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# Shariah Supervisory Board's Conception of Accountability and Competency - An Ethnographic Study of Bank Muamalat Malaysia Berhad

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### ABSTRACT

**Background:** This study describes the rationales for the study and the importance of proper recognition of the accountability conception and competence among Shariah Supervisory Boards (SSBs) in the Islamic Financial Institution (IFI). **Objective:** This research examines the relationship between the level of accountability conception and competency of the members of Shariah Supervisory Boards (SSBs) of Islamic Financial Institution (IFI) on their main duties and responsibilities. It also examines the IFI interpretation and evaluate whether in accordance with Shariah principles; and the epistemological conception of accountability amongst SSB members in the IFI and examine the association between the level of competency and accountability of SSB. **Methodology:** In this study, the qualitative research method was applied and ethnographic research approach was employed so as to understand the social context on the accountability and level of competency amongst SSB. **Results:** The findings of this study primarily revealed that the SSB members dealing precisely with regards to the Shariah compliance comprehension in association with IFI interpretation and accountability conception. Moreover, this study also found that the epistemological conception of accountability emphasizes on the subjection, transparency, independence, confidentiality, faith and justice shows the relationship between self and statutory regulations positively influenced by Islamic business ethic. Hence, the association level of competency and accountability has a significant influenced in supporting SSB supervising the IFI accordingly. **Conclusion:** This research can make a significant contribution to the IFI in providing full range of knowledge and skills to determine the problems or issues pertaining to the concept of accountability among SSB. Results of the study could be used to improve existing services and formulate strategic decisions in order to achieve competitive advantage, designing and implementing suitable remedial measures.

### INTRODUCTION

Over the last decade, Islamic banking, finance and accounting has grown tremendously in Malaysia. The term "Islamic banking" indicates that the conduct of banking operations is in consonance with Islamic teachings which are based on Shariah principles. In view of this definition, the Islamic institutions are expected not to have the same philosophy and objective as adopted by the conventional banks (Haron and Nursufiza Wan Azmi, 2008; Devi, Hooper, and Davey, 2008). Islam prescribes a broad accountability framework in all aspects of life comprising conduct in managing a business and this significantly has an impact on accounting practices (Baydoun and Willett, 2000; Gambling, Jones, and Karim, 1993).

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Furthermore, the essential feature of Islamic banking is interest-free or forbid any charges of interest but it does not mean that capital is costless in an Islamic system (Ariff, 1988). The prohibition of *riba* (usury or interest), in the Holy Quran has been repeatedly condemned and prohibited (Chong and Liu, 2009; Olson and Zoubi, 2008; Rammal, 2006; Grais and Pellegrini, 2006; Lewis, 2001; Hamid et al., 1993; Karim, 1990) and the application of trading and commerce are the cornerstones of Islamic accounting, banking, finance and so forth. Thus, all Islamic banks are required under the Islamic Banking Act (IBA) 1983 to establish a Shariah body known as Shariah Supervisory Board (SSB) being one of the most important governance mechanisms to ensure compliance with Shariah rulings (Karim, 1995).

The main objective of setting up Islamic Financial Institution (IFI) is to practice activities that complied with Shariah principles in the field of economics, dealings, and transactions for communities. Initially, many countries have put in place laws and regulations for IFI and international bodies such as the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), the Islamic Financial Standard Board (IFSB), the International Islamic Rating Agency (IIRA), the International Islamic Financial Market (IIFM), and the Liquidity Management Center (LMC) to establish an adaptable standards of conventional financial services in order to promote harmonisation in the application of Shariah and the creation of standards (Hassan and Lewis, 2007).

Specifically, the objectives of the study mainly to examine IFI interpretation and evaluate if it is in accordance with Shariah principles, secondly to position the epistemological conception of accountability amongst SSB members in the IFI and thirdly to examine the association between the level of competency and accountability of SSB. This study is expected to provide a significant contribution to the IFI in providing full range of knowledge and skills to determine the problems or issues pertaining to the concept of accountability among SSB. Results of the study could be used to improve existing services and formulate strategic decisions in order to achieve competitive advantage, designing and implementing suitable remedial measures and adopted as guidelines for future references and evaluation and useful for Malaysian educational institutions especially in Islamic accounting field.

The remainder of the paper is structured as follows. The next section provides a literature review related to the study. This is followed by discussion on the methodology adopted in the study. Subsequent section introduces Bank Muamalat Malaysia Berhad (BMMB) as the primary subject of the study. Next it will elucidate the outcome of the result, analysis and discussion based on findings delivered from the descriptive analysis. The paper ends with limitation and suggestions for better future research.

## **1.0 Literature Review:**

### **1.1 Institutionalised Structure Of Islamic Supervisory Committees:**

In Malaysia, The Central Bank of Malaysia (CBM) Act 1958 is the main act that regulates the setting up of the Shariah Advisory Council (SAC) which plays the role of a Shariah custodian. The compliance with Shariah principles is an integral feature in the Islamic banking and finance (Olson and Zoubi, 2008). As mentioned earlier by Grais and Pellegrini (2006) and Karim (1990), in Islamic banks or IFIs, there are in-house religious advisers known as the SSB. The definition of the SSB according to AAOIFI Governance Standard for Islamic Financial Institutions (GSIFI) No. 1 is stated as follows: "An independent body of specialised jurists in *fiqh al-muamalat* (Islamic commercial jurisprudence) However, the SSB may include a member other than those specialised in *fiqh al-muamalat*, but who should be an expert in the field of IFI and with knowledge of *fiqh al-muamalat*. The SSB is entrusted with the duty of directing, reviewing, and supervising the activities of the IFIs in order to ensure that they are in compliance with the Islamic Shariah Rules and Principles. The *fatwa* and rulings of the SSB shall be binding on that IFI."

### **1.2 Shariah Supervisory Board Functions And Responsibilities:**

As mentioned by Rammal (2006), and Banaga, Ray, and Tomkins, (1994), the functions of SSB can be described as follows: answering the enquiries that come from the community at large; issuing formal legal opinions according to the Islamic law and enquiries submitted by bank management or any other interested party; reviewing and revising all the dealings and transactions between the bank and client so as to ensure it will be in line with Shariah. If any deals or transactions contradict or against the Shariah principles, such transactions will not be approved or prohibited to proceed further. Reviewing on any particular subject and issuing their opinion; holding regular meetings to discuss all enquiries received and record the minutes of each meetings; receiving enquiries from the management or others and presenting them to the board of directors, preparing draft opinions and delivering them to those who are concerned. In addition, SSB also responsible to finalise and issue written opinions once the Board have satisfied and no need for any second opinion. Besides that, the SSB members prepare contracts and other relevant documentation in cooperation with the bank legal advisor. They also participate in the preparation of the draft decree, decisions and directions set by the bank, and provide additional clarification notes as well as to ensure the banks and their branches are implemented with the Shariah controls.

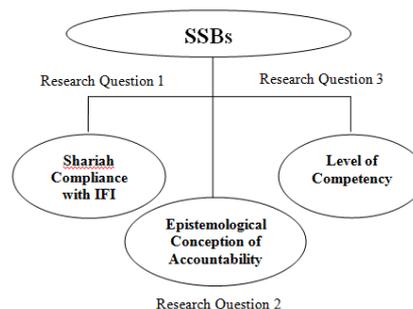
The Guideline on the Governance of SC by CBM, 2005 (BNM/RH/GL/005-6) has outlines the main duties and responsibilities of the SSB such as to advise the BOD on Shariah matters relating to business operation to ensure that the business operations of the IFI comply with Shariah principles at all times. The SC has to endorse Shariah Compliance Manuals and the IFI should have a Shariah Compliance Manuals which this manual operated as guideline that specify the manner in which a submission or request for advice be made to the SC, the conduct of the SC's meeting and the manner of compliance with any Shariah decision. In addition, the SAC is established by CBM to streamline and harmonise the Shariah interpretations among banks (Chong and Liu, 2009).

### 1.3 Accountability In Auditing:

Auditing is a discipline born from the need to measure those factors in business that determines success or failure (Cornwell, 1995). The Companies Act 1965 stressed the need for the auditor to be independent and was given broad powers to inspect records and to obtain information for audit, as well as to have the right to attend and address the general meeting of the company, however it was silent on the academic and professional qualifications of the auditor. Karim (1990) mentioned in a previous study that one of the distinctive features of Islamic banks is the religious audit conducted by in-house adviser whose task is very similar to those external auditors. Religious auditors of the Islamic bank are very much influenced by moral values compared to external auditors who are largely affected by economic factors. They are also an employee and responsible to report to the shareholders of the bank in order to strengthen their independence.

### 1.4 Conceptual Framework:

In order to gain knowledge, researcher has to go to the field listening to the discourse of the actors of an organisation and seeing their everyday life (Geertz, 1988). The researcher gathers the information and includes it in the conceptual framework of the analysis on the accountability and competency amongst SSB members, as shown in the Figure 1 below. The foundation framework should not be seen as model to be-tested; rather, it is an initial pathway for the research then is used as the basis for explanation and enhanced accordingly (Davies, 1990).



**Fig. 1:** The Conceptual Framework for the Analysis on Accountability and SSB.

## 2.0 Research Methodology:

### 2.1 Ethnographic: Scope And Function:

According to Jonsson and Macintosh (1997), ethnographic research in general involves intensive, face-to-face participant observation in natural settings over long time periods and the aim is to produce a systematic narrative of the behaviour culture, organisation, profession, or community of some sort including their perceptions, discursive practices, and interrelationships with each other. Ethnography design is a set of data collection and analysis perspectives, assumptions and skills that can be used to understand a particular environment or domain of people for the express purpose of designing new technology products (Cooper and Schindler, 2008, p.164).

### 2.2 Reason For Choosing Ethnography:

There are few significant reasons to choose ethnography in doing the thesis as it directly involves negotiating and conducting relationships through the various processes of gaining initial permission and gaining access until the completion of a final report (Irvine and Gaffikin, 2006). Hence, the researcher observes and has direct interactions with the people in the organisation and systematically, records the words and behaviours of the research subjects (Cooper and Schindler, 2008; Stone, 1978).

In collecting data, one of the most ordinary ways in ethnographic research is a direct, daily observation of own participation which may include participating observation. Most of the methods in ethnography involve

studying people within their own cultural environment through intensive fieldwork; they emphasise the subjects' frames of reference and understandings of the world (Cooper and Schindler, 2008).

### **2.3 Researcher As Research Instrument:**

The background of the researcher's level of educations and years of experiences provide appropriate and suitable theoretical as well as practical competences to deal with the problems and relevant aspects of the study.

### **2.4 In Gaining Initial Permission:**

In this study, the researcher concentrates on the concept of accountability among religious auditors of the IFI. Data are collected at BMMB Head Office through observation, survey and interview for a period of two months. The reason for choosing BMMB as an experimental subject is that it is one of the largest and a well-established Islamic bank and financial institution.

### **2.5 In Gaining Access:**

In order to gain access, the researcher has to submit an authorised letter issued by the university to officially conduct the research at the bank and subsequently been allowed to do the same for two months.

### **2.6 Writing The Ethnographic: Data Capturing:**

Several types of data were gathered over a period of two months. The data gathered from interviews, archival records, field notes, direct observations and a study of documents will form the reservoir of materials. According to Gioia and Chittipeddi (1991) the interviews were designed to let the informants engage in a stream of consciousness, and to provide rich, descriptive data on the perceptions about the change process and their efforts to manage it. According to Kornberger, Justesen and Mouritsen (2011) the research interest in practices of managing and the identity of the managers are significant to focus on the concrete and lived reality of the organisational members.

## **3.0 Case Study: BMMB:**

### **3.1 Background Of The Company:**

In 1st October 1999, a second Islamic bank, namely BMMB, commenced its operations. The establishment of BMMB was the effect of the spin-off following the merger of BBMB, BOC, and BBMB Kewangan.

### **3.2 CORPORATE IDENTITY**

The BMMB logo and identity were formed with a dynamic line in a continuous motion. The single line links the five domes that signify efficiency, clear and focused vision, as well as reflection of the strong relationship between the Bank, customers, and its external environment. An hour glass embedded in the centre within the logo design stands for time.

### **3.3 Corporate Governance And Accountability:**

Bank corporate responsibility means optimising the impacts of their financial business on employees, communities, and the environment in which they operate, as well as the society at large. As a corporate entity, BMMB has acknowledged that the ability to develop and to grow into a sustainable business is highly dependent on the concerted efforts that undertake in elevating relationships with customers, employees, suppliers, shareholders, regulators, as well as the community. According to Abu-Tapanjeh (2009), good corporate governance has long been considered as a crucial role for stakeholders in the business environment.

### **3.4 Structure Of Accountability:**

#### **3.4.1 Board Of Directors:**

The Board comprised of ten (10) members; one (1) CEO/ Executive Director and nine (9) Non-Executive Directors, of which five (5) are Independent and four (4) are Non-Independent. The Non-Independent Non-Executive Directors are the representatives of the shareholders, namely DRB-HICOM Berhad and Khazanah Nasional Berhad.

#### **3.4.2 Board Committees:**

The Board has established several Board Committees, whose compositions and terms of reference are in accordance with the Revised BNM/GP1-I, as well as the best practices prescribed by MCCG 2012.

#### **3.4.3 Internal Audit And Control Activities:**

Based on the 2014 annual report, the Committee affirmed that it is responsible to ensure that the Bank's systems of internal control is adequate and effective to manage the risk profile within the Bank's risk appetite

and recognises the need for, and the value of, a sound system of internal control Bank-wide. The Committee is supported by the Internal Audit Department (IAD) which assists the Committee by providing reasonable assurance and value-added service on adequacy, integrity, and effectiveness of the system for internal control and financial reporting, plus compliance with internal policies, procedures, as well as externally applicable rules and regulations.

#### 3.4.4 Shariah Committee:

In BMMB, the SC was established in accordance with the requirements of the IBA in 1983, and the Bank's Articles of Association, which prescribed the setting up of a Shariah body to ensure that the conduct of the Bank in its affairs is in accordance with the Shariah principles.

#### 3.4.5 Remuneration Of Directors And Shariah Committee Members:

BMMB has a Remuneration Committee that provides a remuneration policy for Directors, CEO, and key senior management officers, besides ensuring that the Bank's compensation package is competitive and consistent with its culture, objectives, and strategies (annual report, 2014).

The SC of BMMB has both supervisory and consultative functions, since the Shariah scholars on the religious board carry great responsibility; it is important that only high level scholars are appointed to such board. The board also should consist of trustworthy scholars who are highly qualified to issue fatwa on financial transactions. In addition, they must have considerable experience with knowledge of modern dealings and transactions.

#### 3.5 Products Of Accountability:

All Islamic products based on the types offered by BMMB must be approved by the SC. Each product type should have its own product sub-type that is categorised based on Islamic concept. As a service-oriented business, the image of BMMB is a central factor in the effort to differentiate itself from its competitors. Generally, the way the products or the services are served is made available to customers to help in creating the BMMB image in the minds of the customers. This image should be reflected in the customers' perceptions and feelings about the products or services offered. Hence, BMMB is aware about being innovative in terms of their products and services, as only through innovation in products and services they can sustain their competitive advantage against other competitors.

#### 4.0 Data Analysis And Discussions:

##### 4.1 Analysis And Discussion Of Findings:

When the researcher first arrived at the BMMB Shariah Department, the researcher adopted Geertz's (1988) interpretation on ethnographic research as to search for symbolic forms, such as words, images, institutions, and behaviours. The study was conducted in the Shariah Department of BMMB Head Office at Level 20, Menara Bumiputra, Jalan Melaka, Kuala Lumpur for the period of two months. The three key objectives had been set up in order to address the research questions. As a consequence of these objectives, the researcher adopted a deliberately constrained view of the data to be collected from the outset.

##### 4.1.1 Shariah Compliance With Ifi Interpretation:

In this study, it identified the interpretation of accountability among SSB members in terms of their responsibility and competence in assisting IFI to adhere to the Islamic concept, as well as to ensure all its financial transactions, including all aspects and its operations are in accordance with the Shariah principles. Based on the discussion, it had been agreed that all banking businesses of the IFI, namely business operation; manual, policies, and guidelines; concept and structure of products and services; documentations; advice sought by external; advice on matters to be referred to SAC of CBM; written opinions; and reference for advice, were solely complied under Section 2 IBA 1983 as 'banking business whose aims and operations do not involve any element, which is not approved by the Religion of Islam'.

According to Haron and Nursofiza Wan Azmi, (2008), all principles of Shariah are expected not only to have a significant impact on the decision-making process of Muslim, but also to have an influence on their perceptions towards Islamic banks. Table 1 below shows the Shariah Compliance with IFI interpretation.

**Table 1:** Shariah Compliance with IFI Interpretation.

Shariah Compliance with IFI Interpretation	Accountability in IFI
Draft, approve, update, and improve	In collaboration with other concerned departments and officials, model contracts and agreements to govern and regulate all the IFI activities and dealings to conform to Shariah principles, rules, and spirit.
Study and decide	From the Shariah's point of view, any issue or problem submitted by the BOD.
Offer advice and instructions	Especially to the management of the IFI as SSB has been entrusted with the authority to inspect IFI operations, examine the necessary documents, and summon any official of the IFI.
Present, whenever necessary to the BOD	Reports to the General Manager or BOD conveying the SSB's views and observations on the IFI activities. Submit to the general meeting of shareholders an annual report containing among other things, the opinions from the SSB on the compliance of the IFI operations with Shariah precepts.

#### 4.1.2 Epistemological Conception Of Accountability

The conceptual framework of the analysis on the accountability and the SSB members is used as the basis for explanation and improved accordingly. The accountability conception identified as subjection, transparency, independence, confidentiality, faith and justice, as well as competency matters. In addressing accountability in BMMB, all the SSB members dealt with both self and statutory regulations. As for self-regulation, SSB played an important role in creating the awareness among the stakeholders. With regard to statutory regulation, the SSB members must be knowledgeable in the Arabic language to interpret the Holy Quran and Hadith correctly. The decision to have a banking relationship with Islamic banks is not because of profit motive, but rather to gain blessings of Allah (Haron and Nursofiza Wan Azmi, 2008). Table 2 indicates the summary of findings pertaining to the epistemological conception of accountability.

**Table 2:** The Summary of Findings on Epistemological Conception of Accountability.

	Epistemological Conception of Accountability	Findings
1	<p style="text-align: center;">Subjection  <i>(the condition of becoming subject who might be able to give an account)</i></p>	The SSB of BMMB is accountable to accomplish their jobs as they are competent means that they are experts in Islamic jurisprudence and Islamic commercial law. They also have background in accounting, banking, finance, economics, business or law. Furthermore, there should be a requirement for practical experience and exposure for at least three years at giving Shariah rulings. These requirements enable the establishment of a higher standard of practice for Shariah supervision in IFI.
2	<p style="text-align: center;">Transparency  <i>(seeing behind or within the corporate entity)</i></p>	The SSB of BMMB is accountable to accomplish their jobs as they are competent means that they are responsible to provide true, as well as fair view disclosure and transparency. The essential concept of Islamic accountability is that all resources are made obtainable to individuals in terms of trust.
3	<p style="text-align: center;">Independence  <i>(unbiased when submitting opinions)</i></p>	The SSB of BMMB is accountable to accomplish their jobs as they are competent means that they take unbiased viewpoint in the performance of their assignment. Independence is divided into two; independence of mind and independence in appearance. They are responsible for the endorsement of Shariah policies and procedures, and at the same time, to conduct Shariah review and audit the overall operations and services that are compliant to Shariah.
4	<p style="text-align: center;">Confidentiality  <i>(keeping information secret from unauthorised parties)</i></p>	The SSB of BMMB is accountable to accomplish their jobs as they are competent means that Shariah scholars are only allowed to sit as a member of the SSB in one IFI at the same time. This state of affair implies a risk of conflict of interests if they sit on a number of IFIs. In addition, there is the issue of confidentiality of information when a Shariah scholar serves more than one IFI.
5	<p style="text-align: center;">Faith  <i>(human are given free choices, but they are also responsible and accountable for their choices, either they can choose to believe and obey God's orders or reject faith)</i></p>	The SSB of BMMB is accountable to accomplish their jobs as they are competent means that they have the mandate as a trustee of Allah in all situations. They have to maintain and strengthen good relationship with others, namely management, superiors, subordinates, and clients, in conforming to the divine norms and rules. Their decision making does not only comply in the hands of superior officials, but also extends to the responsibility to fulfil obligations beyond stakeholders.
6	<p style="text-align: center;">Justice  <i>(particularly important when in a position of authority because making judgement will affect many people)</i></p>	The SSB of BMMB is accountable to accomplish their jobs as they are competent means that they are responsible to conduct justice that involves aspects of fairness and just system.

#### 4.1.3 SSBS' Level Of Competency:

The SSB competency can be categorised into execution and self-determining. Execution is implementation of the competency of SSB, and it can be classified as leisure, quick, perceive or fair, whereas self-determining is classified as strong, medium or weak for the actions taken by the SSB members.

Furthermore, based on the respondents, they viewed this as basic needs in oneself as a human, whereby usually, the built system is sometimes good, but the problem is the man himself. Hence, the Muslims must be responsible in front of Allah, and not only show accountability in front of their clients only. All levels of a company or bank should play the role in creating self-accountability among their staff and should be practiced equally. Self-accountability is a must in everyone because this is to ensure that the staffs has a sense of responsibility to perform their duties assigned correctly without making any mistake and the duty done in an ethical way, and in this case, it must be according to the Islamic principles.

Nonetheless, when it comes to accountability, most of the staff depends on the accountability of leadership. Good leadership will eventually create and form self-accountability among their employees. For some respondents, accountability is not owned by all individuals and it depends on the individual how they interpret accountability. The staff who ignore and do not stress on the importance of self-accountability will lead to poor corporate performance. In fact, some staffs who attend talks given by Islamic preachers are also involved in Islamic banking. This clearly gives better picture for newbie's in this industry to understand the concept of Islamic banking. Thus, one must fully understand the differences between Islamic banking and other commercial banking.

#### Limitations:

There are two common limitations in this study, first is the general limitation about the ethnography study, while the second is about the specific limitation. The criticism in ethnography study is that it leads to in-depth knowledge only of a particular context and situation (Harvey and Myers, 1995). Ethnographic study was used at both the data collection and the data analysis stages of this study. This research had been a qualitative study, so, the ethnography method was one of the suitable methods employed in collecting and analysing the data.

The second limitation and this limitation is also one of the specifics of the study, which is time constraint. According to Harvey and Myers (1995), the process of ethnography can be overwhelming for new researchers. Time management is much needed and planning is one of the best methods here. There is no term of fixed framework, especially for new researches, because in this kind of research, fixed framework and fixed type of questions are not reliable. The data are not predictable because they tend to be different from one member to another, even though the questionnaire is similar.

### **Suggestions:**

This study looked into the conception of accountability of SSB in IFI, as well as the relationship between the accountability of SSB members and competence with the Shariah based principles. Nevertheless, some suggestions are offered for the purpose of improvisation and in gaining new knowledge. In addition, it could be useful to the authorities in designing and implementing suitable remedial measures, especially for AAOIFI. Furthermore, the findings of this research could also be used as a guideline for future references and evaluation by the organisations. At the same time, the findings of this research could be useful to the Malaysian educational institutions in curriculum development of Islamic accounting.

### **Conclusion:**

From this study, the assessments of the Malaysian IFI model, especially the accountability and the competency of the SSB, were suffused with ambivalence. The spirit of accountability had become more critical and had embraced avant-garde innovations. The existence of the SSB is to ensure that the financial institutions operate in conformity with the Shariah. They are hired by the IFI and act as an internal control body for the organisation. Primarily, this enhances the credibility of the institution in the eye of its customers and bolsters their Islamic credentials.

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