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Conceptual Framework of IFRS and Islamic bank's Financial Reporting

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Abstract:

The recording and disclosing of financial transactions are executed by following a set of principles and standards issued by standard setting bodies. The prohibition of Riba and requirement of following Shariah guidelines by Islamic banks motivated experts and scholars to advocate for separate set of accounting standards. In this study, a thorough critical examination is presented of two main aspects i.e., 'time value of money' and 'substance over form' which make base for separate accounting standards for Islamic banks. The study concluded that, time value of money is accounted in Islamic finance when investment is done in real assets and economic substance of Islamic financial transactions is not different from its legal. However, if there is a difference in substance over form then economic substance shall prevail. In the end, the accounting standards issued by ICAP on Murabaha is comparatively analyzed with AAOIFI guidelines and how well IFRS provisions address the recording of Murabaha transactions without violating Shariah provisions while keeping in view the time value of money and substance over form

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1. Introduction and Background of the Study:

Islamic banks are operating on completely separate set of operational procedure as far as financial instruments and provisions of financial services for individuals and at corporate level is concerned. The difference in operations of Islamic banks is in comparison with conventional or traditional banks and in this regard, Islamic banks entirely contradict in theme of developing their financial products. On the basis of this drastic difference, Islamic banking research has focused on formulation of every aspect to be totally different from conventional financial institutions. These endeavoring aims and efforts have taken the Islamic banking industry to a new level of research and build a strong theoretical and conceptual base for the smooth operational management of Islamic banking industry (Mehreen et al. 2020).

Moreover, it is considered that Islamic accounting discussion and research is relatively a new concept as compared to Islamic banking and finance discussions and research activities. Therefore, a very little discussion in literature has been done on the efficacy and significance of Islamic accounting in the context of Shari'ah guidelines. Hannifa and Hudaib (2010) discussed this issue in their paper, in which they pondered upon two issues, i.e., what is Islamic accounting and why research on Islamic accounting is important. They concluded that, lack of platforms for research on these topics made this issue more suppressed and therefore, suggested a journal specified for this purpose.

The pursuit of creating completely different and unique guidelines for Islamic banking operation from conventional counterpart also addressed and meticulously examined the accounting requirements of Islamic banks. In this regard, very thorough and comprehensive research work has been done which led to the foundation of Accounting & Auditing Organization for Islamic Financial Institutions (AAOIFI). AAOIFI is providing guidelines and standards for Islamic banks and financial institutions in fields of Shari'ah, accounting, auditing, governance and ethics. But due to no implementation power of the organization, no Islamic bank around the globe is following accounting standards issued by AAOIFI for preparation and disclosure of financial statements and information (Ehsan et al. 2018).

On the contrary, there is a strong argument which advocate about no need of separate accounting and reporting standards for Islamic banks and emphasized on sufficiency of already prevailing standards in fulfilling the needs of Islamic banks. Scholars and experts believe that, formulating a separate set of new accounting standards for Islamic banks is tantamount to reinventing the wheel. It is also believed that there is no concept which Islamize accounting, and accounting standards is just procedure and guidelines for recording and presenting financial transactions of an entity (Kamla 2009). Third point which emphasized on no need of separate accounting standards is that the world is going towards harmonization of accounting standards and hence Islamic banks need to focus on this aspect instead (Karim 2001).

The harmonization of accounting standards is emphasized to make financial statements easily interpreted all around the world by investors which allow them to make their decisions easily. The process of harmonization also reduces the cost of preparing financial statements for an entity. Hence, introducing a new set of accounting standards specifically designed for Islamic banks hinder the harmonization of accounting standards process. The advocates of harmonization of accounting standards also believe that introduction of separate set of accounting standards for Islamic banks would lead to isolation of Islamic finance industry worldwide which would consequently reduce the business of the industry (Karim 2001).

The proponents of need for separate accounting standards for Islamic banks focus their discussion on two main concepts in order to prove their point of view. These two concepts are 'time value of money' and 'substance over form'. These two concepts are termed as base for differentiating the accounting needs of Islamic banks from other prevalent accounting standards. It is therefore, necessary to have comprehensive brainstorming on the above mentioned issues in order to provide a well thought viewpoint for Islamic accounting standards. The current research study is mainly focused on provision of critical review of the two concepts in relation to Islamic accounting standards for Islamic financial institutions. The objective of the study is to present a comprehensive view which may provide way for harmonization of accounting standards without infringing any *Sharīʻah* guidelines.

The rest of the research study is organized as follows: the next section introduces and explains the significance of conceptual framework It is followed by discussion on two main discussed issues concerning to the topic i.e., time value of money and discussion on substance over form. Later, the concepts are examined in light of financial reporting requirements of Islamic banks. In the end a comprehensive discussion will be carried out regarding different issues in financial reporting of Islamic banks and their treatment in the context of ICAP[4], AAOIFI and how these aspects may be addressed by IFRS keeping in view the discussion on time value of money and substance over form. In the end, the study provides a comprehensive conclusion which may help in paving way for addressing the issues and matters raised in the study.

2. Conceptual Framework: Introduction and Significance

Conceptual framework is set of different concepts organized in a systematic and organized principles to make distinction on how different people view a single item in different ways. Financial Accounting Standard Board (FASB, 2010) defines conceptual framework for accounting standards in following words:

> "The Conceptual Framework is a coherent system of interrelated objectives and fundamental concepts that prescribes the nature, function and limits of financial accounting and reporting and that is expected to lead to consistent guidance. It is intended to serve the public interest by providing structure and direction to financial accounting and reporting to facilitate the provision of unbiased financial and related information. That information helps capital and other markets to function efficiently in allocating scarce resources in the economy and society."

It can be said that conceptual framework is basically providing statement of concepts which define objectives and fundamental concepts that act as baseline for the formulation and development of financial accounting and reporting guidelines.

[4] Institute of Chartered Accountants of Pakistan issued standards for accounting and reporting of financial transactions of Islamic banks of Pakistan.

AAOIFI defines conceptual framework as:

> *"*The Conceptual Framework introduces the main objectives as well as the concepts underlying financial accounting and reporting by Islamic financial institutions."
>
> "The Conceptual Framework provides the basis for the financial accounting standards of the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI*)."*

Whereas, according to IFRS (2018), conceptual framework is defined as follows:

> "The (conceptual) Framework's purpose is to assist the IASB (International Accounting Standard Board) in developing and revising IFRSs that are based on consistent concepts, to help preparers to develop consistent accounting policies for areas that are not covered by a standard or where there is choice of accounting policy, and to assist all parties to understand and interpret IFRS."

Hence, it can be concluded that formulating conceptual framework is inevitable in the process of construction of accounting standards. It is also observed that conceptual framework is more a structure to provide not only guidelines for the preparation of accounting standards but also provide enough discretion to the concerned authorities towards resolution of novel issues and problems. Additionally, it formulates basic objectives which mention the requirements of framing accounting standards.

According to AAOIFI the importance of establishing conceptual framework is to provide better understanding of the financial statements and enhancement of the confidence level of financial institutions. Conceptual framework endeavors towards harmonization of accounting standards and provide favorable environment for development of new accounting standards. Conceptual framework provides necessary guidelines to financial statement preparers regarding recording and disclosing of accounting information which is not covered under prevailing accounting standards. Conceptual frameworks help to interpret the accounting information recorded and disclosed in financial statements. Similarly, IFRS (2010) and FASB (2010) also emphasize on similar patterns and traits regarding the importance of conceptual framework as mentioned by AAOIFI accounting standards.

Hence it can be concluded that, the objectives of conceptual framework may be defined as to provide guidelines and basic framework of concepts necessary for the preparer of financial statements when faced with new and novel issues, no such accounting standard is available, and to make the process of recording and disclosing of financial matters easy and smooth.

2.1 Objectives of Financial Reporting

Financial reporting can be considered as process of measurement, recording and disclosing of financial information of transactions and other relevant matters. The purpose of this practice is to provide information to different stakeholders of the entity and also to keep record for various analysis of entity's own benefits. Therefore, while preparing financial reports the need of information of users should be taken into serious consideration in order to keep the effectiveness and significance of financial reporting intact.

The objectives of financial reports mentioned by conceptual framework of AAOIFI are as follows:

Financial reports should provide the following types of information:

- "Information about the IFI's compliance with the Islamic Shari'ah and its objectives and to establish such compliance, and information regarding the manner in which prohibited earnings and expenditures, if any, were recorded and dealt with."
- "Information about IFI's economic resources and related obligations (the obligations of the entity to transfer economic resources to satisfy the rights of its owners or the rights of others), and the effect of transactions, other events and circumstances on the IFI's economic resources and related obligations. This information should be directed principally at assisting the user evaluate the adequacy of the IFI's capital to absorb losses and business risks; assessing the risk inherent in its investments and; evaluating the IFI's liquidity position and the liquidity requirements for meeting its obligations and its operational requirements."
- "Information to assist in the determination of Zakah."
- "Information about the IFI's discharge of its fiduciary responsibilities"
- "Information about the IFI's discharge of its social responsibilities"

Similarly, the objective and usefulness of financial reporting mentioned by FASB are also very much same in its spirit and intention as mentioned above. It also says that the basic function or objective of preparing financial reports is to provide financial information of an entity in order to make this information useful for different stakeholders which include potential future investors, existing investors, lenders, creditors and customers. It is also to examine and analyze future prospects of entity in the context of cash flows, profits and other earnings (FASB 2010).

The objectives of financial reporting mentioned by conceptual framework issued by IFRS in 2010 also highlights similar sort of situations and features required to be disclosed in financial reports. The purpose of providing this level of information to stakeholders of financial reports is to deliver them enough information so that they can make their decisions regarding future investment avenues (IFRS 2010).

2.2Qualitative Characteristics of Accounting Information

In order to make the information relevant and useful for the stakeholders and easy to interpret for further analysis, accounting information should have some basic qualitative characteristics. These characteristics are supposed to satisfy or show compliance with the objectives of conceptual framework. Qualitative characteristics of financial information can be categorized into two categories, whereas, few others have categorized these into six different features and some have categorized these characteristics into four features. The two main unanimously agreed categories are relevance and reliability, whereas, some believe that relevance and faithful representation are fundamental characteristics of financial information and, comparability and consistency are secondary qualities (Smith 1996).

There are others complementary characteristics which enhances the already mentioned features and characteristics of financial information and these are understandability, materiality and conservatism (Beest, Braam and Boelens, 2009). According to AAOIFI accounting standard number 02, the qualitative characteristics of financial reporting are; relevance, reliability, neutrality, comparability, consistency and understandability. All these features should be intrinsic features of financial reporting in order to make them useful and significant for stakeholders to make their decisions with easement.

In view of these qualitative characteristics the advocates of need for separate accounting standards for Islamic banks present two main issues in prevailing accounting standards which do not accommodate the need of accounting requirements of IFIs. These two concepts are 'time value of money' and 'substance over form' and in the below section a detailed, comprehensive and thorough discussion shall be done on these points in order to examine the significance of separate and specialized accounting standards for Islamic banks.

3. Time Value of Money

Time value of money can be defined as amount of money owned in present time is worth more than the same amount of money in any future time. The rise in overall prices or inflation causes the purchasing power of people to decline which means that disposable income of consumer declines. Since the disposable income of people decline, the value or purchasing capacity of a unit of money also declines and therefore, value of money declines (Irena and Mariana, 2017). In order to address the issue of time value of money in financial management, different techniques are used which are known as compounding, discounting, capitalization, and Indexing. All these techniques allow financial managers, investors and lenders to calculate the level of interest rate to be charged on loans and profit rates on future investments.

On the other hand, one of the basic and fundamental difference among conventional and Islamic financial system is interest (Riba) and focus of research scholars remained on the discussion of providing strong rationale which differentiates Islamic finance. Therefore, every aspect of conventional finance and financial management which somewhat discuss or manage the issue of interest was taken seriously and full efforts were made to negate the concept in its full capacity. Similar sort of criticism and issues were also faced by time value of money by Islamic scholars and researchers but as mentioned earlier, this criticism later evolved into a more comprehensive and thorough logical point of view.

Khan[5] (1991) focused his discussion on the concept of time value of money and discounting in Islamic perspective. The study focused on a question that, does Islam permit or consider time preference in its teaching of *Fiqh ul Muamalat*. Khan (1991, 2017) in both research studies emphasized on the modes of Islamic financing which intrinsically accommodate the time value of money i.e., deferred payment sales (*Bay Muajjal*), *Bay Salam*[6]

[5] Fahim Khan is Former Chief of Research Division, Islamic Research and Training Institute (IRTI), Islamic Development Bank (IsDB).

[6] Salam contract is a mode of transaction in which price is paid before delivery of product. The contract is approved form the sayings of the Prophet Muhammad SAAW and specifically approved for the needs of farmers after complete prohibition of Riba (interest).

and Murabaha (deferred payment sale). Bay Salam is an exception to general concept of sale contract and such a provision is given by Prophet Muhammad SAAW[7] to the farmers of Medina after the prohibition of *Riba* (interest) and specifically for the small scale farmers who faced liquidity issues (Ehsan and Shahzad 2015), (Rehman and Shahzad 2016; 2017).

The focus of Khan (1991, 2017) is that, in our daily life financial practices, value of time is always considered, for example, rent of a house accounts more than the amount of depreciation of the building and hence value of time in rent is considered. Therefore, rent, wages, *Bay Salam and Murabaha,* all consider and include fixed and pre-arranged component as reward for time. There are other scholars of early times of whom contemporary research on Islamic finance and banking is termed as authentic, advocated the permissibility of time value of money and discounting in Islam (Zarqa 1983 and Azhar 1986). But these scholars did not mention a proper criterion of setting and describing discounting.

Price paid in future is more or different from the cash price of a same transaction is due to: time preference and supply demand conditions. The amount of price which is to be paid in cash is not equal in value with the same amount if paid in future time, and therefore, future price is higher or different from the price paid immediately due to time preference. The second reason of different or higher amount of price to be paid in future time is, supply and demand condition, which states that, price in market economies are set on equilibrium of supply and demand. Therefore, supply and demand condition in future would be different which means price would also be different from present time and hence, future price in deferred payment sale is different from the cash price amount (Khan 1991).

Zarqa (2017) proposed a model which advocates the existence of zero interest rate economy (ZIRE) and how time value of money is considered in such Islamic model of economy. Zarqa (2017) mentioned two main categories in Islamic finance and Islamic ZIRE i.e., loanable funds and investable funds. Loanable funds are not for profit activities which include loans of money or in any other kind, and should fulfill the purposes of charity, to help poor and encourage the concepts of brotherhood and solidarity. Any kind of reward or profit or interest in return of these type of loans or charitable transactions is prohibited in Islam and therefore, the concept of time value of money is not applicable in this section of the transactions.

On the other hand, investable funds are concerned with the investment funds which generate income and profit. This category of financing includes, trade credit sales i.e., deferred payment sales, equity financing mode, rental income of real assets. In all these modes profit, income or additional amount is gained after a certain period of time and all these financing modes are permissible. In deferred payment sale agreement, higher price is taken or given on deferred sales which is dependent on the amount of time given or taken to pay the price. In equity financing modes, investment of real assets is done through Mudarabah and Musharakah and such investment initiatives are done in a hope of earning profit in future time. The ratio or percentage of profit rises as the time period increases and therefore it can be said that time in this type of investment is priced.

[7] Hadith of Prophet Muhammad SAAW, “When Allah’s Messenger came to Medina, the people were paying one and two years in advance for fruits, so he said, Those who pay in advance for anything must do so for a specified weight and for a definite time.” (Bukhari: 2241)

Hence, a distinction has emerged between Islamic and conventional financial system that is distinction between rate of return and rate of interest in the context of time value of money. Islam allows rate of return to be decided on business transactions (investable funds), whereas, rate of interest is prohibited in Islam which is normally concerned with debt based or loanable funds and hence, time value of money is not taken into consideration (Zarqa, 2017). Zarqa (2017) came to a conclusion in which he stated that discounting is allowed in Islam, necessary to use in investment project evaluation. He said;

> "Discounting in investment project evaluation is meant to make comparable prospective sums of money or resources occurring at different time periods, thus, facilitating comparison of investment alternatives. Shari'ah scholars affirm the permissibility of such discounting, notwithstanding the fact that the same mathematical formulas are used in interest based lending."

The above discussion may be concluded that, discounting of financial management in Islamic perspective arises when investment decisions are to be made (Abdul Khir 2013*)*. It is because of the reason that, individuals go for investments for two reasons: first, for economic reasons i.e., earning profits in future and secondly, for non-economic or gratuitous purposes. Therefore, as long as investments done in *Sharīʻah* compliant ventures, discounting can be done to evaluate the efficiency of the option in terms of profit making, whereas, no reward is expected from this world in case of non-economic or gratuitous investments (zakat and voluntary charity etc.) and no discounting is required.

4. Substance over Form

4.1 Overview

The concept 'substance over form' is the second aspect which is termed as base for the justification of proposing alternative accounting standards for Islamic banks due to banks' entirely different scheme of financial operation. The concept may be defined as:

> "*Substance over form is an accounting concept which means that the* ***economic substance*** *of transactions and events must be recorded in the financial statements than just their* ***legal form*** *in order to present a true and fair view of the affairs of the entity."*[8]

Hence, it can be inferred from the above definition that there are two features of a financial transaction i.e., economic substance of the transaction and its legal form (Meyer 1976). Economic substance of the transaction is relevant to its operational existence and how does it operate and what sort of benefits it brings due to its operations. On the other hand, legal form is concerned with the mentioned or stated property of the financial product or transaction (Hopwood 1990).

According to Conceptual Framework of FASB (2010), substance over form can be elaborated as follows:

> "Substance over form is not considered a separate component of faithful representation because it would be redundant. Faithful representation means that financial information represents the substance of an economic

[8] https://accounting-simplified.com/financial/concepts-and-principles/substance-over-form.html

phenomenon rather than merely representing its legal form. Representing a legal form that differs from the economic substance of the underlying, economic phenomenon could not results in a faithful presentation."

The criteria for recording of financial transactions in view of their economic substance or legal form is also clarified in IASB conceptual framework of 2010 in following words:

> "In assessing whether an item meets the definition of an asset, liability or equity, attention needs to be given to its underlying substance and economic reality and not merely its legal form. Thus, for example, in the case of finance leases, the substance and economic reality are that the lessee acquires the economic benefits of the use of the leased asset for the major part of its useful life in return for entering into an obligation to pay for that right an amount approximating to the fair value of the asset and the related finance change. Hence, the finance lease gives rise to items that satisfy the definition of an asset and a liability and are recognized as such in the lessee's balance sheet."

Hence, more emphasis is inserted on economic substance of the financial transaction while recording it in view of IASB conceptual framework. The organization has come up to this concept after going through bitterness of recording legal form of financial transaction in the form of mega frauds like the case of Enron Corporation[9]. The issue of Enron led the accounting standards setters to rethink and revise their approach of rules based accounting standards to a more dynamic and principle based approach of accounting standard.

It can be concluded from the above discussion that, to precisely reproduce a company's financial position and results of actions, accounting standards should be applied in a method that is faithful not only to the verbal meanings of the standard, but reliable with the economic substance of the transactions of the unit. Looking for excuses to catch means about the language of the standards obscures financial reporting and troubles users of financial statements by generating information that is not a true reflection of economic reality (Baker and Hayes 2004).

4.2Substance over form and Islamic Financial Products

The pursuit of developing every aspect of Islamic financial architecture different from the conventional counterpart led to hinderance in availing useful of various conventional financial aspects without violating any *Sharīʿah* guidelines. Similarly, Islamic finance experts opined that in recognition and measurement of Islamic financial transactions, legal form of these transactions should be given more preference than its economic substance (Asian Oceanian Standard-Setters Group 2010). The importance of the concept is thoroughly mentioned in a study conducted by Asian Oceanian Standard-Setters Group (2010) in following words:

> "Many Islamic financial transactions are based on sales. Thus, there is an argument that the proceeds from such transactions should be accounted for as revenue from the sale of goods. However, in many cases, payment for the sold item is deferred. Under IAS 18, revenue on a sale of goods is measured at the fair value of the consideration received or receivables. When payment for an item is deferred, the fair value of the consideration may be less than the nominal amount of cash received or receivable. Whether advertently or by design, the economic effect of the sale may closely resemble that of a financing transaction.

[9] The company was founded in 1985 in Nebraska, USA, and ceased its operations in 2007. It had around 29000 employees and founder of the company were Jeffrey Skilling and Kenneth Lay. Headquarter of the company was in Houston, USA and it was a publicly listed company on New York Stock exchange. The field of operations of the company was energy sector.

In such circumstances, IAS 18 would require the difference between the fair value and the nominal amount of the consideration to be recognized as interest revenue.”

It is a matter of presentation of true picture of the financial transaction to focus on economic substance of the transaction when recognizing and recording the transaction in financial statements. Therefore, the point presented by IAS 18 that the difference between the fair value and the nominal amount of the consideration to be recognized as rate of revenue or profit.

It can be concluded that there is no contradiction between economic substance and legal form in Islamic financial products. It is because of the fact that discussion and issue of substance over form only comes into play where economic substance of any transaction is different from its legal form and only in these scenarios, substance is preferred over form.

5. Comparing IFAS with AAOIFI and IFRS

In this section of the study, an example of an accounting standard for Islamic banks of Pakistan issued by the Institute of Chartered Accountants of Pakistan (ICAP)[10] shall be examined and compared with the treatments provisioned by AAOIFI and IFRS. The purpose is to dichotomize the differences and similarities between accounting standard issuers and doing so would enable us to evaluate the efficacy of specifically issued accounting standards for Islamic banks.

5.1 Islamic Financial Accounting Standard (IFAS) 1: Murabaha

Three accounting standards have been issued for Islamic financial institutions by ICAP i.e., IFAS 1: *Murabaha*, IFAS 2: *Ijarah* and IFAS 3: Profit and Loss Sharing on Deposits. The requirements of the Islamic accounting standards issued by ICAP are similar to AAOIFI’s. It is necessary to mention that ICAP has taken the stance of declaring time of value of money illegal for IFIs (Asian Oceanian Standard-Setters Group, 2010).

In this study, the IFAS 1: Murabaha shall be taken as an example. The accounting practice prescribed for recognition and recording of financial transaction of Murabaha in IFAS 1 is given below:

The Murabaha transaction is recorded on the basis of historical cost convention and treatment of every aspect of inventory created due to Murabaha in IFAS 1 is prescribed as to follow the principles and guidelines issued by IAS and should be shown in ‘other assets’.

The profit recognition of Murabaha transaction is done in following way:

(a). “Purchases and sales under Murabaha and the resultant profit should be accounted for on the culmination of Murabaha transaction.”

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[10] “Institute of Chartered Accountant of Pakistan is a professional accountancy body in Pakistan. The institute was established on July 1, 1961 to regulate the profession of accountancy in Pakistan. The institute is also responsible for:

- Review and adoption of international accounting and auditing standards,
- Development of local standards and technical releases,
- Development of accounting standards for Islamic financing and investment,
- Preparation of draft proposals for finance bill and corporate laws,
- Response to the queries of members and other agencies.

The above support is implemented through the following:
Accounting standards Board.” (www.icap.net.pk)

(b). However the profit on that portion of sales revenue not due for payment should be differed by accounting for by a debt to ‘Unearned Murabaha Income’ account with the corresponding credit to ‘Deferred Murabaha Income’ account and shown in the balance sheet as a liability.”

5.2 Financial Accounting Standard No 2: Murabaha and Murabaha to the Purchase Orderer

Financial Accounting Standard (FAS) No. 2, issued by AAOIFI is guidelines for accounting treatment of Murabaha and Murabaha to the purchase orderer transaction. The recording treatment of Murabaha transaction in view of FAS 2 is also based on historical cost convention[11], which is same as of provision of IFAS 1 issued by ICAP. As far as, the accounting treatment of Murabaha receivable or amount to be received by the Islamic bank from customer[12] is concerned, it is also similar to the IFAS 1. The last aspect is accounting treatment of profit recognition and in this regard, the profit is recognized dominantly in similar manners in guidelines of both the accounting standard i.e., IFAS 1 and FAS 2.

5.3 Accounting Treatment of Murabaha in the context IFRS:

It is necessary to take into consideration about the discussion done in previous sections of the study on time value of money in Islamic perspective and matter of substance over form while examining the possible treatment of Murabaha in the context of IFRS.

Murabaha mode of transaction is used for the investment purposes and issuing entities intend to earn profits on these deferred payment sales. There are two ways to consider the Murabaha sale or transaction in conventional form of finance while considering its economic substance of the transaction. In this regard, if Murabaha transaction is considered or classified as financing arrangement, then “*IFRS 9: Financial Instruments*” can be applied to recognize and record the accounting of Murabaha transaction. This will not violate the Shari'ah guidelines in any respect as the only two major and core reservations on the conventional accounting treatment of Islamic products are; time value of money and substance over form, which are very much resolved in the current research study.

Secondly, if economic substance of the Murabaha transaction is classified as trading arrangement i.e., the Murabaha transaction or mode of financing is used for the purpose of trading of real goods which have intrinsic value on deferred payment then, “*IFRS 15: Revenues from Contracts with Customers*” can be applied and adopted to recognize the accounting structure of Murabaha transaction.

6. Conclusion:

Islamic banks are operating on completely separate set of operational procedure as far as financial instruments and provisions of financial services for individuals and corporate level is concerned. On the basis of this drastic difference, Islamic banking research has focused on formulation of every aspect to be totally different from conventional financial institutions.

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[11] “**2/1 Measurement of asset value at acquisition by the Islamic Bank:** *Financial Accounting Statement No. (2): Concepts of Financial Accounting for Islamic Banks and Financial Institutions* stipulates that historical cost shall be the basis used in measuring and recording the assets at the time of acquisition thereof”. *(FAS No. 2: Murabaha and Murabaha to the Purchase Orderer, Issued by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)*)

[12] “**2/3 Murabaha Receivables:** Short term or long term Murabaha receivables shall be recorded at the time of occurrence at their face value. Murabaha receivables are measured at the end of the financial period at their cash equivalent value i.e., the amount of debt due from the customers at the end of the financial period less any provision for doubtful debts, (para 7)” *(FAS No. 2: Murabaha and Murabaha to the Purchase Orderer, Issued by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)*)

It is also considered that Islamic accounting discussion and research is relatively a new concept as compared to Islamic banking and finance discussions and research activities. The pursuit of creating completely different and unique guidelines for Islamic banking operation from conventional counterpart also addressed and meticulously examined the accounting requirements of Islamic banks and AAOIFI is one of the major outcomes of this effort. On the contrary, there is a strong argument which advocate that there is no need of separate accounting and reporting standards for Islamic banks and already prevailing standards are sufficient enough to fulfill the needs of Islamic banks.

The proponents of need for separate accounting standards for Islamic banks focus their discussion on two concepts in order to prove their point of view. These two concepts are 'time value of money' and 'substance over form'. The current research study is mainly focused on provision of critical review of the two concepts in relation to Islamic accounting standards for Islamic financial institutions. The objective of the study is to present a comprehensive view which may provide way for harmonization of accounting standards without infringing any *Sharī'ah* guidelines.

The study comprehensively mentions the significance of conceptual framework in view of different accounting standard setting bodies. The purpose is to mention the importance and significance of issuing accounting standards and what need these standards are supposed to fulfill and what qualitative characteristics accounting information should possess. It is the qualitative characteristics which advocates of separate accounting standards for IFIs make the base and emphasized that the two main issues i.e., 'time value of money' and 'substance over form' which differentiates Islamic banks' transactions and accounting treatment from their counterparts.

The research study concluded that discounting of financial management in Islamic perspective arises when investment decisions are to be made (Abdul Khir 2013*)*. It is because of the reason that, individuals go for investments for two reasons: first, for economic reasons i.e., earning profits in future and secondly, for non-economic or gratuitous purposes. Therefore, as long as investments done in *Sharī'ah* compliant ventures, discounting can be done to evaluate the efficiency of the option in terms of profit making, whereas, no reward is expected from this world in case of non-economic or gratuitous investments (zakat and voluntary charity etc.) and no discounting is required.

As far as issue of 'substance over form' is concerned, the study concluded that there is no contradiction between economic substance and legal form in Islamic financial products. It is because of the fact that discussion and issue of substance over form only comes into play where economic substance of any transaction is different from its legal form and only in these scenarios, substance is preferred over form.

The concluding section of the study mentioned an example of accounting treatment guidelines of Murabaha issued by SECP and prepared by ICAP, and comparing its provisions with AAOIFI guidelines and evaluating its possible treatment in IFRS guidelines while taking into consideration the discussion on time value of money and substance over form. The study concluded that there is no difference in recording of Murabaha transaction in light of IFAS 1 and FAS 2. In addition to this, the study also concluded that if Murabaha transaction is considered or classified as financing arrangement, then "*IFRS 9: Financial Instruments*" can be applied to recognize and record the accounting of Murabaha transaction. Secondly, if economic substance of the Murabaha transaction is classified as trading arrangement i.e., the Murabaha transaction or mode of financing is used for the purpose of trading of real goods which have intrinsic value on deferred payment then, "*IFRS 15: Revenues from Contracts with Customers*" can be applied and adopted to recognize the accounting structure of Murabaha transaction.v