

THE DIFFERENCES BETWEEN WESTERN VIEWS AND ISLAMIC VIEWS OF FINANCIAL REPORTS WITH RELATIONS TO THE FIVE OBJECTIVES OF SHARIAH AND THREE LEVELS OF MAQASID PARADIGM

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Abstract

Financial reporting are one of the most important elements that is usually use to know the financial information in an organisation either it's finance is in a good condition or otherwise. The purpose of this paper is to enhance one's knowledge base by discussing and sharing the current inconsistencies between western and Islamic financial reports. The following are the study's objective in further detail which are to know the inconsistencies between western and Islamic financial reports as well as to analyse the relationship of financial reports with the five objectives of shariah and three levels of *maqasid* paradigm. The problems arise in this issues are due to the conflicts between western and Islamic views on financial reports in organisations as well as conflicts in the used of financial reports from western views or Islamic views in Islamic organisations. The methodology applied is qualitative, which are study through articles and journals. Therefore, the findings that are found in this study is the analysis of comparative between the financial reports from western or conventional views and Islamic views in terms of the balance sheet and income statement like zakat elements and Islamic derivatives financial instruments in Islamic views. There is a lack of academic research in the comparative of financial reports from western views and Islamic views especially in terms of its relationship with the five objectives of shariah and three levels of *maqasid* paradigm (*al-dharuriyyat*, *al-hajiyyat* and *al-tahsiniyyat*). Thus, this study provides the information on the comparative analysis between the two views as well as the relationship with the five objectives of shariah and three levels of *maqasid* paradigm.

Keywords: *Western and Islamic views, Financial reports, Maqasid shariah, Maqasid paradigm*

PERBEZAAN PANDANGAN BARAT DAN PANDANGAN ISLAM TERHADAP PELAPORAN KEWANGAN SERTA KAITANNYA DENGAN LIMA OBJEKTIF SYARIAH SERTA TIGA PERINGKAT PARADIGMA MAQASID

Abstrak

Pelaporan kewangan adalah salah suatu elemen terpenting yang biasanya digunakan untuk mengetahui maklumat kewangan dalam sesebuah organisasi sama ada kewangannya berada dalam keadaan baik atau sebaliknya. Tujuan penulisan artikel ini adalah untuk meningkatkan asas pengetahuan seseorang dengan membincangkan dan berkongsi ketidakselarasan semasa antara laporan kewangan barat dan Islam. Berikut adalah objektif kajian secara terperinci iaitu untuk mengetahui ketidakselarasan antara laporan kewangan barat dan Islam serta menganalisis hubungan laporan kewangan dengan lima objektif

syariah dan tiga peringkat paradigma maqasid. Permasalahan yang timbul dalam isu ini adalah disebabkan oleh percanggahan pandangan barat dan Islam terhadap laporan kewangan dalam organisasi serta konflik dalam penggunaan laporan kewangan dari pandangan barat atau pandangan Islam di dalam sesebuah organisasi Islam. Metodologi yang digunakan adalah kualitatif iaitu kajian melalui artikel dan jurnal. Oleh itu, dapatan yang ditemui dalam kajian ini adalah melalui analisis perbandingan antara laporan kewangan dari pandangan barat atau konvensional dan pandangan Islam dari segi kunci kira-kira dan penyata pendapatan seperti terdapat elemen zakat dan instrumen kewangan terbitan Islam menurut pandangan Islam. Terdapat kekurangan kajian akademik dalam perbandingan laporan kewangan dari pandangan barat dan pandangan Islam terutamanya dari segi hubungannya dengan lima objektif syariah dan tiga peringkat paradigma maqasid (*al-dharuriyyat*, *al-hajiyyat* dan *al-tahsiniyyat*). Justeru itu, kajian ini memberi maklumat tentang analisis perbandingan antara kedua-dua pandangan serta hubungannya dengan lima objektif syariah dan tiga peringkat paradigma maqasid.

Kata kunci: *Pandangan Barat dan Islam, Laporan kewangan, Maqasid syariah, Paradigma Maqasid*

INTRODUCTION

Financial reporting can be referred as the transmission of financial information, such as financial statements, to financial statement users, such as investors and creditors. According to the Malaysia World's Islamic Finance Marketplace (2023), there is statistics shown that the global Islamic finance industry to grow by 10% in 2023 to 2024 despite there is economic slowdown. Therefore, financial reporting is a standard accounting technique in which financial statements are used to reveal a company's financial information and performance over a specific time period, usually annually or quarterly (Bensoussan, 2020). A financial report, in basic terms, is essential for knowing how much money that the company have, where it comes from, and where it needs to go. Financial reporting allows managers to make knowledgeable business decisions based on the financial health of the firm. In addition, the company's financial reporting will also be used by potential investors and banks to determine if they want to invest or lend the money to the company (Drury, 2021). A balance sheet, income statement, statement of owner's equity, and statement of cash flows are all part of a general purpose set of financial statements, but financial reporting is much more than that. Financial reporting encompasses all financial communication from the company to outside parties, including press releases, shareholder minutes, management letters and analyses, auditor reports, and even the financial statement notes (Bonetti et al., 2016). Basically, it is referring to anything that may be used to communicate financial facts to the general public.

There are three levels of financial reporting which are level one is compilation, level two is financial statement review and level three is audit. Level one of compilation is occur when Certified Public Accountant (CPA) assist a customer in presenting financial information in the form of financial statements (Doyle et al., 2007). A CPA does not review documentary evidence, do any inquiry or analytical methods, test any underlying financial data, or conduct any type of fraud risk assessment during a compilation. Then, the second level is financial statement review. Financial statement reporting is a review that is costlier and time consuming than a compilation since the CPA will undertake analytical processes and make inquiries with company employees to give limited confidence that the financial statement presentation is free of major mistakes (Clor-proell et al., 2014). Next, the third level is audit. The audit is the highest and most expensive degree of independent financial reporting. In order to identify fraud risk areas, the audit engagement team will meet prior to fieldwork to create audit tests and review internal controls (Carcello et al., 2004). During this level, CPA has the obligation to develop, implement, and maintain internal controls to prevent and identify fraud. Overall, CPA

has a responsibility to inquire about any known cases of fraud and to bring any issues or concerns to management's notice.

Next, in elaborating the multidimensional process of sustainable development from an Islamic perspective, Nouh (2012), stating that Islam promotes a balance between economic and social development on the one hand, and environmental importance on the other, in order to maintain efficient and effective resource utilisation. The key to success is happiness, and the *maqasid*, which means "in the end," according to Laldin et al. (2013), is the key to pleasure, comfort, and contentment (Rasool et al., 2018). In terms of long-term comfort and sustenance, the Islamic *maqasid* al-shariah, which encompasses the five exegeses of protections, such as life, belief, honour, intellect, and property, which, in other words, provide a peaceful, clean, and decent living, i.e. Hayat-e-Tayyaba (Rasool et al., 2018), may be enormously indispensable. According to Alam et al. (2015), the Islamic set of principles led by *maqasid* aims to achieve *masalih* (betterment) in society under the Islamic paradigm (Dusuki et al., 2011). In terms of shariatic applications, the *maqasid* collection of rules addresses the why and how issues. As a result, this *maqasid* enshrines the common knowledge, as expressed by Maslow in his hierarchic theory, in which self-actualization is the primary objective in reaching the greatest level of life achievement (Ahmed et al., 2011; Alam et al., 2015; Bakar et al., 2011; Dusuki et al., 2011).

RESEARCH ISSUES

The problems arise in this issues are due to the conflicts between western and Islamic views on financial reports in organisations as well as conflicts in the used of financial reports from western views or Islamic views in Islamic organisations.

RESEARCH OBJECTIVES

The major objective of this paper is to enhance one's knowledge base by discussing and sharing the current inconsistencies between western and Islamic financial reports. The following are the study's aims in further detail which are to know the inconsistencies between western and Islamic financial reports as well as to analyse the relationship of financial reports with the five objectives of shariah and three levels of *maqasid* Paradigm.

METHODOLOGY

The methodology that has been used in this study is qualitative in nature. The qualitative data sources that collects information which are relevant to the research objective. One of the ways that are being used are by using document analysis with reviewing and evaluating documents from both printed and electronic which comprises of computer-based and internet-transmitted material. This data analysis requires data that be examined and interpreted in order to acquire meaning, gain understanding, and develop empirical knowledge. The sources include observation by using various documents and texts as well as refer to journals, and websites to obtain information related to the study.

ANALYSIS OF ISSUES – FINDINGS

General Western Views

According to western views, financial reports is a type of information system that recognises, documents, and communicates an organization's economic events to relevant parties (Akkas et al., 2008). This communication is usually in the form of financial statements in monetary terms, all under the supervision of competent management. The traditional accounting method is designed to aid economic decision-making, with the ultimate goal of effectively allocating

scarce resources in lucrative ways. As a result, in western views, it's refers to accounting systems that identify, measure, and record the financial elements of a company and convey the information to interested consumers without adhering to Islamic shariah.

General Islamic Views

According to Islamic views, financial reports is a style of accounting that defines its goals and conducts all of its activities in order to achieve those (goals) ethically and objectively within the constraints and boundaries of Islamic shariah. In other words, Islamic views refers to the financial reports system that identifies, measures, records, and analyses the financial elements of a business in accordance with Islamic shariah (Islam SMF, 2015). In reality, Islamic views refers financial reports that delivers required financial and non-financial information to a company's stakeholders, ensuring that the entity continues to operate within the Islamic shariah's limits. Islamic accounting is a powerful instrument that allows Muslims to assess their personal accountability to Allah (SWT), the Almighty.

Differences Between Western and Islamic Views on Financial Reports

One of the distinctions between western and Islamic perspectives on financial reports is that Islamic organisations provide shariah advisory reports, which are not supplied by western or non-Islamic organisations. The report from Islamic institutions, on the other hand, is far more thorough than the one from non-Islamic organisations. They included more precise descriptions of what the committee discussed, evaluated, and authorised during the financial year through meetings for Islamic reports. This is crucial in determining whether or not an organization's product creation adheres to shariah regulations. In addition, the discrepancies in the financial statements are attributable to the fact that the activities are different between Islamic and western views. Although the names of the transaction descriptions may appear to be almost same, the real source or occurrences are not. The discrepancies in title for transactions in balance sheets and income statements are seen in Tables 1 and 2.

Table 1: Differences of components in Balance Sheet of Islamic and Western Views

Items	Western Views	Islamic Views
Assets	Cash and short-term funds Deposits and placements Loan & Advances Statutory Deposits Fixed Assets Other Assets	Cash and short term funds Deposits and placements Financing & Advances Statutory Reserve Fixed Assets Other Assets
Liabilities	Deposits Bill & Acceptances Derivative Liabilities Provision of tax	Deposits Bill & Acceptance Islamic derivative financial instruments Provision of tax and zakat
Equity	Owners' Equity	

Sources: Safeza et al., 2012

Generally Islamic and western views on assets site do have cash and liquid assets. But in Islamic views, these are mainly cash assets and not instruments like treasury bills as in the western views. Various mechanisms, including as direct credit replacements, irrevocable

pledges to provide credit, and foreign exchange related contracts, are used to create Islamic derivative financial products. Currency forwards and swaps, options, and interest rate swaps are the next derivatives from a western perspective.

Table 2: Differences of Components in Income Statement of Islamic and Western Views

Western Views	Islamic Views
Interest income (Interest expense)	Income from depositors and shareholders' funds
Net Interest Income	(Allowances for losses on financing)
+ Non Interest Income	(Impairment losses)
Net Income	(Profit Equalization Reserve)
(Non-interest expense)	Total Distributable Income
(Allowances for losses on loans and advances)	(Income distributable to depositors)
Operating profit	Total net income
(Impairment losses)	(Overheads and Expenses)
Profit before taxation	Profit before tax and zakat
(Taxation)	(Tax and zakat)
Profit (Loss)	Net profit (Loss)

Sources: Safeza et al., 2012

The variations in the income statements are the result of the varied systems of operations for both Islamic and western perspectives. Because western perspectives work on an interest-based structure, the source of money or revenue will come straight from these features. In Islamic perspectives, revenue is derived only from the funds of depositors and shareholders as a consequence of the profit sharing system in *mudharabah* or *musharakah* finance.

Financial Period Assumption

The ultimate result of an economic unit should be established at the conclusion of the operation or as soon as the activity is done. Zakat, on the other hand, is imposed when a property is maintained for a year according to Islamic law. As a result, this common western financial reports accounting assumption is invalid for determining zakat.

Conservatism (Restrictive Convention)

It has been claimed in western financial reports that precautionary measures do not result in hidden reserves. Reporting an entity's assets and revenues at a lower level than reality, or reporting spending and debts at a greater level than reality, breaches the impartiality and trustworthiness of financial data. This idea is incompatible with Islamic financial reporting standards, which makes it difficult to calculate Zakat. The present worth of assets, in reality, validates the zakat computation.

The Idea of Transparency

According to Islamic perspectives, disclosure in financial reports can take two forms: (a) full disclosure and (b) social accountability. In the context of Islamic content, the notion of accountability in financial reports is linked to complete transparency with the goal of

preserving stakeholders' interests. According to this logic, all of an entity's information should be revealed in its financial reports. Meanwhile from western perspectives, they place a premium on information, but Islamic financial reports place a premium on moral accountability.

Relationships of Financial Reports with Five Objectives of Shariah and Three Levels of Maqasid Paradigm

The goal of guaranteeing the *maqasid* is to ensure that all stakeholders gain while no one is harmed (Azhar Rosly, 2010; Kamali, 2011). Imam al-Shatibi and Imam al-Ghazzali, proponents of *maqasid*, created a three-levels of *maqasid* hierarchy to assess which are *al-daruriyyat* (need), *al-hajiyyat* (complements or supports), and *al-tahsiniyyat* (embellishments), where *al-daruriyyat* refers to absolute necessity. Furthermore, *al-daruriyyat* has five subsections (Alam et al., 2015; Dusuki et al., 2011), namely, protection of faith - i.e. seeking truth and justice, protection of life through well-being, protection of intelligence through knowledge enhancement, protection of lineage and honour through fulfilling obligations to future generations, and finally protection of wealth through ensuring economic justice. As a result, ensuring the preservation of fundamental needs (*al-Daruriyyat*), which includes faith, life, offspring, intellect, and property, is the goal of assessing the *maqasid*. For example, in Islam, the prohibition of interest is equivalent to not injuring any party, because unjust tactics, such as compounding interest charges, might lead one to lose all of his possessions (Azhar Rosly, 2010). To stave against societal damage, the Qur'an encourages healthy and sustainable economic practises while prohibiting reliance on interest earnings in the economy (Al Qur'an 2:275). Islam supports the formation of mutually beneficial contracts and demands that they be honoured.

Therefore, Islamic paradigm promotes healthy business and economic activities in accordance with the *maqasid* element, which is supported by an awareness of the societal context and advantages, where a minimum degree of affliction to anybody is necessary. Economic activity will be sustained if fundamental requirements are met, as well as an equal distribution of income and wealth is achieved, which may be achieved through moral well-being and sufficient training in the long run. If these healthy economic activities do not thrive, civilisational progress may suffer, and the real existence of humans and environment may be jeopardised. In addition, according to Sadeq (1996), zakat is a strong instrument for the Islamic economic framework in order to achieve sustained grassroots human development in an Islamic state. It also provides *asnaf* (zakat recipients according to the Qur'an and hadith) a sense of self-reliance and, if they genuinely desire to, the ability to lift themselves out of poverty. Next, according to *maqasid* advances, that fits in first and foremost with the safeguarding of life and health, as well as riches and offspring, religion, and finally intelligence. In the goal of sustainable development, this is also in line with economic or financial sustainability.

RECOMMENDATIONS AND CONCLUSIONS

The study reveals that there are significant differences between western and Islamic financial reports, and that when all of these differences are taken into account, Islamic financial reports provide greater service and assures comprehensive welfare to the users than western financial reports. As a result of the *muamalah* link, Islamic financial reports may be the ideal approach for Muslims to practise financial reports. Despite the fact that conventional or western views on financial reports has become more profitable for a group of individuals and is used by a huge number of people all over the world, it still has a number of flaws due to its man-made qualities. As a result, it is important to encourage businesses to use Islamic financial reports because it benefits not only the company but also the entire society. Islamic financial reports

can be a means of true ethical practise that can limit western financial reports, which only benefits a small number of people.

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