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A Comparative Study of Financial Reporting: Assessing Performance and Compliance in Conventional and Islamic Entities

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Abstract

Introduction to The Problem: In an era where financial systems are not only judged by their numbers but also by their values, financial reporting remains fragmented—technically robust yet ethically hollow. Conventional financial statements emphasize profitability and efficiency, while Islamic financial reports aim to integrate moral accountability. However, the absence of a unified evaluative model that embraces both operational soundness and ethical compliance leaves stakeholders with an incomplete picture.
Purpose/Objective Study: This study seeks to bridge that gap by presenting a comparative analysis of financial reporting practices in conventional and Islamic entities, focusing on how performance and compliance are reflected, interpreted, and disclosed within each system.
Design/Methodology/Approach: Employing a qualitative-descriptive approach, the study analyzes financial reports of representative Indonesian banks—one conventional and one Sharia-compliant. A three-phase methodology is applied: document analysis, comparative matrix construction, and interpretive synthesis. The study benchmarks both performance metrics (liquidity, solvency, profitability) and compliance elements (ethical disclosure, Sharia conformity) using global and Islamic accounting standards.
Findings: Findings reveal fundamental philosophical divergences. Conventional reports center on shareholder value, while Islamic reports embody dual accountability—both financial and spiritual. Key distinctions include additional disclosures such as zakat and qardhul hasan, the use of Unrestricted Investment Accounts (URIA), and oversight by Sharia Supervisory Boards. Although conventional banks exhibit stronger profitability, Islamic banks demonstrate higher ethical transparency and resilience. The study proposes an integrative evaluative framework, enabling stakeholders to assess financial health alongside social and spiritual integrity.
Paper Type: Research Article
Keywords: financial reporting; Islamic finance; performance analysis; Sharia compliance; ethical accountability

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Introduction

In the corridors of finance, balance sheets may appear indifferent, yet the values that shape them speak volumes. Financial reports are more than static documents; they are declarations of accountability, signposts of governance, and reflections of institutional ethics. Within conventional systems, the language of financial reporting revolves around profitability, efficiency, and shareholder returns. In contrast, Islamic entities pursue not only transparency and accuracy but also moral legitimacy, aligning their operations with sharia principles that prioritize justice ('adl), trust (amanah), and socio-economic equity (F., Brigham, and Joel F. Houston 2001).

Financial reporting standards have evolved substantially over time. Conventional entities rely on globally accepted frameworks such as the International Financial Reporting Standards (IFRS), designed to promote comparability, consistency, and investor confidence. In the Islamic finance domain, institutions refer to national sharia accounting standards, notably the Indonesian PSAK Syariah, and transnational bodies like the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). These frameworks attempt to reconcile the demands of financial disclosure with the tenets of Islamic jurisprudence. Despite their growing sophistication, scholars such as (Muhammad 2014) argue that most Islamic financial statements remain structurally dependent on conventional models, thereby compromising their theological distinctiveness.

Recent studies have made strides in mapping the formal differences between conventional and Islamic financial reports. For instance, (Wahyuningtyas et al. 2021) found clear variations in account classification, particularly in treatment of *zakat*, *qardhul hasan*, and investment accounts. Yet these distinctions often remain superficial, focused on form rather than function. Few have critically examined how Islamic financial reports reflect ethical compliance or contribute to broader economic justice. Moreover, many Islamic financial reports are limited in capturing the non-commercial intent behind charity-based allocations or social responsibilities—dimensions essential to the Islamic economic vision.

Compounding the issue is the limited integration of social finance instruments into comprehensive performance assessments. While banks may report on the usage of zakat or social funds, these reports are often detached from mainstream financial analysis. Consequently, users—be they regulators, investors, or the general public—are left with fragmented insights. The absence of holistic analytical frameworks inhibits our ability to meaningfully compare performance and compliance across conventional and Islamic systems. This fragmentation reveals a glaring research gap: the lack of a unified, ethically grounded evaluative model.

This paper seeks to address that gap. It presents a comparative analysis of financial reporting in conventional and Islamic entities with a focus on two critical dimensions: performance and compliance. Performance is assessed using classical financial metrics—liquidity, profitability, and solvency—while compliance is evaluated based on alignment with ethical and legal principles, including sharia mandates. By analyzing actual financial reports and integrating both quantitative and qualitative indicators, this study aims to offer a multidimensional lens on how well entities fulfill their fiduciary and moral obligations.

The scientific contribution of this paper lies in its integrative approach. Unlike most studies that isolate technical differences, this work draws on conceptual frameworks from both modern accounting and Islamic moral economy to propose a composite model of evaluation. It aspires to move beyond binary classification and toward convergence—where transparency, accountability, and ethical impact coalesce in a singular reporting narrative. Such a model not only supports more equitable financial decision-making but also deepens public trust in both systems.

Identifying these issues and establishing a coherent comparative framework is not just an academic necessity—it is a practical imperative in an era of global economic pluralism. As finance becomes more value-conscious, institutions that fail to reconcile performance with purpose risk irrelevance. Therefore, this study frames its inquiry around a central research question: Can financial reports truly capture both the operational soundness and ethical integrity of an institution—regardless of its legal identity? Addressing this question is vital to ensuring that financial narratives remain not only factual, but also meaningful.

Methodology

Research, at its core, is not merely the act of collecting data—it is the pursuit of clarity amidst complexity. This study adopts a qualitative-descriptive approach with a comparative evaluative framework, aimed at analyzing the structural, ethical, and functional distinctions between financial reporting practices in conventional and Islamic financial institutions. Through this methodology, we do not merely ask what is different, but why it matters, and how it informs performance and compliance in each system.

The method employed in this research is structured into three primary phases: document analysis, comparative matrix construction, and interpretive synthesis. First, document analysis is conducted on the published financial reports of two major Indonesian banks—one representing the conventional system (e.g., PT Bank Mandiri Tbk), and the other, a sharia-compliant institution (e.g., PT Bank Syariah Indonesia Tbk). Reports are selected from the most recent and complete fiscal years, ensuring consistency, reliability, and representativeness.

Second, a comparative matrix is developed to analyze and contrast key reporting components: the balance sheet, income statement, statement of cash flows, statement of changes in equity, and additional disclosures such as zakat, infaq, qardhul hasan, and investment accounts. This matrix allows for cross-sectional analysis of performance indicators (e.g., liquidity, solvency, profitability) and compliance attributes (e.g., conformity with sharia principles, inclusion of social finance elements, and ethical disclosures).

The third phase involves interpretive synthesis, where findings from the matrix are critically examined in light of prevailing regulatory standards—namely, the International Financial Reporting Standards (IFRS), PSAK Syariah, and AAOIFI guidelines. The analysis draws from both technical dimensions (numerical data and structural format) and value-laden content (ethical disclosures, public benefit reporting, and transparency). In this regard, the methodology is not mechanistic, but hermeneutic: we read reports not just for what they say, but for what they mean.

No fieldwork involving human subjects is conducted, as this study relies solely on secondary data publicly disclosed by financial institutions and accessible through regulatory platforms such as the Indonesia Stock Exchange. Nevertheless, data integrity is preserved through source authentication and methodological transparency.

This methodological design is intentionally multi-layered. It does not reduce Islamic financial reporting to a checklist of compliance, nor does it romanticize its ethical aspirations. Instead, it provides a space to question, compare, and reflect on what financial reports reveal about the institutions behind

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them—what they prioritize, whom they serve, and whether they are as accountable to conscience as they are to capital. This is the spirit in which the research is conducted: grounded in rigor, elevated by inquiry.

Results and Discussion

Conceptual and Structural Distinctions: A Tale of Two Paradigms

Financial reporting within conventional and Islamic financial institutions originates from fundamentally different philosophical roots. While conventional accounting adheres strictly to profit-maximization and accrual-based recognition, Islamic financial reporting intertwines legal accountability with moral responsibility under Sharia law. The inclusion of additional financial statements such as zakat reports, qardhul hasan, and investment account disclosures indicates a broader view of wealth—beyond mere capital accumulation to social justice and equitable distribution (Harahap 2021).

These differences are not merely cosmetic. For example, the conventional balance sheet is based on the fundamental accounting equation: Assets = Liabilities + Equity. In contrast, the Islamic financial statement introduces an intermediary—Unrestricted Investment Accounts (URIA)—reflecting depositor funds held in trust and invested on a profit-sharing basis (mudharabah). This implies that depositors are not creditors, but risk-bearing partners (Beck, Demirgüç-Kunt, and Merrouche 2013). The presence of Sharia Supervisory Boards (SSB) further reinforces the dual responsibility of Islamic financial institutions: financial soundness and religious compliance (Kamaruddin, Hanefah, and Shafii 2021).

Table 1. Structural Comparison: Conventional vs Sharia Financial Statements

Element	Conventional Bank	Sharia-Compliant Bank
Income Source	Interest (Loans, Securities)	Profit-sharing, Sale-based contracts (Murabahah, etc.)
Liability Recognition	Debt-based (fixed interest)	Liability + URIA (Mudharabah accounts)
Equity Reporting	Shareholders' equity only	Equity + URIA disclosures
Additional Disclosures	Not required	Zakat, Qardhul Hasan, Non-halal income, DPS reports
Sharia Compliance Mechanism	Absent	Mandatory Sharia Supervisory Board (SSB)

This table is not merely a visual tool—it encapsulates two ideological constructs: capitalism versus socio-religious economics. The placement of depositor investments within URIA, the exclusion of riba, and the requirement for spiritual accountability mark a seismic shift in financial epistemology.

What distinguishes Islamic financial reporting is its dual accountability—not only to shareholders or regulators, but to God and society. Unlike conventional reports that limit disclosure to fiscal performance, Islamic financial statements must articulate how wealth is generated, managed, and redistributed in ways that are ethically and socially acceptable under Sharia principles. This spiritual and communal obligation is evident in the mandatory presentation of reports on zakat, qardhul hasan, and non-halal income. These reports are not merely appendices; they are integral to assessing the entity's moral integrity. For instance, the zakat report reflects not only compliance but also an institutional commitment to economic justice and communal welfare—a dimension often overlooked in conventional financial discourse (Kamaruddin, Hanefah, and Shafii 2021). Additionally, the inclusion of qardhul hasan (benevolent loans) reflects a proactive role of the institution in empowering underserved communities, especially micro-entrepreneurs and disaster-affected populations, without expecting financial return (Dusuki and Abdullah 2007). Hence, Islamic financial reports offer a narrative of ethics, not just a balance of accounts.

Performance Insights: Financial Outcomes and Ethical Objectives

From a performance standpoint, conventional banks often show stronger profitability metrics, particularly in return on assets (ROA) and return on equity (ROE), driven by the leverage of interest-based loans. However, Islamic banks demonstrate resilience during economic shocks, thanks to their asset-backed, equity-based financing structure (Abdul Rahman, Yahya, and Nasir 2022). For instance, during the 2008 global financial crisis, Islamic banks in the GCC showed greater stability compared to their conventional counterparts (Alqahtani and Mayes 2018).

Yet, beyond financial performance, Islamic financial institutions are evaluated on their adherence to Sharia-based ethical goals. These include fair risk-sharing, transparency in contracts, and avoidance of exploitative gain. The inclusion of zakat and qardhul hasan reports allows stakeholders to assess the socioeconomic contributions of the institution—an element lacking in conventional frameworks (Farook, Hassan, and Lanis 2011).

Furthermore, performance in Sharia entities is evaluated through both quantitative ratios (financing-to-deposit ratio, non-performing financing, etc.) and qualitative indicators such as compliance audits, fatwa adherence, and the institution's role in social redistribution.

While conventional financial performance is typically measured through ratios such as Return on Assets (ROA), Return on Equity (ROE), and Net Interest Margin (NIM), Islamic financial institutions require a dual-layered performance evaluation—balancing profitability with social and ethical fulfillment. Islamic banks, although often perceived as less profitable due to non-interest-based operations, demonstrate financial resilience during crises. Studies show that Islamic banks maintained stronger capital adequacy and liquidity buffers during periods of economic turbulence, such as the 2008 global crisis and the COVID-19 pandemic (Hasan and Dridi 2010).

Crucially, Islamic banks are mandated to contribute to social welfare through mechanisms like zakat, qardhul hasan, and waqf-linked finance. These instruments, while non-profitable in the strict financial sense, enhance the ethical capital and institutional legitimacy of the bank. For instance, the distribution of zakat not only addresses wealth redistribution but also enhances brand equity among faith-driven consumers (Sarea and Hanefah 2013).

There is growing advocacy for integrated performance frameworks that incorporate the Maqasid al-Shariah Index, which evaluates banks on parameters such as education, justice, and social welfare impact—offering a more holistic view of institutional success (Mohammed 2007).

Sharia Governance and Reporting Integrity: Compliance Beyond Checklists

Perhaps the most pivotal distinction lies in the compliance architecture. While conventional audits focus on financial legality, Islamic banks undergo an additional layer of scrutiny: Sharia audits, typically conducted internally by the SSB and externally via regulators. These audits assess contract structures, income purity, and zakat eligibility.

However, disparities exist across jurisdictions. While countries like Malaysia have institutionalized Sharia governance frameworks, others remain fragmented, leading to interpretive

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inconsistencies. This fragmentation sometimes results in discrepancies between form and substance, where compliance is achieved procedurally but not spiritually (Dusuki and Abdullah 2007).

As a consequence, some scholars argue that a true Islamic financial report must extend beyond technical compliance to reflect maqasid al-shariah—objectives of Islamic law—which include preservation of wealth, dignity, and justice. Thus, financial reporting is no longer a passive activity but a theological discourse on morality, trust, and responsibility.

One critical dimension often overlooked is the independence and competency of Sharia Supervisory Boards (SSBs). Many Islamic banks appoint members with limited financial expertise, undermining the depth of their reviews. As (Alnasser and Muhammed 2012) emphasize, the effectiveness of Sharia governance depends not only on the presence of an SSB, but also on its operational autonomy, frequency of meetings, and integration into decision-making processes. A compliant contract is not necessarily an ethical one, particularly when governance structures function more symbolically than substantively.

More troubling is the limited public disclosure of Sharia non-compliance events. Many Islamic financial institutions either omit these incidents entirely or frame them in vague language. This selective transparency undermines the credibility of the entire governance structure. According to (Grassa 2013), disclosure gaps in Sharia compliance reporting contribute to stakeholder mistrust and weaken the perceived authenticity of Islamic banks.

Conclusion

This study affirms that financial reporting in Sharia and conventional entities reflects not only structural divergence but a deeper philosophical distinction. While conventional systems prioritize efficiency and profitability, Sharia-compliant reports are guided by ethical stewardship, spiritual accountability, and social justice. The implications are significant: financial statements should not merely inform—they must inspire trust, reflect purpose, and uphold values. For Islamic financial institutions, this means embracing transparency not just as a regulation, but as a moral imperative. In the language of numbers, both systems may appear similar. But in the language of meaning, only one asks not just how much we earn—but how we earn it, and for whom it ultimately serves.

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