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# 2016

Pengkongsian Ilmu Dari Perspektif Islam

30 November 2016 | Rabu  
UiTM Cawangan Pahang  
Kampus Jengka



## The Development of Islamic Corporate Social Responsibility (*I-CSR*) Disclosure Index

Azlan Md. Thani<sup>1\*</sup>, Mohd. Azmi Nias Ahmad<sup>2</sup>, Mohd. Aripin Amat<sup>3</sup>, Azizi Hashim<sup>4</sup>

<sup>1-4</sup>Faculty of Accountancy, Universiti Teknologi MARA Pahang,  
Kampus Jengka, 26400 Bandar Tun Abdul Razak Jengka, Pahang, Malaysia.  
annasibn\_malik@pahang.uitm.edu.my, azminias@gmail.com, aripin@pahang.uitm.edu.my,  
azizih@pahang.uitm.edu.my  
\*Corresponding Author

**Abstract:** This paper attempts to discuss the importance need to extend the corporate social reporting with Islamic values, ethics and principles to ensure that the shariah-approved companies (SACs) are act accordance to *shariah* law. Consequently it will help the relevant stakeholders to evaluate the level of accountability and transparency of SACs from the eyes of Islamic perspectives. As Malaysia is targeting to become international hub for Islamic finance and halal industry, the inclusion of Islamic values in the report of SACs in Malaysia need to be improvised.

**Keywords:** Islamic Corporate Social Responsibility, *Shariah*-Approved Companies

### 1. Introduction

Corporate Social Responsibility (CSR) for Muslims assumes a broader and more holistic significance. The concept of CSR in Islam encompasses a broader meaning embracing taqwa dimension (God-consciousness) by which corporations as groups of individuals, assume the roles and responsibilities as servants and vicegerents in all situations (Dusuki, 2008). Therefore, every Muslims must act in accordance to please Allah and responsible to control themselves as well as managing the resources as a trust. Since the emerging market of products from Islamic banking such as *murabahah*, *mudharabah* and many more, many studies has been focusing on it. The disclosure of Corporate Social Responsibility (CSR) with elements of Islamic values has been the central point of research also since Islamic banks carry the full fledge image of Islam. In fact, Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) has come up with the draft on CSR Conduct and Disclosure for Islamic Financial Institution. However, there is lack of study focusing on Islamic Corporate Social Responsibility (*i-CSR*) for the non-financial institution or classified as shariah-approved companies (SACs) especially in Malaysia (Othman and Md. Thani (2010), Ousama and Fatima (2006), Muhammad (2006), Mohamed, Alwi and Muhammad Jamil (2010), Bala (2012), and Ibrahim, Marshall and Abdul Rahman (2013).

The findings from Abdul Rahman (2007), Mohamed et al. (2010), Othman et al. (2010) and Ibrahim et al. (2013) showed that lack of Islamic information provided to the users through the annual report and web report. The growing awareness and demand for investing in accordance to Islamic principles on a global scale has created a flourishing Islamic Capital Market (ICM). In 2009, Malaysia had recorded the largest share of the global ICM estimated between 60%-70%. However, the majority of the ICM comes from domestic investors (The Edge, 2009) which show that Malaysia still unable to attract foreign investors especially from Gulf Cooperation Council (GCC) *shariah*-approved portfolio investors to actively involved in our local ICM. This is quite a great loss of opportunity if Malaysia wishes to become international Islamic financial hub. One of the reasons is due to misconception that Malaysia's ICM index screening criteria is more lenient than other ICMs in the world. Whereby, international investors prefer investments with strict *shariah*-compliant guidelines. For that case, initiative and innovation have to be formulated in order to turn up the misconception. This can be done by strengthen the image and charismatic of the SACs in Malaysia by disclosing extension of the financial reporting with the inclusion of Islamic values and activities in their

report strategically. Therefore, there is demand for research to study on this area perhaps it will help to boost the local ICM.

## 2. Research Objective

Disclosure is a crucial aspect of the accountability function of SACs to its stakeholders. From an Islamic perspective, the main objective of corporate reporting that overrides other objectives is to allow Islamic enterprises to show their compliance with *shariah* (Baydoun and Willet, 1997). According to Maali et al. (2006), social responsibility disclosure by Islamic businesses can be categorized into three broad objectives as follows:

1. To show compliance with Islamic principles and laws, in particular dealing justly with different parties;
2. To show how the operations of the businesses have affected the well-being of the Islamic community;
3. To help Muslims to perform their religious duties.

Therefore, the objective of this paper is to discuss the development process of ICSR reporting index before the index is to be validated by experts from various fields for reproducibility and reliability.

## 3. Islam and CSR

Islamic CSR offers a holistic spiritual view based on the teaching of *Quran* and *Sunnah* describing better principles by the *shariah* philosophical framework for man's interaction with nature as well as his fellowmen (Ahmad, 2002). In fact, the moral and ethical principle derived from divine revelations are more enduring, eternal and absolute (Ahmad, 2002; Ahmad 2003), thus may serve as better guidelines for corporations when exercising their business and social responsibilities simultaneously. Therefore, a religious bond under *shariah* framework assumes more vital role than the conventional CSR theories such as social contract. The religious bond requires man to submit to the *shariah* by committing himself to the contractual obligation and leading life in accordance with high virtue and moral consciousness as stipulated (Dusuki, 2008). CSR in Islam stems from the concept of brotherhood and social justice (Naqvi, 1981). The practice of social justice will prevent Muslims from doing harm (Yusoff, 2002). Allah SWT reveals:

*“Allah commands justice, the doing of good and liberality to kith and kin, and He forbids all shameful deeds, and injustice and rebellion...”*

(An-Nahl 16:90)

The commitment of Islam to justice and brotherhood demands Muslim society to take care of basic need of the poor (Naqvi, 1981). This can be fulfilling through zakat, donation, charity, prohibition of *riba* (usury), encouraging of *al-qard al-hassan* (free-interest loan) and *waqf* which are highly encouraged in Islam. The Prophet Muhammad SAW says:

*“A Muslim is a brother of another Muslim; he neither wrongs him, nor leaves him without help, nor humiliates him.”*

(Muslim)

The main aim of an Islamic economy is to allow people to earn their living in a fair method and profitable way without exploitation of others, so that the whole society may benefit (Lewis, 2001). Islam accepts disparity of wealth within reasonable limit but not accept too many gaps until the poorer and needy living in misery and hunger.

Meanwhile, the concept of *Khilafah* (vicegerency) defines a person's responsibility to both community and himself or herself. As *Khilafah* the individual is regarded as the trustee for God resources. This presumes to influence the way of conducting business as well in Muslim society and Islamic businesses are therefore expected to report on their fulfilment of such responsibility (Aribi et al., 2012).

The business in Islam also part of *tawhidic* paradigm for the Muslims. Islam is a *shumul* religion which encompasses all aspect of life guided through Divine resources namely *Al-Quran* and *As-Sunnah*. Under the concept of *tawhid*, man has to maintain a good relationship not only to Allah SWT (*hablun min Allah*), but also with human being (*hablun min al-nas*) and its environment. Mukhazir (2006) has further discussed these three different relationships namely (i) man and Allah, (ii) man and human beings and, (iii) man and environment in more details. The relationship to Allah is strongly built from the essence of the six pillars of faith and five pillars of Islam. This relationship must free from any intermediaries as stated in the Quran:

“He knows what is in the heavens and on earth; and He knows what ye conceal and what ye reveal; yea Allah knows well the (secrets) of (all) hearts.”

(At-Taghabun 64:4)

Muslim must aware that Allah SWT is always watching us at all time to ensure that they are practicing in every action according to *shariah*. Therefore, the corporation especially *shariah*-approved companies must prove that their business activities are following the *shariah* or *muamalah*. Meanwhile, man's relationship with other fellow human beings should be inspired by the values of trust, truthfulness, firmness, fairness, respect of law, kindness, tolerance and other good deeds (*amal soleh*). With the concept of *dakwah* in Islam '*amal makruf nahi anil munkar*' is to call people for good deeds and forbidding people from bad deeds. In the business operation, leaders must respect the right (*haq*) of all parties or stakeholders to be given fair treatment while achieving the target of profit maximizing in order to attain the concept of *al-falah* (success) and *barakah* in Islam. Everything in this world is created by Allah SWT for its specific function and use. Everything in the world is valuable and as a trust by Allah for the people to use it in the right manner and protecting it from any harm. Therefore, the protection of environment as well as utilization of natural resources for business purposes should be socially responsible.

The above examples quoted from the so-called Divine contract between man and his Master is in fact a real contract, not a fictitious or presumed one like the social contract (Osman, 2001 as cited in Dusuki, 2008). The philosophical foundation in Islam will unite people to cooperate each other to please Allah rather than to condemn each other. A person's relationship with God should, by right, determine the mode of relationship with fellow servants of God and not vice versa (Ahmad, 2003; Hassan, 2002). Therefore, it will influence the behavior of the person's daily interactions and transactions that will highly inspired by the values of truthfulness, firmness, fairness, respect for the law, kindness, forbearance, tolerance and uprightness instead of all the bad deeds (Hassan, 2002). This should naturally be manifested in the individuals' business activities and operations as well as their relationships with all their respective stakeholders. The invocation of *shariah* and the reflection of *taqwa*-paradigm in business imply that the entrepreneur is no longer driven only by the principle of profit maximization, but also by the pursuit of the ultimate happiness in this life and the Hereafter, besides discharging his social and moral responsibility for the well-being of his fellow-men such as consumers, employees, shareholders and local communities (Dusuki, 2008).

#### 4. Steps to Develop the ICSR Disclosure Index

According to Marston and Shrive (1991), to develop the disclosure index is not an easy task because the number of items that could be disclosed by a company is very large. Marston

and Shrivs (1991) also conclude that, the construction of disclosure indices inevitably involves subjective judgment; however, it has been proven to be a valuable research tool that will continue to be used as long as company disclosure is a focus of research. Since the pioneering work of Cert (cited in Barako, 2007), several different approaches have been adapted to measure disclosure quality and quantity, but there is no general theory that offers guidance on the selection of items to measure the extent of disclosure item. Disclosure, by its very nature, is an abstract construct that does not possess inherent characteristics by which one can determine its intensity or quality (Wallace and Naser, 1995).

An extensive review of prior studies was undertaken to develop a list of relevant ICSR that may be disclosed by a company. The main aim is to check for commonalities across the studies and to isolate those items that have been consistently identified as relevant and which may be disclosed by companies. For an item to be included, it must have been used in previous published study. However, only a few empirical studies were found on the development and use of disclosure index with ICSR specifications for non-financial institutions (Othman et al. (2010), Ousama and Fatima (2006), Muhammad (2006), Mohamed et al. (2010), Bala (2012), and Ibrahim et al. (2013). A majority of the studies were on Islamic financial institutions such as Haniffa and Hudaib (2004), Harahap (2003), Maali et al. (2006), Haniffa and Hudaib (2007), Paino et al. (2011), Arshad et al. (2012), Farook et al. (2011). It was also found that many conceptual studies are on the relevant ICSR suggested to be disclosed by a company but yet to be tested empirically. Therefore, all these sources are blended to get the best result for ICSR. For that matter, the following steps have been taken to form the basis for development of the disclosure index in this study:

**Step 1:** Adoption of the index from Haniffa and Hudaib (2007) as the main source and adding up from Othman et al. (2010), Ousama and Fatima (2006), Sulaiman (2005), Mohamed et al. (2010), Harahap (2003), Maali et al. (2006) and Haniffa (2002). The final construct of the index is described in Table 2 below.

**Step 2:** Reviewing the disclosure requirements (mandatory disclosure) of the Companies Act 1965, Financial Reporting Act 1997, Malaysian Accounting Standards Board, Financial Reporting Standards 2006 and Malaysian Code of Corporate Governance Revised 2007; and excluding them from the primary disclosure index developed in Step 1 above, and

**Step 3:** Validation of the index with the following experts from various fields:

1. Representative from *Shariah* Advisory Council of Bursa Malaysia
2. Representative from Supervisory Board from any company
3. Religious scholar with involvement in commercial industry
4. Religious scholar with no involvement in commercial industry
5. Representative from Bank Negara
6. Academician with conventional CSR background
7. Academician with Islamic CSR background
8. Representative from top management of industry
9. Financial analyst
10. Consultant firm on *shariah*-compliant investment portfolio

**Table 1.** Proposed ICSR disclosure index

	<b>THEME: Underlying philosophy and values</b>	Haniffa and Hudaib (2007)
<b>A</b>	<b>DIMENSION: Vision and Mission Statement</b>	Haniffa and Hudaib (2007)
	1. Commitments in operating within <i>Shariah</i> principles	Haniffa and Hudaib (2007) Haniffa and Hudaib (2007)
	2. Commitments in providing returns within <i>Shariah</i> principles	Haniffa and Hudaib (2007) Haniffa and Hudaib (2007)

	<ol style="list-style-type: none"> <li>3. Current directions in serving the needs of Muslim community</li> <li>4. Future directions in serving the needs of Muslim community</li> <li>5. Commitments to engage only in permissible investment activities</li> <li>6. Commitments to engage only in permissible financing activities (including policy on <i>riba</i> activities)</li> <li>7. Policy on any ambiguity/<i>gharar</i> activities</li> </ol>	<p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007), Harahap (2003), Haniffa (2002)</p> <p>Haniffa (2002), Maali et. al (2006)</p>
<b>B</b>	<p><b>DIMENSION: BOD and top management</b></p> <ol style="list-style-type: none"> <li>1. Religious status of board</li> <li>2. Board composition: Muslim vs non-muslim</li> <li>3. Ownership shareholding between Muslim and non-Muslim</li> </ol>	<p>Haniffa and Hudaib (2007)</p> <p>Othman et. al (2010)</p> <p>Othman et. al (2010)</p> <p>Sulaiman (2005)</p>
<b>C</b>	<p><b>DIMENSION: Product</b></p> <ol style="list-style-type: none"> <li>1. No involvement in non-permissible activities</li> <li>2. Involvement in non-permissible activities (if any)</li> <li>3. Reason for involvement in non-permissible activities</li> <li>4. <i>Halal</i> status of the product (if relevant)</li> </ol>	<p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Sulaiman (2005)</p>
	<b>THEME: Development and Social Goals</b>	Haniffa and Hudaib (2007)
<b>D</b>	<p><b>DIMENSION: Zakat, Charity (<i>saddaqa</i>) and Waqf</b></p> <ol style="list-style-type: none"> <li>1. Company liable for <i>zakat</i></li> <li>2. Amount paid for <i>zakat</i></li> <li>3. Sources of <i>zakat</i></li> <li>4. Uses/beneficiaries of <i>zakat</i></li> <li>5. Balance of <i>zakat</i> not distributed amount</li> <li>6. Reasons for balance of <i>zakat</i></li> <li>7. SSB attestation that sources and uses of <i>zakat</i> according to <i>shariah</i></li> <li>8. SSB attestation that <i>zakat</i> has been computed according to <i>shariah</i></li> <li>9. Sources of charity (<i>saddaqa</i>)</li> <li>10. Uses of charity (<i>saddaqa</i>)</li> <li>11. Sources of <i>waqf</i></li> <li>12. Uses/type of <i>waqf</i></li> </ol>	<p>Haniffa and Hudaib (2007), Haniffa (2002)</p> <p>Haniffa and Hudaib (2007), Mohammed et. al (2010)</p> <p>Haniffa and Hudaib (2007), Mohammed et. al /2010)</p> <p>Haniffa and Hudaib (2007), Mohammed et. al (2010)</p> <p>Haniffa and Hudaib (2007), Mohammed et. al (2010)</p> <p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007), Haniffa (2002), Sulaiman (2005)</p> <p>Haniffa and Hudaib (2007), Haniffa (2002), Sulaiman (2005)</p> <p>Haniffa (2002)</p> <p>Haniffa (2002)</p>
<b>E</b>	<p><b>DIMENSION: Employees</b></p> <ol style="list-style-type: none"> <li>1. Training on <i>Shariah</i> awareness</li> <li>2. Regular talk on Islam for employees' spiritual development</li> <li>3. Muslim employees are allowed to perform their obligatory prayers during specific times on their working days</li> <li>4. Muslim employees are allowed to perform fasting</li> </ol>	<p>Haniffa and Hudaib (2007)</p> <p>Haniffa and Hudaib (2007)</p> <p>Sulaiman (2005)</p> <p>Sulaiman (2005)</p>

	during Ramadhan 5. Proper place and appropriate time for 'solat' for Muslim employees 6. No restriction to cover the 'aurat' for Muslim 7. Employees benefit with regard to Islamic code and conduct such as sponsoring for <i>haji/umrah</i> , bonus for hari raya, breaking fasting during Ramadhan etc	
<b>F</b>	<b>DIMENSION: Debtors</b> 1. Debts policy/ 'qard al-hasan' 2. Amount of debts written off	Haniffa and Hudaib (2007), Maali et. al (2006), Ousama et. al (2006) Haniffa and Hudaib (2007)
<b>G</b>	<b>DIMENSION: Community</b> 1. Conferences on Islamic economics 2. Participating/sponsoring on any Islamic event such as Maulidur Rasul, etc	Haniffa and Hudaib (2007) Haniffa and Hudaib (2007)
	<b>THEME: Reviews by Shariah Supervisory Board (SSB)</b>	Haniffa and Hudaib (2007)
<b>H</b>	<b>DIMENSION: Shariah Supervisory Board (SSB)</b> 1. Names of members 2. Pictures of members 3. Remuneration of members 4. Report signed by all members 5. Numbers of meeting held 6. Examination of business compliance with <i>shariah</i> status as set by <i>Shariah</i> Advisory Council under Bursa Malaysia. 7. Profile of board members	Haniffa and Hudaib (2007) Haniffa and Hudaib (2007) Haniffa and Hudaib (2007) Haniffa and Hudaib (2007) Haniffa and Hudaib (2007), Mohammed et. al (2010) Haniffa and Hudaib (2007), Mohammed et. al (2010) Sulaiman (2005), Harahap (2003), Ousama et. al (2006)
<b>I</b>	<b>DIMENSION: Ethics and Values</b> 1. Islamic ethics being practice 2. Adherence to Islamic principles	Ibrahim et al. (2013)

Uniquely, this study is very straight focused on the very specific items on Islamic values and activities in the corporation. This is not to misunderstand because the existing conventional CSR also in parallel with the Islamic practices. The ICSR is an extension of current CSR practices with some emphasis on Islamic values.

## 5. Research Methodology

### 5.1 Content Analysis

For this study, the use of disclosure index has been chosen to retrieve the required information. Disclosure index studies assume that the amount of disclosure (the quantity) on specified topics proxies for the quality of disclosure. Researchers tend to assume quantity and quality are positively related (Botosan, 1997). Marston and Shrives (1991) provide an excellent review of the use of disclosure indices in accounting research, particularly in company annual report and accounts. They also emphasize that the index score can give a measure of the extent of disclosure but not necessarily the quality of disclosure. Scoring can take several forms, most commonly either a nominal score to indicate the absence/presence of the item or an ordinal level score to capture the degree of specificity of the item. In this study, nominal score is used to record the absence (represented by "0") and presence (represented by "1") of an item which is called unweighted approach.

## 5.2 Scoring

Consequently, the measurement of the extent of disclosure items is calculated as follows:

$$TS_j = AS_j / MS_j$$

Where total disclosure score (TS) of a company is equal to actual disclosure score (AS) divided by maximum disclosure score (MS).

## 6. Description of Corporate Social Responsibility Continuum

Finally, from the total disclosure score (TS) of the selected company, the level of disclosure of SACs can be classified as follows:

**Table 2.** Level and description level of CSR disclosure of companies.

Level	Description
Level 1: Irresponsible	This is an extreme situation depicting a firm's behaviour, which is irresponsible and even breaches the minimum moral standards required by law. Such actions vary from fraud, misrepresenting accounting statements, false advertising, dumping toxic waste in residential areas, violating employees' protection laws and rights such as health, safety, pay, work hours etc., to damaging environment and abusing other human rights. Many recent scandals and fiascos illustrate this point well, e.g. Enron, WorldCom, Xerox Corp., Arthur Anderson etc.
Level 2: Minimalist	Firms in this category are complying with the minimum requirement of legislation i.e. discharging its legal responsibility and playing by the 'rules of the game'. Beyond the legal compliance, they engage in few or no activities that might be labelled voluntary CSR or more specifically those activities, which are considered altruistic or philanthropic. The only primary objective of such companies is to maximize profits or shareholders' wealth.
Level 3: Apathetic	Companies at this level operate within the ambit of the law, at the same time are committed to the mandatory ethical responsibilities i.e. conduct business morally, doing what is right, just and fair, and avoiding harm. Their participation in other social responsibility activities like being altruistic and philanthropic is usually minimal, piecemeal, and with mixed motives. In some cases the motive may be profit-oriented such as adding employees benefits to attract and retain highly skilled employees; in other cases, it may be personal, such as contributing to an owner's favourite charity. Hence, we could label such behaviour as apathetic or indifferent in the sense that there is no strategic effort on the part of the firm to engage in the CSR activities.
Level 4: Tactical	Companies in this category fulfil their social responsibilities, including the philanthropic or altruistic responsibilities such as making voluntary contributions to society, giving time and money to good works, which they perceive can give benefits to the firm in the long run, through positive publicity and goodwill, hence enhancing the companies' reputation and eventually securing long-

	term profits.
Level 5: Taqwa-centric	Companies at this level manifest their social responsibilities based on the belief that a company should be socially responsible regardless of the financial consequences, positive or negative. This belief is enshrined in the Islamic worldview, guided by Shari'ah. Their commitment to societies is the manifestation of the taqwa-paradigm or God-consciousness, which also reflects their comprehension of the Islamic principles such as vicegerency or trusteeship and justice. This is the highest order moral position representing the Islamic view of CSR.

Source: Adopted from Dusuki (2008)

## 7. Conclusion

It is a high time for the Malaysia to have their own standard on ICSR disclosure guideline for SACs to portray their image that following the *shariah* in order to attract more foreign *shariah*-compliant investors to invest in our local ICM.

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