontier. Furthermore, the digitization of Islamic finance will force a reckoning for accounting standards. When a Murabaha is executed via a smart contract on a blockchain, the accounting entry must be automated. Whether that automation follows the logic of FAS 2 (Sale) or IFRS 9 (Loan) will determine the very soul of the digital Islamic economy. Ultimately, the harmonization of "Revelation and Reporting" remains an unfinished project, requiring a continuous dialogue between the scholars of the text (Fuqaha) and the scholars of the ledger (Accountants).

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