AN EXPLORATORY STUDY OF ACCOUNTING ON IJARAH AS PRACTICED BY MALAYSIAN FINANCIAL INSTITUTIONS

Ros Aniza Mohd. Shariff dan Abdul Rahim Abdul Rahman
Department of Accounting,
Kulliyyah of Economics and Management Sciences,
International Islamic University Malaysia,
Jalan Gombak, 53100 Kuala Lumpur,
Malaysia.

ABSTRACT

Prior studies on *Ijarah* were mainly focusing on the economics, legal and financial aspects, there was, however, so far no in-depth study on accounting for *Ijarah*. The main objective of this study is to explore the nature of accounting practices as practiced by Malaysian financial institutions. First, the study makes comparison between the International Accounting Standard on leasing (IAS 17); the accounting standard for *Ijarah* (FAS 8) as developed by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI); and the Malaysian Accounting Standard Board (MASB 10). The study found that there are major differences as to the nature of leasing and *Ijarah*, and as a result accounting principles that have driven all the three standards as well as accounting techniques developed for leasing and *Ijarah* are significantly different. Secondly, the study examines the level of acceptability of the AAOIFI's FAS 8 among the Malaysian financial institutions. The result of the questionnaire survey shows a low level of acceptability of FAS 8 and the result from the interview survey further confirms this finding. This study indicates, subject to further studies on other Islamic financial instruments and other Islamic countries, that the effort to harmonise the accounting practices on Islamic financing practices by financial institutions internationally may be a difficult task. Secondly, until and unless the AAOIFI standard is adopted by the regulatory agency as in the case of Malaysia, Bank Negara Malaysia, AAOIFI standards will remain only as a reference but do not have the legal authority. Consequently, the quality and comparability of accounting information of Islamic financing such as *Ijarah* will be seriously at a stake.

Vol. 13, No.1/2,Desember 2005

Introduction

Ijarah has been conceptually understood as a contract of exchange where one party enjoys the benefit arising from employment by another party in return for a consideration for the services rendered and from the use of an asset. Scholars of the four schools of Islamic jurisprudence (Shafi'ie, Maliki, Hanbali and Hanafi) have cited various definitions of the contract of *Ijarah*. In brief, these definitions agree on the fact that the contract of *Ijarah* is a contract on using the benefits or services in return for compensation (Kharofa, 1997).

There is a considerable body of research on the Islamic financial system in general. However, literature that specifically discusses the *Ijarah* contract is limited. The study is motivated to explore accounting issues in *Ijarah* due to the lack of studies on *Ijarah*. The scarce availability of literature written on the topic of *Ijarah* is due to several possible reasons. The most fundamental reason is the infancy stage of Islamic banking and finance as compared to conventional finance. The idea of Islamic finance was inspired by the first conference on Islamic economics in 1976. Obviously, *Ijarah*, which is part of Islamic finance, is very much in its early stages of development.

The first objective of this study is to examine the nature of *Ijarah* financing and its differences with conventional lease financing from the legal and accounting perspectives. This is considered as important because without a proper understanding on the nature of *Ijarah* and the differences compared to conventional leasing, the conceptualization of the accounting implications for *Ijarah* may not be complete. Consequently, the second objective of this study is to determine the level of acceptability of Accounting and Auditing Organization of Islamic Financial Institution's (AAOIFI) accounting standard on *Ijarah* in Malaysia using questionnaire and interview survey among Malaysian's commercial banks. This is important to explore the current practices in Malaysia vis-à-vis AAOIFI standard. The findings will hopefully provide some insights into the nature and issues of accounting practices of an Islamic financial instrument.

Islamic Financing Principles

Islamic finance is an ethical, indigenous and equitable mode of finance, which derives its principles from the *Qu'ran* (The revealed book of Muslims), the traditions of the Prophet Muhammad (peace be upon him), and the *Shari'ah Islami'ah* (Islamic law), which is based on the *Qu'ran* and *Sunnah*. There are clear distinctions between Islamic finance and 'conventional' finance (Qureshi and Millet, 1999). These differences are derived from three main prohibitions by the *Shari'ah Islami'ah*. The first prohibition is against *riba'* (usury). This prohibition is intended to prevent exploitation and to maximize social benefits. Secondly, Islam prohibits *gharar* (uncertainty) in activities. *Gharar* is considered as not Islamic because it can cause injustice to another party. The third prohibition is against *maisir* (gambling).

One of the most important principles of Islamic finance is the scriptural injunction against *riba'* and there is now a general consensus among Muslim economists that *riba'* is not restricted to usury but encompasses interest as well. The prohibition of usury is ordained in Islam in all forms and intent. This prohibition is strict, absolute and unambiguous. The Holy *Qur'an* in verse 278 of Surah Al-Baqarah states: *"O ye who believe! Fear Allah and give up what remains of your demand for riba, if ye are indeed believers"*, and verse 2: 279 says *"If you do it not, take notice of war from Allah and His Messenger, but if ye turn back, ye shall have your capital sums. Deal not unjustly and you shall not be dealt with unjustly"*.

Riba' can be defined as predetermined payment over and above the actual amount of the principal. It is prohibited because while profit is legitimately allowed, the parties cannot predetermine a guaranteed profit. This is based on the principle of "uncertain gains" which, on a strict interpretation, does not even allow an undertaking from the customer to repay the borrowed principal plus an amount to take into account inflation.

Riba is also prohibited as it leads to injustice (*zulm*) and Islam is against all forms of injustice and exploitation and pleads for an economic system, which aims at securing extensive socio-economic justice. The Islamic law of prohibition of *riba*, which includes interest, was originally not based on economic theory but on Divine Authority, which considers the charging of usury is as an act of injustice.[1]

Gharar is from the Arabic word which means risk, peril and uncertainty. It is a kind of sale, which involves giving an undertaking, which the seller is not certain to fulfill such as the sale of fish before they are caught. The prohibition of *gharar* is because it affects both the subject-matter and the price, which can generate unearned profit or an unacceptably huge loss. Hence, the motive behind the prohibition of *gharar* is the avoidance of risk in sale. Another rationale behind the prohibition of *gharar* is that, it depends not on the existence or non-existence of the goods, but on the vendor's obligation to deliver the subject-matter of the sale. If he is not in a position to do so, because, for example the contract contains an element of *gharar* risk, the transaction will be void according to the degree of *gharar* involved.

Development of Islamic Financial Institutions

The pioneering effort to establish Islamic bank can be traced in Egypt and it took the form of a saving bank based on profit-sharing in the town of Mit Ghamr in the early 1960s. Later on, the Organization of Islamic Conference (OIC) initiated the Islamic

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[1] Siddiqui, S. H. Islamic Banking: True Modes of Financing. http://www.islamic-banking.com/ ibanking/ ibanking_aom/sh_siddiqui.php

Development Bank (IDB) in 1975, but it was primarily an intergovernmental bank aimed at providing funds for development projects in member countries. The IDB now also extends to the private sector for project and trade finance facilities.

In the mid-seventies, Islamic banks came into existence in Saudi Arabia and the United Arab Emirates. Since then, Islamic financial institutions have emerged in a large number of Muslim countries including Kuwait, Bahrain, Qatar, Turkey, Pakistan, Indonesia and a belt of other IDB member countries. These institutions have taken the form of commercial banks, investment banks, investment and finance companies, insurance companies, etc.[2] In the early years, investments and products used by most Islamic financial institutions were driven by the concept of *Mudharabah* (referred to as trust financing) and focused on short-term investments. During this period, *Murabahah* (cost-plus finance) emerged as the instrument most widely used by Islamic banks, accounting for over 80 percent of a portfolio of an Islamic bank.[3]

The last few years have seen a growth in the number of conventional banks, which offer Islamic banking products (Cunningham, 1994). Indeed, conventional banks have also begun to realize that offering Islamic products is a way of capturing deposits. Many investors keep most of their money in a conventional account, but like to place part of their funds in Islamic accounts. A conventional bank with an Islamic finance division can capture all of such a client's business rather than just a limited part.

In Malaysia, there is a dual banking system whereby the Islamic banking system and the conventional banking system exist side-by-side. The legal basis for the establishment of Islamic banks was the Islamic Banking Act (IBA), which came into effect on 7 April 1983. The IBA provides Bank Negara Malaysia with powers to supervise and regulate Islamic banks, similar to the case of other licensed banks. The Government Investment Act 1983 was also enacted at the same time to empower the Government of Malaysia to issue government securities issued based on *Shari'ah* principles. The first Islamic bank to be established in the country was Bank Islam Malaysia Berhad (BIMB), which commenced operations on 1 July 1983.

In contrast, other institutions come under the jurisdiction of the Banking and Financial Institutions Act 1989 (BAFIA). The BAFIA, which came into force on October 1, 1989, provides for the licensing and regulation of institutions carrying on banking, finance companies, merchant banks, discount houses and money-broking businesses. However, the Islamic banks are not the only financial institutions involved in Islamic banking. In

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[2]Khan, I. Issues and Relevance of Islamic Finance in Britain. http://www.islamic-banking.com/ ibanking/ ibanking_aom/ia_khan.php

[3]Khan, I. Issues and Relevance of Islamic Finance in Britain. http://www.islamic-banking.com/ ibanking/ibanking_aom/ia_khan.php

1993, other financial institutions can also offer Islamic banking services through the "Islamic Banking Scheme".

Nature of Ijarah Financing

There are many types of *Ijarah* such as *Al-Kara'* (Contract of employment), *Ijarah Al-Tashyghiliah* (Operational Leasing) and *Ijarah Al- Masrafiah* (Financial Leasing). Literally, *Ijarah* means to give something on rent. As a term of Islamic *fiqh*, *Ijarah* can also refer to wages paid to a person in consideration of the services rendered by him. In the following discussion, the term *Ijarah* is used to represent the usufruct of assets and properties, and not the service of human beings. In the context of Islamic banking, *Ijarah* can be defined as a process by which the "usufruct of a particular property is transferred to another person in exchange for a rent claimed from him/her" (Hairetdinov, 1998).

Ijarah has been conceptually understood as a contract of exchange in which one party enjoys the benefit arising from employment by another party in return for a consideration for the services rendered and from the use of an asset. This classical definition was the basis of many of the contracts of exchange even before the times of the Prophet and was popular amongst the *fuqaha* as documented in much of the literature. Since that time, the operation of these contracts developed to a higher level of sophistication during the period of the companions of the Prophet (p.b.u.h.). However, the basis of operation remained confined to simple *Ijarah* contracts.

The basic feature of the *Ijarah* contract has been that it is a contract of exchange between one to another party (hereinafter called one-to-one *Ijarah*). For example, one party is given the right to use the services of a person or of a given asset from another party for a consideration. This contract has not involved the transfer of ownership to the other party as there has been no intention to purchase or to own the *Ijarah* object by the interested party. Over time, however, this concept has developed into transactions with more complex features that give rise to variations from the basic structure of the *Ijarah* transactions.

The distinguishing feature of this mode is that the assets remain the property of the Islamic bank to put them up for rent every time the lease period terminates so that they do not remain unutilized for long periods of time. Furthermore, there are some conditions that *Ijarah* transactions need to follow in order to be in consonance with the principles of Islamic finance. These conditions are mainly concerned with the object leased, the contract and the maintenance of the leased assets.

Basically, the lease contract must state the lease period clearly. Renewal terms must also be stated clearly, and things like the rentals for all subsequent years, after the first year, should not contain clauses like "left to the sole discretion of the lessor" and the like. It is also a condition that the subject of the contract must actually and legally be attainable. It is not permissible to lease something that cannot be delivered. Furthermore, it is permissible for the two parties to agree during the lease period to review the lease period or the rental or both. That is because the lease contract occurs periodically unlike the sale contract where the transfer of ownership is immediate. Part of the conditions also state that the lessor bears the liabilities when leasing the asset such as damage, payment of premium cost and basic maintenance. There is no objection to authorizing the lessee to undertake all the above but the costs thereof must be borne by the lessor or owner.

The Need for Accounting Standard on Ijarah

The need for an accounting standard is not very different from the need for any other kind of standards, whether they be standards for weights and measures, or standards for clothing sizes, grades of beef, or baseball statistics (Mirza and Baydoun, 2000). The goal or objective of an Islamic accounting standard is to facilitate comparisons and thereby minimize the social and economic costs of assessing the alternatives with which one is faced in making rational decisions.

Unless a proper disclosure with regard to the financial reporting, the underlying *Shari'ah* principles and the accounting methods adopted is made, the information contained in the financial statement will not be useful for a comparison of the performance of different Islamic banks (Hamat, 1994). Inadequate disclosure of the underlying *Shari'ah* principles will subject the Islamic banks' activities to a lot of questions with regard to their Islamicity. Thus, the need for standard accounting practices in the reporting of Islamic banks' operations is very clear.

The emergence of Islamic banks and financial institutions as relatively new organizations and the great challenge they face to successfully serve the societies in which they operate, have led them, together with specialists in Islamic *Shari'ah* and accounting, to seek the most appropriate means through which accounting standards could be developed and implemented in order to present adequate, reliable, and relevant information to users of the financial statements of such organizations. The presentation of such information is critical to the economic decision making process by parties who deal with Islamic banks and would also have a significant effect on the distribution of economic resources for the benefit of society.[4]

The structure and processes of Islamic banks do not readily fit in with those of conventional universal banking, which combines both commercial and investment businesses. This seems to have resulted in supervisory bodies adopting different approaches to regulate Islamic banking. Such variations in the regulation of Islamic banking appear, in turn, to have resulted in Islamic banks adopting different accounting treatments for the same transaction. This rendered the financial statements of Islamic banks non-comparable (Karim, n.d.).

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[4] Concepts of Financial Accounting For Islamic Banks and Financial Institutions, AAOIFI, Para 1.

Another major problem in the accounting and operation of Islamic banks is the lack of precision in the application of the *Shari'ah* principle to Islamic banking. The *Shari'ah* does not refer directly to banking or its accounting, but to broad issues relating to the prohibition of the paying and receiving of *riba*, transactions relating to pork, gambling, speculation, etc. Therefore, for Islamic countries to operate, in a practical manner, the application of *Shari'ah* principles to the accounting and operations of Islamic banks is important (Naser and Pendlebury, 1997.)

However, even though the need for Islamic accounting standards for the reporting of Islamic banks' operations is very obvious, this does not mean that Islamic banks must come up with complete sets of new accounting standards (Hamat, 1994). The existing standards can continue to be applicable, as long as they do not go against the requirements of the *Shari'ah*.

The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) is an organization that seeks to support the faith of Islam by developing accounting standards for Islamic investment vehicles. In 1991, several parties including practicing accountants and *Shari'ah* scholars helped set up the AAOIFI- a private sector standard-setting body in Bahrain with the aim of producing international accounting standards based on the *Shari'ah* precepts for Islamic banks and financial institutions.

In regulating the financial reporting of Islamic banks, the AAOIFI claims that financial accounting plays an important role in providing the information which the users of the financial statements of Islamic banks depend on in assessing the bank's compliance with the precepts of the *Shari'ah*. However, to perform this role effectively, accounting standards need to be developed and complied with by Islamic banks. The development of such standards must be based on clear objectives of financial accounting and agreed upon definitions of its concepts (Karim, 1995).

The growing need for accounting standards and the AAOIFI's regulatory effort have been focusing on certain of the Islamic investment vehicles (Pomeranz, 1997). The AAOIFI also expected to strengthen the effectiveness of *Shari'ah* committees by facilitating the evaluation of emerging financing instruments and by aiding in the implementation of Islamic ethics. Nonetheless, the AAOIFI seeks the implementation of its rules partly by getting central banks to adopt them and partly by trying to persuade Islamic institutions of their usefulness.

Furthermore, at present, the AAOIFI has neither the consent of regulatory bodies (e.g. central banks) nor the power to force Islamic banks to implement its proposed standards (Karim, 1995). Hence, in order to ensure compliance with its standards, the AAOIFI may have no choice but to obtain the support of the regulatory bodies concerned or to try to secure the cooperation of at least the major Islamic banks and their auditors.

Research Methods

A review of the literature has shown the lack of studies undertaken to understand accounting practices for *Ijarah*. Most of the literature looked at the description of *Ijarah* financing (Qureshi and Millet, 1999; Hairetdinov, 1998; Al-Hathal, 1997; Cunningham, 1994; De Belder et al, 1993;). Some of the literature touched on the beefing up by Islamic financial institutions of their *Ijarah* (leasing) capacity in expectation of unprecedented future demand. It is also rapidly becoming the most popular form of Islamic finance (Collett, 1996; Collet, 1995). This creates a need to study the dynamics of this type of financing in order to address the lack of awareness and understanding of the accounting treatment of *Ijarah* financing.

There are three research questions in this study. The first research question is: "What are the differences between *Ijarah* and conventional leasing from legal (definitions, types and principles) and accounting perspectives?" The second research question is: "What are the current accounting practices of *Ijarah* by Malaysian financial institutions?" Finally, the third research question is: "To what extent the AAOIFI's accounting standard on *Ijarah* (FAS 8) is adopted in and acceptable to the Malaysian financial institutions?"

The data collection for the first question involves the review of the accounting standards. Thus, for the first objective, in order to have a better comparison between the *Ijarah* standard and conventional leasing, it is necessary to study the standard of *Ijarah* recommended by the AAOIFI and compare it with the conventional leasing standard set by the International Accounting Standard (IAS 17) and the Malaysian Accounting Standard Board (MASB 10).

For the second and third questions, a survey research method is chosen to measure the level of acceptability of the AAOIFI's standard on *Ijarah*. Since the AAOIFI is the only standard setter for Islamic financial products, this research hopes to find evidence of its level of acceptability in Malaysia. This survey investigation attempts to explore the nature of accounting practices on *Ijarah*. The questionnaire for this research was sent to the Islamic Banking Division of the financial institutions. The questionnaires were sent to a total of 14 financial institutions operating in Malaysia and the questionnaires were addressed to the manager or head of the Islamic Banking Division. Out of the 14 questionnaires, 13 replies were received and covering almost all of the financial institutions that were involved in *Ijarah* financing.

In order to ensure the reliability and validity of the analysis and findings of the questionnaire survey, a semi-structured interview via telephone is chosen. In the interviews, five financial institutions were selected based on their adoption of accounting standards. The interviews were directed to the same person that responded to the earlier questionnaire survey. This is to get clarification on selected issues that they had answered in the questionnaire survey. The adoption of multiple data sources is an attempt to ensure the reliability and the validity of the questionnaire findings.

Comparative Study of AAOIFI FAS 8, IAS 17 and MASB 10

This section discusses the descriptive analysis of the comparative study between the AAOIFI's standard on *Ijarah* (FAS 8) and the leasing standards set by the International Accounting Standard (IAS 17) and the Malaysian Accounting Standard Board (MASB 10).

Legal Perspective

The AAOIFI defines *Ijarah* as "ownership of the right to the benefit of using an asset in return for consideration"(please refer to appendix (B) Juristic Rules, FAS 8, Paragraph 1/1). Some *Islamic scholars* have included the duration of the benefit in the definition. As for leasing, the IAS 17 defined a lease as "an agreement whereby the lessor conveys to the lessee in return for rent the right to use an asset for an agreed period of time". The definition given by the MASB 10 is quite similar to the definition given by the IAS 17. The MASB 10 defined lease as "an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time".

All the above definitions capture the element of exchange of usufruct for money transactions. Nevertheless, the definition given by the AAOIFI is furnished with extra conditions, which will distinguish *Ijarah* from conventional leasing. Juristic Rule 1/3/3/2 in the AAOIFI's standard (FAS 8) states that the fulfillment of the benefit should be of a permissible nature and the benefit should be in accordance with the *Shari'ah*. Thus, the AAOIFI's standard gives more detail with respect to the lawfulness of both usufruct and the rent. This is to ensure that *Ijarah* only signifies such an arrangement where both the usufruct and the return are permissible by the *Shari'ah*.

In contrast, the IAS 17 and the MASB 10 adopt a broader aspect of usufruct and return since religion is never an element to be observed by the standard-setters. Thus, strictly speaking, *Ijarah* cannot be equated to conventional leasing. The second aspect to be scrutinized is the types and principles of *Ijarah* and leasing. The AAOIFI's standard classifies *Ijarah* as Operating *Ijarah* and *Ijarah Muntahia Bittamleek*. The main criterion used in the classification is whether the lease includes a promise that the legal title in the leased asset will pass to the lessee at the end of the lease term.

The AAOIFI's standard on *Ijarah* states that when a lease does not include a promise that a legal title will pass to the lessee, it is classified as Operating *Ijarah* and if there is a promise it is *Ijarah Muntahia Bittamleek*. In essence, the subtle difference between *Ijarah* and *Ijarah Muntahia Bittamleek* lies in the pre-existence of that promise whereby a lease concludes with the legal title passing to the lessee through either: (i) gift (transfer of legal title for no consideration); (ii) token consideration or other amount as specified in the lease; (iii) transfer prior to the end of a lease for a price equivalent to the remaining *Ijarah* installments; or (iv) a gradual transfer of the legal title (sale) of the leased asset.

In the IAS 17 and the MASB 10, a lease is classified as a finance lease if it transfers substantially all the risks and rewards incident to ownership of the asset from the lessor to the lessee. Title may or may not eventually be transferred. All other leases, which do not meet this criterion, are to be classified as operating leases.

A hire purchase contract for the hire of an asset would also fall within the definition of a finance lease. Hire purchase contracts in Malaysia contain provisions, which transfer the title of the asset to the hirer upon payment of all the hire purchase installments. *Al-Ijarah Thumma Al-Bai'* is the Islamic alternative to conventional hire purchase in Malaysia. It is a leasing ending with sale and consists of two different contracts i.e. the contract of lease and the contract of sale.

However, the standard does not elaborate the meaning of "transfer substantially all risks and rewards incident to ownership". It relies on the consideration of substance over form (IAS 1) in deciding whether a lease should be classified as a finance lease or an operating lease. The promise of the lessor to transfer the ownership of the leased asset to the lessee in the *Ijarah Muntahia Bittamleek* is not the same as the substance over form rule as in the IAS 17 and the MASB 10.

In the conventional lease, the referred component relates to the risk and reward incidental to ownership of the leased asset. In *Ijarah*, the lessor holds the ownership rights and obligations from the very beginning till the end of the contract. The lessor must accept responsibility for any defects of the leased asset, which impair the intended use of the asset, and may not exclude his liability for any impairment that the leased property may sustain.

Note that impairment caused by the lessee's misconduct is not borne by the lessor but by the lessee himself. However, maintenance costs should be taken from the lessor's pocket since it is his duty to maintain the asset. Juristic Rules 1/6 sums up the above principles where it states, "the lease property is the responsibility of the lessor throughout the duration of the *Ijarah*, unless the lessee commits misconduct or negligence".

As for the right of the lessor, Juristic Rule 1/5/2 outlines that "the lessee must use the leased asset in a suitable manner or in conformity with common practice and comply with conditions which are acceptable in the *Shari'ah*. He must also avoid causing damage to the leased asset by misuse through misconduct or negligence".

Therefore, in the *Ijarah* agreement, the ownership rights and usufructary rights are treated differently as they are detachable according to Islamic commercial law. In contrast, there seems to be no distinction made between ownership rights and usufructary rights by the IAS 17 and the MASB 10. In other words, there can never be a transfer of ownership risk in the *Ijarah* contract as it deals only with the transfer of usufruct. In the case of *Ijarah Muntahia Bittamleek*, transfer of ownership only takes place when both parties enter into a contract separate from the *Ijarah* contract (see Juristic Rule 2/3). The second contract is drawn up when the promise is fulfilled.

Accounting Perspective

Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) standard was adopted in June 1997 and it has gone through several public hearings attended by representatives from central banks, Islamic banks, accounting firms, *Shari'ah* scholars, and academics for their recommendations and comments. AAOIFI FAS 8 provides representation of accounting principles such as revenue and expenses recognition, measurement methods, disclosure requirements and classification of *Ijarah*.

Between the AAOIFI and the IAS 17 and the MASB 10, the major differences are the revenue recognition and the effect of residual value since the contracts of *Ijarah* and lease are different in their substance. In addition, the IAS 17 reminds the lessor to record the uncertainties of collectability of lease rentals income and the future level of interest rates. As for the AAOIFI, no provision is recorded on interest rate uncertainty because the rental is fixed throughout the *Ijarah* term or the terms of payment are determined up front and the lessor cannot increase the rent unilaterally.

Furthermore, the AAOIFI does not mention the provision for doubtful debt in the case of *Ijarah*, as it might be understood that the provision is commonly practiced but the AAOIFI recommends the financial institutions to establish a provision for the repair of leased assets if the repair expenses differ from year to year over the lease term. This provision is significant under the Ijarah contract because ownership risk is borne by the lessor. Not recording the provision would underestimate the lessor's obligation.

Nevertheless, the AAOIFI is also concerned about the recording of the transaction of permanent impairment of the leased asset before the legal title is passed to the lessee. If that was due to the lessee's actions and the installment paid was more than the fair rental amount, then the lessor has to record the transaction as his liability and recognize it as a loss, which will be posted to the income statement. No such emphasis was given in the IAS 17 or the MASB 10.

On the issue of disclosure, all standards require the major class of assets of accumulated depreciation to be stated. In the IAS 17 as well as in the MASB 10, the method for income recognition and future minimum lease payment to be received for specified future payment must be disclosed. However, in the AAOIFI, since only one method of income recognition is recommended, no such disclosure is needed. In addition, a unique requirement in the AAOIFI disclosure is that lease assets for operating *Ijarah* and *Ijarah*

Muntahia Bittamleek are to be distinguishable whereby assets for operating *Ijarah* are recorded as investment in *Ijarah* assets while assets for *Ijarah Muntahia Bittamleek* are recorded as *Ijarah Muntahia Bittamleek* assets.

Results of Questionnaire and Interview Survey

Most of the financial institutions adopted the MASB rather than the IAS and AAOIFI standards. A total of 11 out of the 13 institutions adopted the MASB in their practice. The reason that may cause this situation is that the MASB is the only standard setter in Malaysia. Therefore, financial institutions in Malaysia are supposed to conform to the MASB, as it is one of the regulatory bodies. Prior to the existence of the MASB, most of the financial institutions followed the IAS requirements. Hence, the IAS still enjoys a higher popularity than the AAOIFI standard. This is shown in that 4 financial institutions still use the IAS.

As for the AAOIFI, it is a new organization compared to the IAS. In addition, the AAOIFI is aimed at Islamic financial institutions. The conventional financial institutions may not be aware of the existence of the AAOIFI standard. Furthermore, this organization is based in Bahrain. Of the three standards, the AAOIFI gained the least number of adoptions by the financial institutions. Out of 13, only 2 institutions had adopted the AAOIFI. Only one institution uses all the three standards. The institution is Bank Islam Malaysia Berhad. As mentioned earlier, the AAOIFI standards are targeted at Islamic banks. Thus, Bank Islam should be aware of the existence of the AAOIFI's standard. As for the IAS, it had been there long before the MASB was established. Therefore, perhaps for this reason, Bank Islam still adopts the IAS. The MASB is mandatory for financial institutions in Malaysia; hence, Bank Islam is not excluded from conforming to the MASB.

Eight financial institutions were found to only use the MASB standard only. This is as expected as most of the financial institutions are conventional in nature. Therefore, they would not be aware of the AAOIFI's standard. In addition, it is only mandatory for financial institutions in Malaysia to adopt the MASB. However, one financial institution only adopts the IAS. The researcher finds this situation is rather peculiar. Even though the contents of the IAS and MASB are quite similar, as a local financial institution, one should not ignore the importance of the MASB.

The Extent of Acceptability of AAOIFI FAS 8

This study attempts to provide evidence of the level of acceptability of the AAOIFI's standard on *Ijarah* in Malaysia. Although this research attempted to measure the level of acceptability of the AAOIFI's standard on *Ijarah*, it should be noted that the list of items used in the questionnaire does not comprise the second part of *Ijarah*, which is the *Ijarah Muntahia Bittamleek* (Financing Lease). It only comprises normal *Ijarah* or operating leases. Since the AAOIFI is the only standard setter for Islamic financial products, this research hopes to find evidence of its level of acceptability in Malaysia.

As for the level of acceptability of the AAOIFI's standard on *Ijarah*, the average score or mean is adopted. It is expected to give a clear understanding of *Ijarah* financing practices in Malaysia. The respondents were asked to indicate the extent to which each item has been implemented in their organization on a five-point Likert scale from 1 to 5. A one (1) was to be assigned if it was totally not applicable for the item to be implemented in their organization and five (5) was to be assigned if it was totally applicable to be implemented in their organization. The points 2 to 4 were to be used to indicate varying degrees of intermediate applicability.

Table 1: Mean 3 and above (relatively strong support for the AAOIFI's standard)

Item	Attributes	Mean
1.	*Ijarah* revenue shall be allocated proportionately to the financial periods in the lease term.	4.33
2.	*Ijarah* revenue shall be presented in the income statements as *Ijarah* revenue.	3.67
3.	Initial direct cost, if material, be allocated to periods in the lease term.	3.36
4.	Initial direct cost, if immaterial, charged directly in the income statement as an expense.	3.09
5.	Asset acquired for *Ijarah* shall be recognized at historical cost.	3.00
6.	Reduction in estimated residual value shall be recognized as a loss.	3.00
7.	Leased assets shall be depreciated consistent with lessor's normal depreciation policy.	3.00

Out of 15 items that have been analyzed, 7 have a mean score of 3 and above. The range of the mean is from 1 to 5, therefore, a score of 3 and above is considered a strong support for the AAOIFI's standard on *Ijarah*.

The highest score is of the level of acceptability for statement that *Ijarah* revenue shall be allocated proportionately to the financial periods in the lease term. Most of the financial institutions that were involved in this survey agreed on this statement. It is quite similar to the accounting standard set by the IAS and MASB. In Paragraph 52 of the IAS 17 mentions that rental income should be recognized on a straight-line basis over the lease term. In addition, Paragraph 49 in the MASB 10 also mentions the same thing. Both the IAS 17 and MASB 10 use the phrase "recognized on a straight-line basis over the lease term". In other words, the rental revenues should be allocated proportionately over the lease term. Hence, it has been a common practice in Malaysia that *Ijarah* revenues are allocated proportionately over the lease period.

The second highest score is for the statement that *Ijarah* revenue shall be presented in the income statement as *Ijarah* revenue. Most of the *Ijarah* practitioners in Malaysia also agreed with this standard. Therefore, it is clear that what has been practiced in this matter conforms to the AAOIFI's standard. Nevertheless, Paragraph 49 in the MASB 10 states that lease income from operating leases should be recognized in income on a straight-line basis over the lease term. While, in Paragraph 27 of the IAS 17, under operating leases, it states that rentals receivable are included in income over the lease term. Both the IAS 17 and MASB 10 agree that the lease income or the rental receivable is recognized as income or revenue. Hence, the standard set by the AAOIFI in this particular matter does not contradict the standards set by the IAS and the MASB.

The statements by the AAOIFI on initial direct cost also fall under the category that has a mean of 3 and above. The first statement mentions that if the initial direct cost is material, it shall be allocated to periods in the lease term. In this matter, the study assumes that what has been practiced in Malaysia regarding the initial direct cost is by chance is a common sense. If the cost is material, it should be allocated to periods in the lease term and if it is immaterial, it should be charged as an expense. In addition, the IAS 17 and MASB 10 also have the same standard, which applies to the initial direct cost. Paragraph 30 of the IAS 17 states that initial direct costs incurred specifically to earn revenues from an operating lease are either deferred and allocated to income over the lease term in proportion to the recognition of rental income or are written off in the period in which they are incurred. The MASB 10 also states the same thing about initial direct cost under the operating leases (please refer to Paragraph 51 of the MASB 10).

However, both standards set by the MASB 10 and the IAS 17 did not mention the level of materiality of the initial direct cost. It is only mentioned that initial direct costs are either allocated to income over the lease term or are recognized as an expense. This is different from the AAOIFI's standard, which has segregated the treatment of the initial direct cost according to its level of materiality.

The AAOIFI's standard also states that the acquiring of assets for *Ijarah* shall be recognized at historical cost. However, the IAS 17 and the MASB 10 are silent on the acquiring of assets under operating leases. Nevertheless, Paragraph 8 of the IAS 17 did mention that the rights and obligations arising from a finance lease are recorded at the beginning of the lease term at the fair value of the leased property. In addition, Paragraph 15 of the MASB 10 also states the same thing. As for the case of operating leases, there is no statement regarding the recognition of the asset.

The AAOIFI standard on *Ijarah* also states that a reduction in the estimated residual value should be recognized as a loss. Nevertheless, the IAS 17 and MASB 10 are also silent on the case of reduction in estimated residual value under operating *Ijarah*. The treatment for a reduction in estimated residual value is only stated under the finance lease. For example, Paragraph 17 of the IAS 17 states that if there has been a permanent reduction in the estimated un-guaranteed residual value, the income allocation over the lease term is revised and any reduction in respect of amounts already accrued is charged to income immediately. The same treatment is used under the MASB 10. Paragraph 39 of the MASB 10 states that any reduction in the estimated un-guaranteed residual value in respect of amount already accrued is recognized immediately.

The last statement by the AAOIFI that falls within this category is related to depreciation of leased assets. The statement states that leased assets shall be depreciated consistent with the lessor's normal depreciation policy.

Table 2: Relatively medium support for the AAOIFI's Standard (Mean of 2.5 to 2.99).

Item	Attributes	Mean
1.	Leased asset shall be depreciated according to lessor's normal depreciation policy.	2.83
2.	At the end of a financial period, amortization of initial direct cost, if material, shall be recognized as an expense.	2.83
3.	At the end of financial period, *Ijarah* installments receivable shall be measured at their cash equivalent value.	2.83
4.	Repair of leased assets, if material, shall be recognized in the financial period.	2.75
5.	Leased assets shall be presented in the financial statement under Investment in Ijarah Asset.	2.73

Table 2 shows the AAOIFI statements that have a mean of between 2.5 to 2.99. This category of mean is considered as medium support for the AAOIFI's standard. There are 5 statements that fall within this category.

The highest mean score from this category is for the statement asserts that a leased asset shall be depreciated according to the lessor's normal depreciation policy. It is assumed that if a statement in the AAOIFI standard is similar to one in the IAS 17 and MASB 10, then the mean should be higher or at least 3.00. This assumption is based on Paragraphs 29 and 53 of the IAS 17 and Paragraph 54 of the MASB 10. These paragraphs clearly state that under operating leases, the depreciation of leased assets should be on a basis consistent with the lessor's normal depreciation policy for similar assets. Therefore, the researcher feels surprised that the above statement made by the AAOIFI has a mean below 3.00 although the IAS 17 and MASB 10 have proposed the same treatment.

The AAOIFI's standard also states that at the end of the financial period, the amortization of initial direct cost, if material, shall be recognized as an expense. At the end of the financial period also, the AAOIFI's standard states that *Ijarah* installments receivable shall be measured at their cash equivalent value. Another statement that also falls within this category is related to the repair of a leased asset. The statement asserts that if the repair of a leased asset is material, it shall be recognized in the financial period.

The above results are not unexpected as neither the IAS 17 nor the MASB 10 mentioned anything about the amortization of initial direct cost, or the measurement of *Ijarah* (operating leases) installment receivable, or the treatment of repair of leased assets. These treatments only exist in the AAOIFI's standard on *Ijarah*. Therefore, it is assumed that the treatments are not popular with most of the *Ijarah* practitioners in Malaysia; thus, they have a lower mean score. This assumption is based on the fact that most of the *Ijarah* practitioners follow the IAS and MASB because they are more familiar with these two standards than the AAOIFI's standard.

The last statement that falls within this category is the statement that leased assets shall be presented in the financial statement under investment in *Ijarah* assets. On the other hand, Paragraph 49 of the MASB 10 and Paragraph 43 and 51 of the IAS 17 have a different opinion on this matter. Both the IAS 17 and MASB 10 agree that the lessors should present assets subject to operating leases in their balance sheet according to the nature of the asset and usually as property, plant and equipment. It can be rationalized that the different treatment by the IAS 17 and MASB 10 has led to a lower mean score for the statement set by the AAOIFI on the matter of asset presentation in the financial statement.

It can be concluded here that the main reason some of the statements set by the AAOIFI have a score lower than 3 (in this case from 2.5 to 2.99) is that they are treated differently compared with the IAS 17 and MASB 10 and some of the treatments only exist in the AAOIFI's standard and not in the IAS 17 and MASB 10. Furthermore, most of the *Ijarah* practitioners in Malaysia are still using the IAS 17 and MASB 10 as their main guidelines for *Ijarah*. This can be verified by the survey conducted on the adoption of accounting standards by financial institutions (please refer to Table 1).

Table 3: Relatively weak support for the AAOIFI's Standard (Mean less than 2.5).

Item	Attributes	Mean
1.	Repair of leased asset, if material and differing in amount from year to year, a provision for repairs shall be established.	2.25
2.	If a provision for repairs has been established, cost of repairs shall be charged against the provision.	2.08
3.	If lessee undertakes repairs with the lessor's consent and the costs are chargeable to the lessor, then the lessor shall recognize these repairs as an expense.	2.00

Table 3 shows a list of the AAOIFI's statements that have a mean of less than 2.5. This category is considered as weak support for the AAOIFI standard. There are 3 statements that are included in this category.

All three of the statements are related to the repair of leased assets. The first statement is that a provision for repairs shall be established if the repair is material and differing in amount from year to year. The second statement by the AAOIFI is that if a provision for repairs has been established, cost of repairs shall be charged against the provision. The third statement highlights that if the lessee undertakes repairs with the lessor's consent and the costs are chargeable to the lessor, then the lessor shall recognize these repairs as an expense.

Most of the *Ijarah* practitioners give a low score to these statements. The reason behind this scenario is that most of them agreed that the repair of the leased asset is totally under the lessee's responsibility. Therefore, the financial institutions that act as a lessor do not have any concern about matters that relate to the repair of the leased asset. Furthermore, the IAS 17 and MASB 10 are also silent on the repair of leased assets. Thus, it gives a low mean score to these statements.

Nevertheless, the lessee should bear the maintenance expenses to keep the leased assets in good working order and be responsible for replacing any worn or damaged parts (Abdullah, 2000; Hairetdinov, 1998). But in other examples, the parties to the lease agreement agree that the main maintenance work must be the responsibility of the lessor and the periodical and partial maintenance is to be assigned to the lessee as it is considered regular and may be considered part of the rental.

Another possible reason that these statements have a low mean score is perhaps that the *Ijarah* practitioners themselves are uncertain how to tackle *Ijarah* issues as most of them are following the IAS 17 and MASB standards for leasing, whereas what they are actually doing is Ijarah financing. In addition, Paragraph 4 of the MASB 10 states that this standard does not deal with Islamic leases as these will be dealt with under separate Islamic Accounting Standards.

Furthermore, they may not be aware of the existence of the AAOIFI's standard on *Ijarah*. Therefore, they still use the MASB 10 and IAS 17 as guidelines. This situation may be due to the lack of promotion or concern given by the higher authorities responsible for Islamic banking products in Malaysia to the adoption of the AAOIFI's standard. In other words, the AAOIFI's standard is not mandatory to be implemented in Malaysia. Hence, not many of the financial institutions are adopting the standard.

Results of Interview Survey

In order clarify some of the issues discussed from the survey questionnaire. A semi-structured interview method is used to achieve this objective. The reason for the use of semi-structured interview is to explore issues raised by the questionnaire and confirm the findings. The financial institutions that are involved in this interview are Bank Islam Malaysia Berhad (BIMB) (adopts the IAS, the MASB and the AAOIFI), OCBC Bank (adopts the IAS and the MASB), Bumiputra Commerce Leasing Berhad (adopts the IAS only), Public Finance (adopts the MASB only), and finally Islamic Development Bank (IDB) (adopts the AAOIFI only). The selection is based on the type adoption of standards in order to get the widest representation of the banks involved in the questionnaire survey.

There are six main issues raised in the interview. These six issues were determined based on the salient accounting treatments as normally available in the conventional accounting standards. The first issue is the valuation of assets. The AAOIFI's standard states that assets acquired for *Ijarah* shall be recognized at historical cost. However, from the questionnaire survey, it can be seen that not all institutions are using historical cost. Thus, in order to establish how the financial institutions recognized assets acquired for *Ijarah*, this issue needed to be clarified through the interview.

The second issue is related to the recognition of income. As stated in the AAOIFI's standard, *Ijarah* revenue shall be allocated proportionately to the financial period in the lease term. This statement has the highest mean score in the questionnaire survey that reflects a high level of acceptability among the financial institutions in Malaysia. However, there is still a need to confirm the finding to make sure the financial institution has actually practiced the issue related to the recognition of income as recommended by the AAOIFI.

The issue of repair is the third issue that needs to be clarified. Out of four statements that related to repair of the leased asset, three of them had the lowest mean score in the questionnaire survey. Thus, it is crucial to discover the contributing factors behind this low level of acceptability. The fourth issue that needs to be clarified is the issue of depreciation. There are 2 statements in the AAOIFI's standard that are related to depreciation. Nevertheless, one of them falls into the category that has a mean score 3.00 and above, while the other falls into the category that has a mean score of between 2.50

and 2.99. This indicates the mixed level of acceptability of practices on depreciation methods by Malaysian financial institutions. Therefore, further clarification is needed to know how the financial institution treats the depreciation of the leased assets.

The initial direct cost is the fifth issue that needs to be clarified. The AAOIFI's standard states that if the initial direct cost is material, it should be allocated to periods in the lease term and if it is immaterial, it should be charged directly in the income statement as an expense. Even though the statements have a mean score of more than 3 in the questionnaire survey, there is a need to look into whether the result of the questionnaire is actually being practiced by the financial institutions.

Finally, the sixth issue that needs to be clarified is the issue of *Ijarah* account receivable. As stated in the AAOIFI's standard, the *Ijarah* installments receivable shall be measured at their cash equivalent value. This statement has a mean score of 2.83 and it is considered as mixed support for the AAOIFI's standard. However, there is a need to know what are other measurements used by the financial institutions to measure *Ijarah* accounts receivable if they are not using the cash equivalent value as recommended by the AAOIFI.

Valuation of Assets.

As for Bank Islam Malaysia Berhad (BIMB), the issue of recognition of assets acquired for *Ijarah* is considered not applicable to the bank. The reason behind this is that BIMB is using a modified lease. It is a combination of both the operating lease and financial lease. It is an operating lease because the bank owns the asset under the *Shari'ah* concept and at the same time it is a finance lease because it is a financial arrangement. As for the accounting practices, the recognition of assets acquired for *Ijarah* is up to the customer because the customer is considered the owner of the asset.

As for OCBC, Public Finance and IDB, the banks do not recognize assets acquired for *Ijarah* at historical cost. As for OCBC, the bank adopts the MASB standard and the IAS. Meanwhile, Public Bank adopts the MASB only. Both standards are silent on the valuation of assets under the operating lease. However, the standards state that under the finance lease, it should be under fair value. In this case, both banks use their own discretion in the valuation of assets under operating leases. As for IDB, the bank claimed that it adopts the AAOIFI only. Nevertheless, in this matter, IDB does not comply with the AAOIFI's standard. However, these three banks are using the market value.

Bumiputra Commerce also does not recognize assets acquired for *Ijarah* at historical cost as proposed by the AAOIFI's standard but at fair value as suggested by the IAS. This is attributable to the fact that Bumiputra Commerce adopts the IAS only for it accounting practices. Therefore, it can be assumed that the bank follows the guidelines of the IAS.

Recognition of Income.

As for the second issue, which is the recognition of income, BIMB is using cash basis. Therefore, the bank does not recognize any accrual income. However, most of the financial institutions used Rule 78 and the Sum of Years' Digits by Bank Negara Malaysia for recognition of income. This situation may be due to the reason that Bank Negara provides the rule, thus, most of the financial institutions follow the guidelines of Bank Negara. The banks that use this rule are OCBC, Bumiputra Commerce, and Public Finance. However, IDB does not use the same method. Which regard to the recognition of income, the method used by IDB is based on actual income derived.

Repair of the Leased Asset.

The third issue is related to the repair of the leased asset. For this matter, it is not applicable for BIMB. This is due to the fact that the repair of the leased asset is borne by the customer. Even though the AAOIFI's standard suggested that repair should be borne by both lessor and lessee, BIMB decided that the repair should be the customer's responsibility as their leasing activities are a finance arrangement.

It is also not applicable for IDB. This is due to the fact that in actual practice, the repair of the leased asset is borne by the customer. Even though the AAOIFI's standard suggests that the repair should be borne by both lessor and lessee, IDB like the rest of the financial institutions decided that the repair should be the customer's responsibility.

As for OCBC, Bumiputra Commerce, and Public Finance these banks also do not recognize any repair of leased assets in the financial period. This is due to the reason that repair expenses are borne by the customer. Furthermore, the bank adopts the IAS and MASB. Neither of the standards mentions any accounting treatment on the repair of leased assets.

Depreciation.

The fourth issue is related to the depreciation of the leased asset. It is also not applicable to BIMB. Even though the AAOIFI's standard, the IAS and the MASB suggested that leased assets should be depreciated according to the lessor's normal depreciation policy, BIMB is the only financial institution that does not deal with depreciation. This is due to the fact that the customer owns the asset. Therefore, the customer should deal with the depreciation of the asset and not the bank.

However, OCBC is using the income tax table. Therefore, it does not use the bank's normal depreciation policy. While Bumiputra Commerce follows the IAS 17. According to the IAS 17, the leased asset should be depreciated according to lessor's normal depreciation policy.

As for Public Finance, the bank depreciates the asset according to the market. The bank has a margin of finance, which is 20% every year. Only IDB follows the AAOIFI's standard for depreciation. Therefore, it is using the bank's normal depreciation policy.

Initial Direct Cost.

As for the fifth issue, which is the issue of initial direct cost, it is not applicable to BIMB or IDB. The reason is that neither bank incurs any initial direct cost such as commission and fees for the leasing activities.

It is also not applicable to OCBC. The bank does not incur any commission or legal fees regarding the leasing activities. However, for property such as buildings, the bank has a stamp duty the cost of which is borne by the customer. Nevertheless, the cost is separate from the lease rental. Therefore, the bank does not allocate the cost to periods in the lease term.

As for Bumiputra Commerce, the bank follows the guidelines of the IAS 17. The initial direct cost should be allocated to the periods in the lease term or charged directly in the income statement as an expense. However, only Public Finance follows the guidelines of Bank Negara Malaysia.

Valuation of *Ijarah* Accounts Receivable.

The last issue, which is the measurement of *Ijarah* accounts receivable, is considered not applicable for BIMB. This is due to the fact that BIMB is using cash basis. As for OCBC, the method that the bank uses is based on total rental. OCBC does not use the cost equivalent value as proposed by the AAOIFI's standard. It also has provision for the account receivable. The policy used for the provision is 2.1%.

The method that Public Finance uses is based on market value. The bank does not use the cost equivalent value as proposed by the AAOIFI's standard. It also has provision for the account receivable. The policy used for the provision is 1.5% as given by Bank Negara Malaysia (Garis Panduan 3).

However, the valuation that Bumiputra Commerce uses is based on the actual amount paid by the customer. The bank has provision for the account receivable. The policy used for the provision is 1.5% as given by Bank Negara. The method that IDB uses is also based on actual amount paid by the customer. The bank does not use the cost equivalent value as proposed by the AAOIFI's standard although the bank claimed that it only adopts the AAOIFI's standard for its accounting practices.

Conclusions

The findings on the comparison between *Ijarah* and conventional leasing from the legal and accounting aspects showed that there are significant differences between these two contracts. Hence, *Ijarah* should not be seen as an imitation of conventional leasing since the definitions, types, principles, objectives, presentation, measurement methods, disclosure and substance of *Ijarah* are dissimilar to those of conventional leasing.

It can be concluded here that the main reason why some of the statements set by the AAOIFI have a score lower than 3 is that AAOIFI treats them differently compared with the IAS 17 and MASB 10 and some of the treatments only exist in the AAOIFI's standard and not in the IAS 17 or the MASB 10. Furthermore, most of the *Ijarah* practitioners in Malaysia still use the IAS 17 and MASB 10 as their main guidelines for *Ijarah*. Another reason why these statements have a low mean score is perhaps that, the *Ijarah* practitioners themselves are uncertain how to tackle *Ijarah* issues as most of them are following the IAS 17 and MASB standards for leasing, whereas what they are actually doing is *Ijarah* financing.

Furthermore, they may not be aware of the existence of the AAOIFI's standard for *Ijarah*. Therefore, they are still using the MASB 10 and IAS 17 as guidelines. This situation may be because of the lack of promotion of concern given by the higher authorities responsible for Islamic banking products in Malaysia to the adoption of the AAOIFI's standard. In other words, the AAOIFI's standard is not mandatory to be implemented in Malaysia. Hence, not many of the financial institutions are adopting the standard.

This study highlights the divergence of accounting practices on *Ijarah*. From the questionnaire survey, it is discovered that most financial institutions used Malaysian accounting standards on leasing (MASB 10) as a guide for accounting practices on *Ijarah*. The results from the interview survey confirm this finding and highlights further constraints that Malaysian financial institutions have to abide. In the case of recognition of income, with the exception of BIMB and IDB, BNM rule to use the sum of year digits has been used by all financial institutions.

The interview survey also shows that BIMB and IDB are the two financial institutions that adopted most of the AAOIFI's FAS 8 requirements. It is understandable as BIMB is the first established Islamic banks in Malaysia and IDB is a foreign Saudi Arabia based development bank. This indicated that other Malaysian financial institutions are not well exposed and introduced to the AAOIFI's accounting standards. This results in a low level of acceptability of AAOFI's FAS 8.

This low level of acceptability of AAOIFI FAS 8 is not unexpected due to the fact that AAOIFI's standard was initially designed for Islamic financial institutions and not financial institutions that undertake Islamic financing transactions. However with the introduction of FAS No.18, Islamic Financial Services offered by Conventional Financial Institution to be effective January 2003, non-Islamic financial institutions are expected to comply. In Malaysia GP8 (Malaysian Central Bank's rules and guidelines on financial reporting) is the regulatory device that influences financial reporting of financial institutions. A small sample size of 13 responses would be indicative rather than conclusive as to indicate the level of acceptability. Future research may try to include a profile analysis developed through focus group survey. Hence, it may be able to capture more useful information for the study.

This study also indicates, subject to further study on other Islamic financial instruments and other Islamic countries, the effort to harmonise the accounting practices on Islamic financing by financial institutions internationally may be difficult task. Until and unless it is adopted by the respective countries regulatory agencies, AAOIFI standards will remain only as a reference but do not have the legal authority. Significant efforts are required from the AAOIFI through publicity negotiation, and lobbying process to "market" its accounting standards to further enhance the credibility and comparability of accounting information of Islamic financing such as *Ijarah.*

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