

AOSSG INTERIM MEETING

15 September 2022

Sharing of MASB's works on Islamic financial reporting

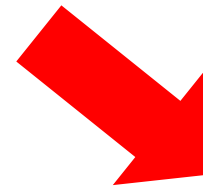
Objective

- ▶ To share with AOSSG members on MASB's work streams on Islamic financial reporting
- ▶ MASB's projects on Islamic financial reporting are generally divided into two work streams:



Standard-setting

Providing input to IASB draft pronouncements specifically from the Islamic financial reporting perspective



Research

Research about the application of IFRS Accounting Standards to existing or new Islamic financial transactions

Application of Malaysian Financial Reporting Standards (MFRSs) to Islamic Social Finance Transactions

Application of MFRS to Islamic Social Finance Transactions

- ▶ Accounting for Islamic social finance under the Malaysian Financial Reporting Standards (MFRSs) is one of the medium-term Islamic research projects
 - ▶ MFRSs are word-for-word IFRS Accounting Standards issued by the IASB
 - ▶ Financial statements that assert compliance with MFRSs shall also assert compliance with IFRS Accounting Standards
- ▶ Why this project?
 - ✓ Social finance is gaining traction and its use has been promoted as an integral part of the Islamic finance ecosystem in Malaysia

Application of MFRS to Islamic Social Finance Transactions

- ▶ What we will cover for today:
 - ✓ Objective of the research paper
 - ✓ Scope of the research paper
 - ✓ Example of a current Islamic social finance (“ISF”) offering
 - ✓ Recommendations of the research paper

Important note: The research paper is still in the draft stage and any points shared during this presentation should not be considered final.

Objective and Scope

- ▶ **Objective:** to provide accounting, reporting and disclosure guidance to Islamic financial institutions (“IFIs”) with Islamic Social Finance (“ISF”) programmes
- ▶ **Scope:** current ISF programmes funded by *zakat* (alms), *sadaqah* (donation) investment account placement and CSR fund, piloted under the Central Bank of Malaysia [*Bank Negara Malaysia* (BNM)]’s iTEKAD Programme
- ▶ Research methodologies
 - ✓ Review of publicly available materials, e.g., disclosures in general-purpose financial statements, sustainability reports, etc
 - ✓ Engagement with key stakeholders
 - ✓ Technical references: MFRSs and other regulatory documents

Definition of “Islamic social finance”

- ▶ For the purpose of the research paper, “social finance” is defined as:
 - ✓ financial structures and business models that aim to **generate sustainable financial returns** while delivering **tangible social outcomes** by mobilising philanthropic capital – this includes Islamic financial instruments such as *sadaqah* (donation), *waqaf* (endowment) and *zakat* (alms or compulsory “donation”).
- [adopted from: *Social finance as an enabler of social development in Malaysia*, BNM’s Financial Sector Blueprint 2022 – 2026]

Overview of Islamic social finance programme

- ▶ iTEKAD by Bank Negara Malaysia
 - ✓ a social finance pilot programme that **blends financial and non-financial services**
 - ✓ used as a platform to accelerate the mobilisation of Islamic financial instruments in **offering seed capital** to targeted customer segments.
 - ✓ IFIs with implementation partners, such as *state Islamic religious councils* (SIRCs) would offer **blended financial solutions** i.e. seed capital, micro-financing and structured training
 - ✓ Approved applications would undergo **training** conducted by appointed training providers - upon completion of the training, **financing** would be offered to eligible applicants
 - ✓ Sources of funds for the financing could be derived from SIRCs, IFIs' own allocated/CSR funds, public donors, etc.

Key recommendations: Accounting considerations

- ▶ The research paper considers the principles in MFRS 15 *Revenue from Contracts with Customers* and MFRS 9 *Financial Instruments* to study the appropriate accounting for Islamic social finance transactions

- ▶ Key considerations include:
 - ✓ Assess the contractual relationship between IFIs and fund providers;
 - ✓ Assess the rights and obligations (explicit or implied) established between IFI and fund providers – whether it is acting as an agent or as a principal. A principal or an agent depends on:
 - which party bears the substantial risks and rewards of the activities; and
 - which party controls the activities (an entity controls an activity if it has the present ability to direct the activity and obtain the economic benefits that may flow from it)

Key recommendations: Proposed disclosures

- ▶ The proposed disclosures shall be guided by the materiality principle as outlined in MFRS 101 *Presentation of Financial Statements* (or IAS 1 *Presentation of Financial Statements*)

- ▶ Among the recommended disclosures to be included in the general purpose financial statements:
 - ✓ Amount of zakat received from SIRC's that have been utilised for the ISF programmes;
 - ✓ SME financing amount under the ISF programmes;
 - ✓ Income and/or expenses in relation to the ISF programme
 - ✓ Off-balance sheet financing extended using crowdfunding platform/ extended by a separate entity which is managed by IFIs

Feedback or comments

- ▶ We would like to hear your feedback on your jurisdiction's experience in relation to Islamic social finance transactions
- ▶ For example, is there any guidance issued on accounting for Islamic social finance transactions?

An update to the study of financial statements of Islamic financial institutions

Financial Reporting by Islamic Financial Institutions

Background

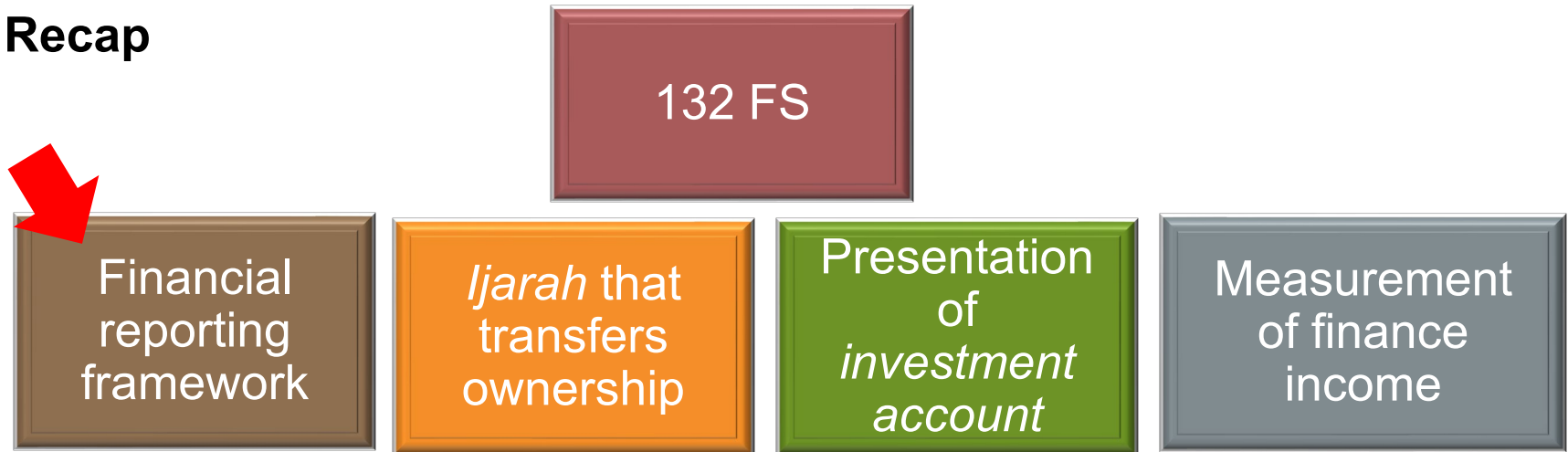
- ▶ At the 2014 annual meeting of the AOSSG, the Islamic Finance Working Group (IFWG) presented a study of 132 financial statements of Islamic financial institutions (IFIs) in 31 countries which was published in 2015
- ▶ An updated report was subsequently published in 2017

2022 work

- ▶ We see the importance of keeping abreast of the financial reporting frameworks applied by IFIs around the “world” (in our case, in the selected 31 countries), and hence we have included this in our 2022 work plan
 - ✓ We will share our preliminary findings with the AOSSG IFWG once we have completed the review; for members’ comments

Financial Reporting by Islamic Financial Institutions

Recap



- ▶ Sample size: 132 as selected from the list of ‘Top Islamic Financial Institutions by Country’ that appeared in the November 2013 issue of *The Banker*.
- ▶ Source: most recent annual financial statements publicly available in English as of 31 July 2022.

Financial Reporting by Islamic Financial Institutions

Classification of financial reporting frameworks

- ▶ All financial statements are classified as complying with one of three frameworks; **based on the assertion in their statement of compliance**:
 - ▶ **IFRS Accounting Standards (“IFRS”)** – IFRS as issued by the IASB; or IFRS as adopted by specific jurisdiction;
 - ▶ **Local GAAP** – asserted compliance with local GAAP or if it included a statement of compliance with IFRS but with a departure(s) to comply with local law(s)
 - ▶ **AAOIFI** – Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)

Financial Reporting by Islamic Financial Institutions



Initial findings

- ▶ 2022: 122 samples (2016: 132 samples)
- ▶ 10 are excluded due to the following reasons:

2: banking license revoked

- Turkey (2016: local GAAP)
- Mauritius (2016: IFRS)

5: mergers and acquisitions

- 3 from Indonesia (2016: local GAAP)
- 1 from Pakistan (2016: local GAAP)
- 1 from UAE (2016: IFRS)

3: latest publication unavailable online

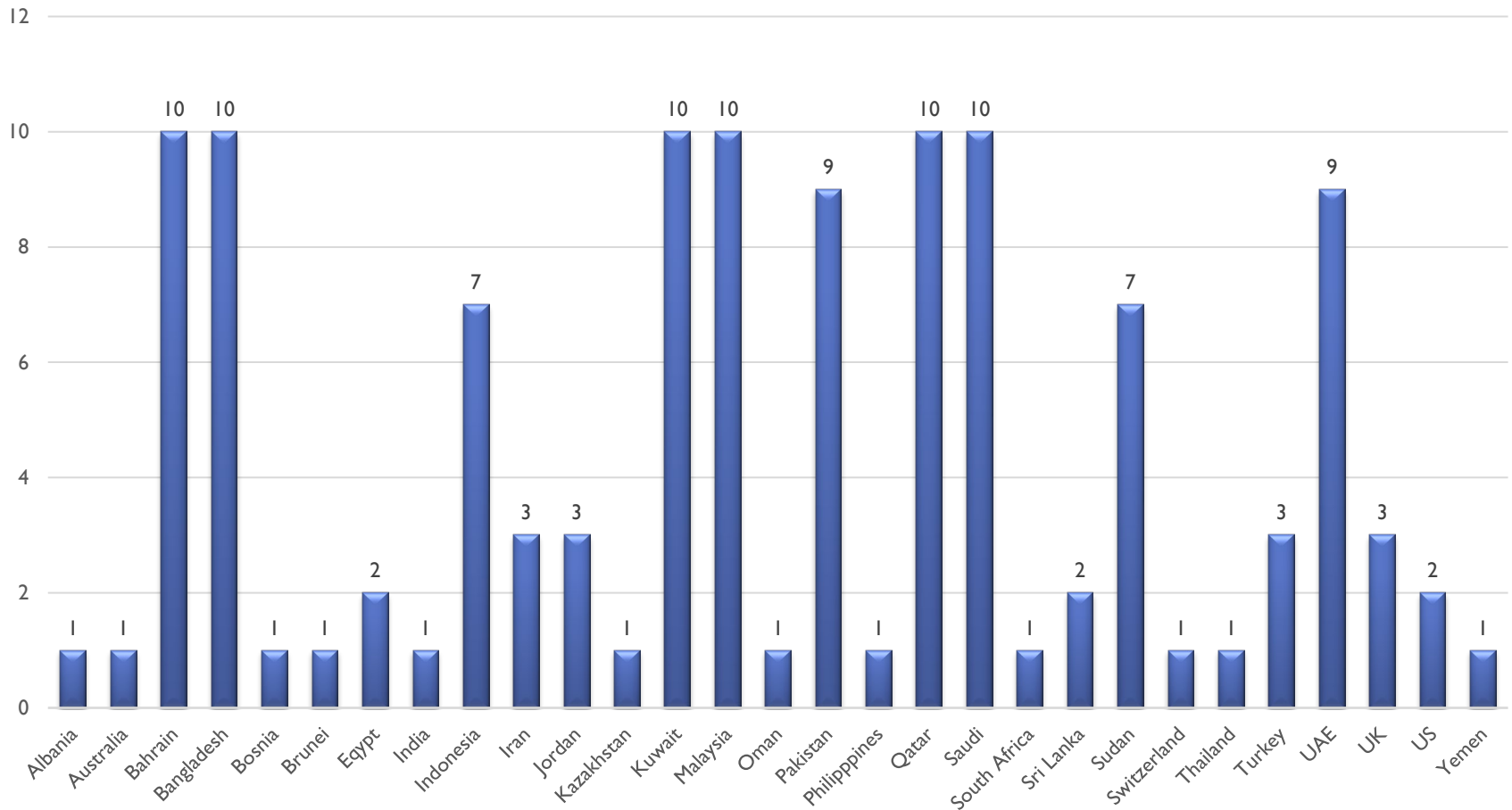
- Lebanon* (2016: AAOIFI)
- UK (2016: IFRS)#
- Iran (2016: Others)#

* Latest full set of financial statements published on the website was for FYE Dec 2012 (as of 30 Aug 2022)

financial reports were no longer available on their websites (as of 30 Aug 2022)

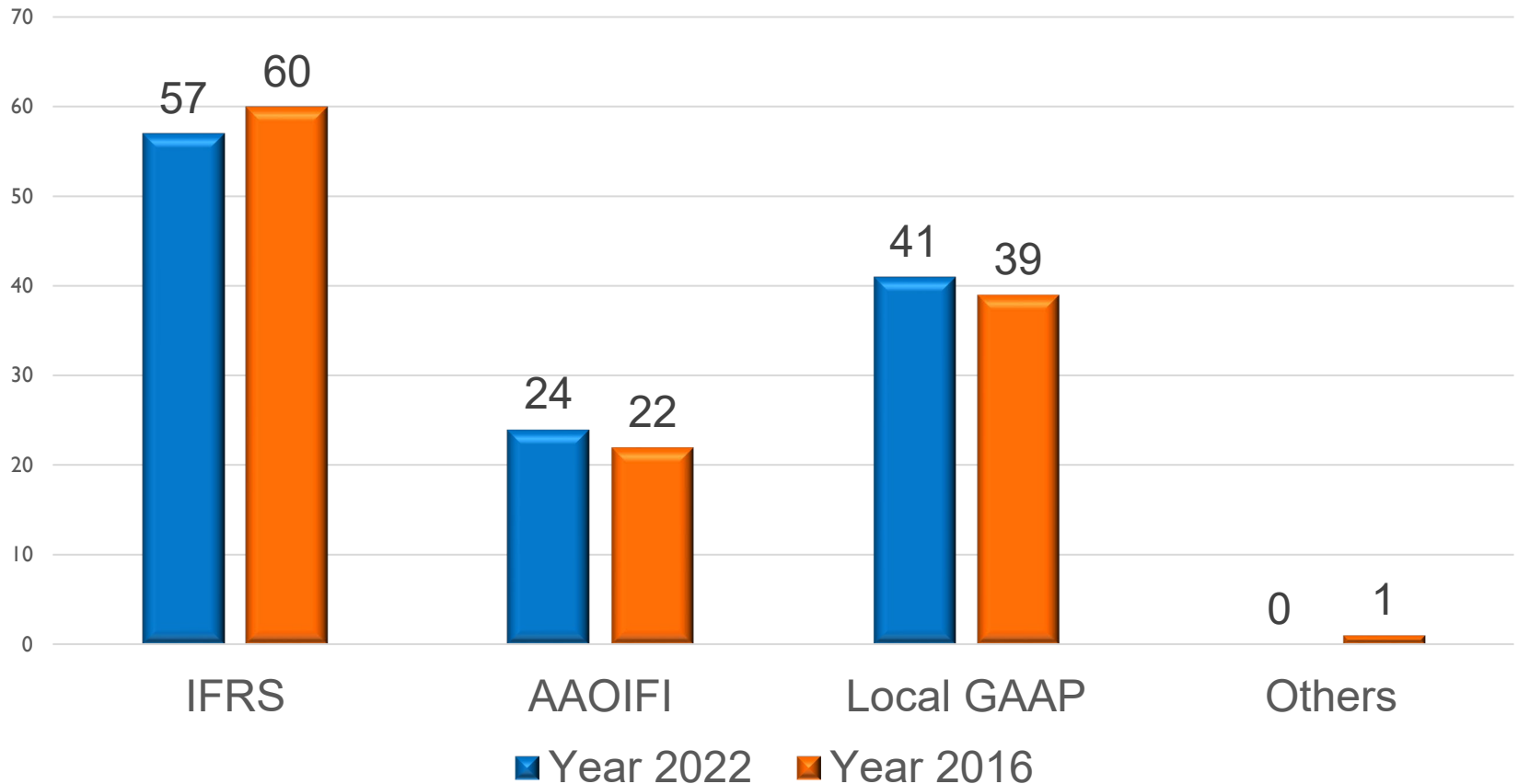
122 samples in 29 countries

122 IFIs by countries



Overall: No major movements noted

Financial reporting frameworks for 122 financial statements

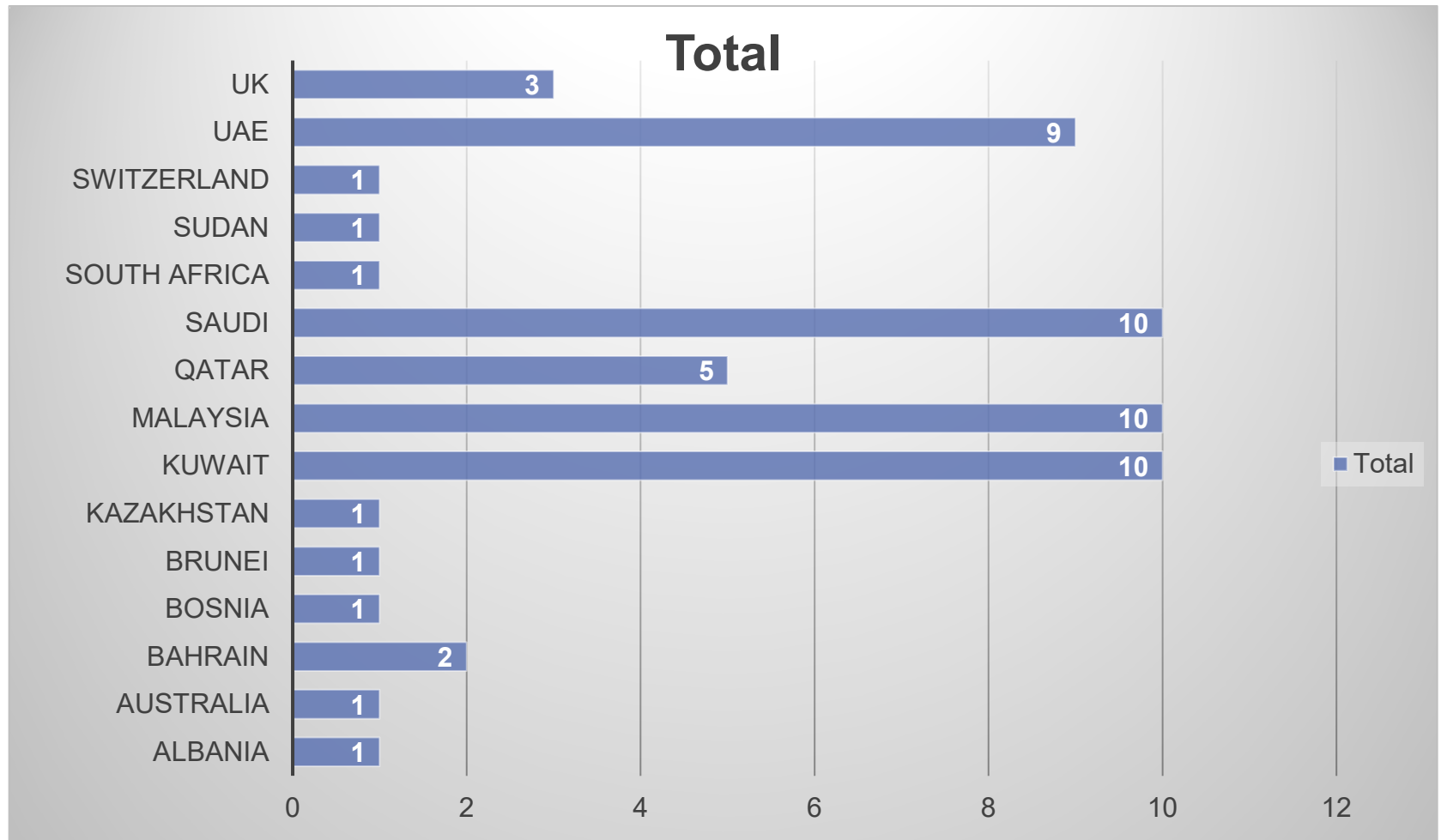


Others (2016) = Financial statements were prepared based on historical cost and market value

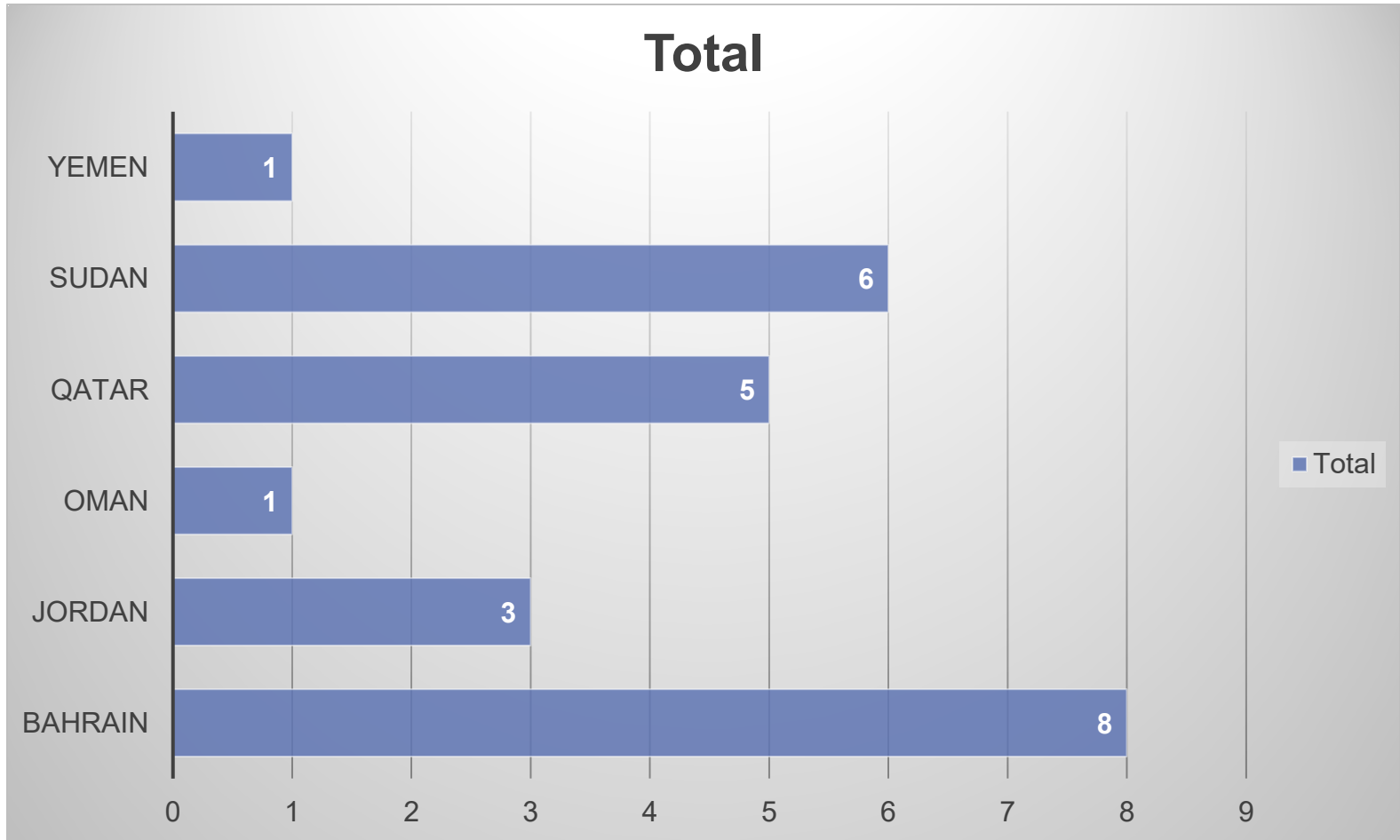
Movement between IFRS & AAOIFI

- ▶ IFRS decreased by 3 (2022: 57; 2016: 60) & AAOIFI increased y 2 (2022: 24; 2016: 22)
 - ▶ 2 banks stated compliance with AAOIFI's standards:
 - ✓ 1 Yemeni bank (FYE Dec 2020) – stated compliance with AAOIFI since FYE Dec 2015
 - ✓ 1 Qatari Islamic insurance company (FYE Dec 2021) – stated compliance with AAOIFI since FYE Dec 2019
 - No change to the remaining 9 samples [IFRS (5); AAOIFI (4)]
 - ▶ 1 bank in Türkiye (FYE Dec 2021) stated compliance with local GAAP since FYE Dec 2019
 - ✓ **The Bank however publishes a separate set of audited IFRS-compliant financial statements on its website**

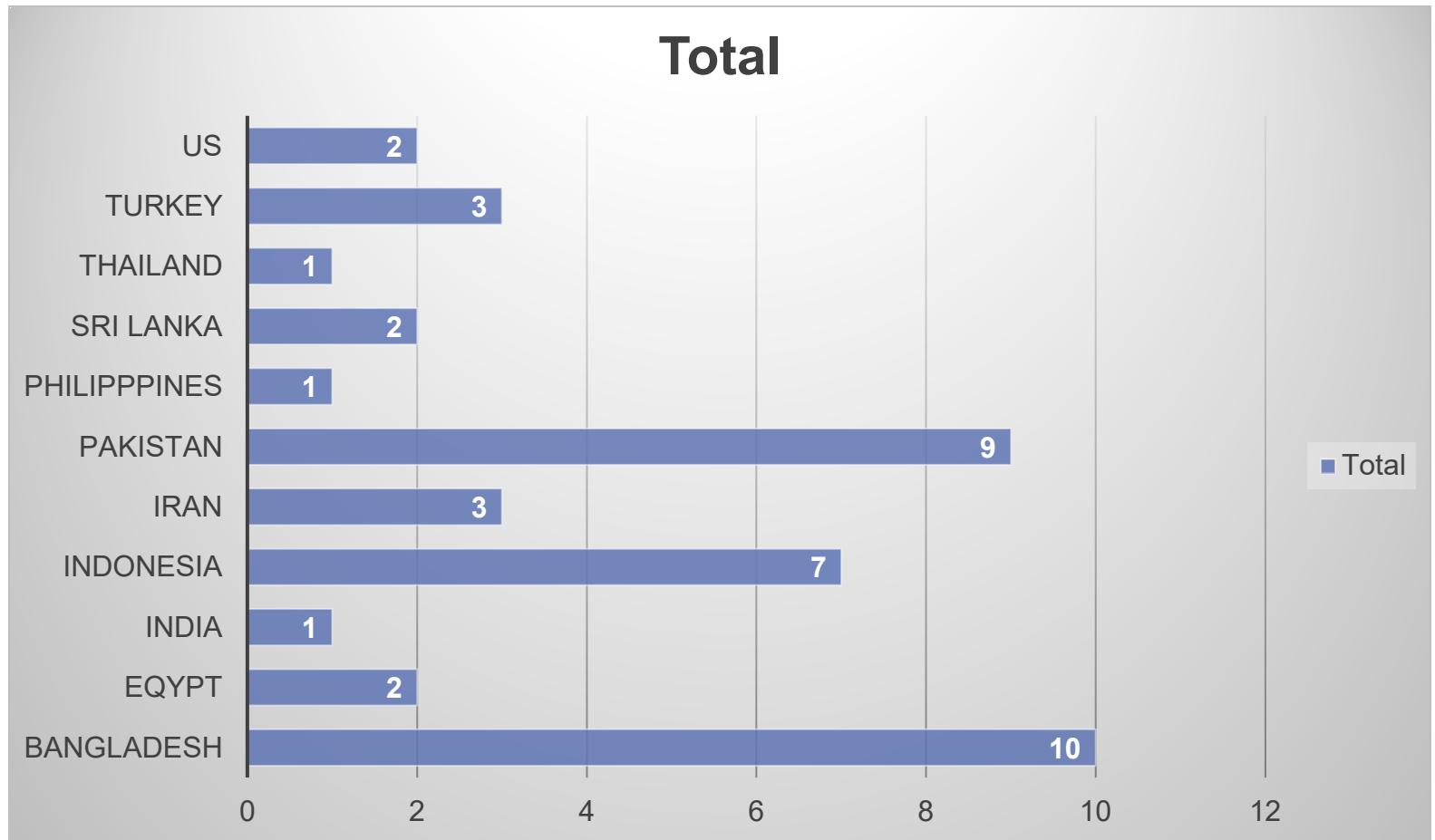
IFRS: 57 IFIs in 15 countries



AAOIFI: 24 IFIs in 6 countries



Local GAAP: 41 IFIs in 11 countries



THANK YOU