
COMPARATIVE EVALUATION OF SOCIAL RESPONSIBILITY DISCLOSURE AND FINANCIAL PERFORMANCE IN ISLAMIC BANKING

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Abstract:

THE SOCIAL RESPONSIBILITY OF ORGANIZATIONS IS RELATED TO ISLAM'S EMPHASIS ON ISLAMIC VALUES SUCH AS SOCIAL JUSTICE AND LIFE BALANCE, BY WHICH THE BASIC REQUIREMENTS FOR HUMAN LIFE ARE PROVIDED. ACCORDING TO JURISPRUDENCE AND SHARIAH (ISLAMIC LAW) TEXTS, ISLAM'S MAIN GOAL OF SOCIO-ECONOMIC JUSTICE IS TO ESTABLISH FAIRNESS IN SOCIETY, SO IT IS SAID THAT IN ISLAM THERE IS NO DISCRIMINATION BETWEEN MEMBERS OF SOCIETY, AND JUSTICE AND SECURITY FOR THE LIVES OF MEMBERS OF SOCIETY, THEIR PROPERTY AND WEALTH MUST ALWAYS BE ESTABLISHED. BE SOCIAL JUSTICE PLAYS A VITAL



ROLE IN THE DEVELOPMENT OF SOCIETY, BUT IT SHOULD BE SEEN WHETHER THESE PROMISES HAVE BEEN FULFILLED OR IGNORED. IN THIS REGARD, IN THIS ARTICLE, FIRST, THE LEVEL OF SOCIAL-ISLAMIC RESPONSIBILITY OF BANKS IN IRAN IS EXAMINED COMPARED TO WHAT IS EXPECTED AT THE INTERNATIONAL LEVEL, AND THEN, USING THE METHOD OF VARIANCE ANALYSIS, THE RELATIONSHIP BETWEEN THE LEVEL OF DISCLOSURE OF SOCIAL-ISLAMIC RESPONSIBILITY AND FINANCIAL PERFORMANCE BANKS ARE STUDIED. THE RESULTS SHOWED THAT THE BANKS IN IRAN DO NOT ADEQUATELY FULFILL THEIR SOCIAL-ISLAMIC RESPONSIBILITIES, AND THE FULFILLMENT OF THESE RESPONSIBILITIES DOES NOT AFFECT THEIR FINANCIAL PERFORMANCE.

Keywords: ISLAMIC BANKING, FINANCIAL PERFORMANCE, SOCIAL RESPONSIBILITY, COMPARATIVE EVALUATION, SOCIAL RESPONSIBILITY DISCLOSURE

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I. Introduction

At present, Islamic banks are considered one of the most important and reliable financial institutions in attracting Muslim deposits, which by solving the concerns of Muslims to invest their resources and relying on methods based on Islam, a large part of the financial circulation of Muslim societies and even western societies (Haseeb, 2018). The scope of activities of Islamic financial institutions is increasingly expanding with features such as the prohibition of interest, participation in profits and losses, and avoiding committing haram in activities. Prohibition of interest does not mean that Islamic banks will not seek profitability, but bank managers should provide a reasonable profit for depositors and shareholders with their honest efforts, while observing the principles of Islam in transactions (Sihotang, M. K., & Hasanah, 2021). For the first time, Haniffa, R., Hudaib (2007) showed that Islamic banks have a "moral identity" and this will lead to their greater social responsibility than conventional banks (which only focus on profitability). Compliance and disclosure of these responsibilities have positive effects on the society and improve relations with stakeholders, improve the bank's financial performance due to public trust in banks and provide cheaper resources for the bank, compared to other competitors (Rahmayati, 2021).

In recent years, due to the occurrence of widespread financial irregularities and the lack of confidence of customers towards banks as one of the investment options, special attention has been paid to the banking industry. If banks act completely in accordance with the principles of Islam and provide relevant information to customers for the purpose of stewardship, the usefulness of the decision will be realized for users and the uncertainty will disappear (Nani, 2019). On the other hand, during the past few decades, social responsibility has gained special importance; Because it is related to issues and problems such as unemployment, poverty, environmental pollution and other social issues (Dehghan Nayeri et al., 2021). It is now widely agreed that the lack of ethics in business not only has



harmful consequences for the financial sector but also for society and the environment (Dehghan Nayeri et al., 2020).

This article will examine the level of compliance with social-Islamic responsibility and its relationship with financial performance in Iranian banks. By evaluating the level of social responsibility disclosure, we seek to find out whether financial institutions in Iran (which are operating in accordance with the usury-free banking law) use social reporting methods, which have been recognized as necessary to prove their Islamic practice. Do they fully disclose or not?

In fact, if financial institutions disclose these methods, they have shown the Islamic nature of their operations and structure; Then, the social responsibility disclosure index is compared with the performance of these institutions, which is also calculated through the ROA ratio, and it is determined whether the performance of social-Islamic responsibility by banks has had an impact on their financial performance. In the rest of the article, after stating the theoretical foundations, a comprehensive review of the background of the researches will be done. In the methodology section, while presenting the research hypothesis, it is examined based on statistical methods, and then the research findings are evaluated and concluded. In the final part, based on the results, suggestions are presented in two fields of implementation and research.

II. Theoretical foundations of research

The concept of social responsibility is the strongest and most critical part in the Islamic banking system, which prohibits illegal banking. Therefore, Islamic banks around the world must strive to fulfill their social responsibilities in order to prove their claim to follow the principles of Sharia (DehghanNayeriet al., 2018). In fact, fulfilling social responsibilities is done for the sake of social welfare instead of just for the benefit of banks or due to legal requirements. Therefore, Islamic banks are committed to social and environmental activities at the global and regional level (Abbasi et al., 2012). Social disclosure in Islamic banking is necessary for accountability and social justice. In fact, the disclosure of these responsibilities proves that they are Islamic (Haniffa, R., Hudaib, 2001). Several studies have shown that most Muslims expect a high level of disclosure of responsibility methods from financial institutions and banks (Haniffa, R., Hudaib, 2007). The disclosure of such information facilitates the Islamic-ethical decision-making of stakeholders, which in turn increases the pressure on banks to continuously disclose more information about Islamic-social responsibility.

According to system-based theories, such as stakeholder theories, legitimacy and economic-political theories, organizations are a whole and a part of larger systems and are influenced by the environment (Khazaeiet al., 2021). Therefore, in this view, the social reporting of Islamic banks can be justified (Farook et al., 2007) in such a way that according to the stakeholder theory, companies are facing different expectations from the stakeholders, and responding to these expectations improves relations with them and as a result, it will lead to the improvement of the company's financial performance in the long term. Also, the theory of legitimacy, which is derived from the economic-political paradigm, implies that society, politics and economy are not separate and economic issues cannot be considered without consideration. He examined social and political issues. Therefore, by performing social reporting, Islamic banks display their political, social, and economic goals for a wide range of users, and thus gain favorable legitimacy. In fact, although the implementation of social responsibility has initial costs for companies, ultimately due to the improvement of the company's reputation, the reduction of costs in the long term and the increase in demand, it leads to an increase in sales and profits, and as a result, it leads to the improvement of the company's performance (Taghipouret al., 2022). On the other hand, failure to disclose social responsibilities can lead to the non-support of the stakeholders of the company and as a result will have inappropriate effects on the company's performance. Of course, some researchers have concluded that there is a positive, negative

and even neutral (no effect) curvilinear relationship between social responsibility and corporate performance (Lin, Yang and Liou, 2009). The lack of a suitable theoretical foundation and methodological problems can be the main reasons for these contradictory results. Of course, it should be considered that the impact of social responsibility on company performance is dependent on the characteristics of the industry, which is often defined as the acceptable level of character, ethics and importance of social activities (Lee, S., Singal, M. & Kang, 2012).

III. Dimensions of social-Islamic responsibility

Determining the social-Islamic responsibility disclosure index of banks was done using the disclosure checklist based on international standards, which includes 9 components. The dimensions of this checklist are briefly introduced:

The first component - the mission and vision of the bank: in today's business environment, stakeholders and shareholders tend to be constantly aware of the news and business plans of the financial institution, and this can be achieved by designing and presenting a statement of mission and vision. In fact, the first stage of strategic planning and the basis of all goals and strategies of the organization are their statements. The mission of each organization clearly expresses its existential philosophy and shows the behavior and culture of the organization. Also, the vision of the organization means the destination and ideal of the organization and displays the future that should be realistic and attractive. The statement should not only be a slogan, but it should be achievable and part of the traditions of the organization. Therefore, in the mission and vision of Islamic banks, the goals and strategies of the bank are introduced to the Islamic society; In addition, the bank undertakes to act according to the principles of Islam (Tuhin, 2014).

Second component - the name and composition of the members of the board of directors and the group of senior managers, the members of the board of directors and the group of senior managers are considered as one of the most important factors of efficient corporate governance in Islamic banks. The characteristics of the board of directors, including their composition and independence, have always been considered. In fact, the presence of independent members in the board of directors is to protect the rights of shareholders and plays an important role in reducing the conflict between shareholders and managers. It is also mandatory to create an audit committee for banks, and members of the board of directors are also members of this committee. This committee helps to reduce agency problems so that accurate, timely and unbiased audit information is available to all stakeholders. In this component, things such as the name, job rank and profile of the members, whether the members are shareholders and the members of the board of directors are examined in the audit committee (Darmadi, 2013).

The third component - bank services, in order to remain in the competitive market, Islamic banks must always seek to create innovation in their services, while in these cases, the principles of Islam must not be violated. Due to intense competition, complex markets and stakeholders' demand for more transparency, these banks must provide effective reports on the details of investments and any new financial services to determine whether they have acted in accordance with Islamic principles and ethical laws or not. For this purpose, such activities must be approved by the Shariah Supervisory Board; Because this work is a way to legitimize new products and services in Islamic banks based on the principles of Islam.

The fourth component - zakat, charity and charitable giving, since zakat, charity and charitable giving are among the fundamental values of Islam, the bank's attention to this component will reduce the gap between social classes (Lewis, 2001). In general, zakat and charity are considered as two tools to reduce poverty and inequality in Islam, and these two spiritual concepts are among the social and moral responsibilities of Islamic banks. Zakat and charity redistribute income and wealth, promote

love, cooperation and harmony among people in society, so that for every Muslim, righteous standards of life are guaranteed (Metwally, 1997). Just as in the principles of Islamic banking, receiving interest (riba) is prohibited, payment of zakat is mandatory for Islamic banks.

The fifth component - human resources, according to Islamic ethics in business, employees are the biggest assets of banks, whose welfare should be taken into consideration. In fact, it is the responsibility of the employers to be sure of paying a fair wage (not less and not more than what they do) to the human force under their employment and to give them the opportunity to fulfill their moral obligations; Because creating equal opportunities is emphasized in Islam. Also, in order to improve the status of Islamic Bank and be successful in the competitive market, it is necessary to establish harmony between the name and reputation of the bank and the behavior of the employees. For this purpose, paying attention to the ability of employees and teaching them the principles of Islamic banking is one of the important things to achieve such success. Disclosing the performance of social responsibilities to employees, including value orientation, equal opportunities policy, welfare, and teaching them monetary matters and the principles of Islam is necessary in the annual report of Islamic banks (Darmadi, 2013).

The sixth component - creditors, this component refers to the bank's debt policy and borrowing activities. The ability of banks to determine appropriate financial policies in order to create investment opportunities is one of the main factors of their growth and development. The choice of debt policy or capital structure is one of the important decisions of banks and affects their performance (Arabsalehiet al., 2019).

The seventh component - society, because according to the principles of Sharia, banks are responsible to the society, they must participate in social activities; For example, the bank should spend part of its resources on educational, cultural, health, and health facilities. Paying attention to this component can have an important effect on the performance of the bank.

The eighth component - environment, environmental responsibility as an important aspect of social responsibility is a necessary condition for the bank's survival and success. In Islam, it is forbidden to harm the person, society or the environment. Therefore, Islamic banks are not expected to finance activities that destroy the environment. In addition, Islamic banks must allocate funds to protect the environment. Although it seems unlikely that the activities of Islamic banks will harm the environment directly, the customers of these banks need to ensure that the activities of the banks do not harm the welfare of the society (Darmadi, 2013).

Ninth component - Investigations of the Shariah monitoring board, according to this component, a board should be formed with the purpose of monitoring the Shariah in Islamic banks in order to ensure that the bank's performance complies with the principles of Shariah (Haniffa, R., Hudaib, 2007). The supervisory board includes prominent scholars who are hired by the bank manager. But they are independent, and have the legal authority and power to approve or reject any proposal presented by the bank manager based on Islamic laws, so that along with the annual report of the Islamic Bank, the supervisory board also reports on the compliance or non-compliance of all transactions with the laws. Sharia provides. In cases where there is no conformity, information about the reasons for the non-conformity and the necessary measures to correct it should be disclosed.

IV. Research background

Haniffa and Hudaib (2007) investigated the ethical identity of Islamic banks in the Persian Gulf countries. By designing an "Ethical Identity Checklist" containing eight components, they showed that there is a big gap between the actual level of social responsibility disclosure and the desired level in Islamic banks. Hasan (2010) studied social responsibility reporting in Islamic banks and concluded that social responsibility is not very important for Islamic banks. Zubairu et al. (2012) researched the



social reporting methods of Islamic banks in Saudi Arabia and found that there is no significant difference between the level of social responsibility disclosure in Islamic and conventional banks. Alperhan(2012) showed in his research that there is a big gap between the theoretical claims of Islamic banks about their social activities and empirical findings. These banks are less likely to disclose social activities in financial reports or websites .Abbasi (2012) compared the social responsibility index in Islamic and conventional banks. His findings showed that there is a slight difference in the level and size of disclosure between these two groups of banks.

In the field of the relationship between the social responsibility of companies and their financial performance, many researchers have been done; But very little research has examined this relationship from the perspective of Islam; In this context, the following can be mentioned:

The results of Mosaid and Bouti (2012) studies show that there is no proper disclosure of social-Islamic responsibility in the annual reports of Islamic banks, and there is no significant relationship between financial performance and the disclosure index of social-Islamic responsibility in these banks . Arshadet al. (2012) investigated the effect of social-Islamic responsibility disclosure on the financial performance of these banks by collecting data from seventeen Islamic banks in Malaysia over three years. To calculate the variable of financial performance, these researchers used the criteria of return on assets (ROA) and return on equity (ROE). The analysis showed that the disclosure of social activities significantly has a positive relationship with the financial performance of Islamic banks. Islam, social activities and their disclosure are important business strategies in creating superior and sustainable performance for organizations. In the end, the researchers emphasized that Islamic banks should pay special attention to all their stakeholders .Tuhin(2014) measured the impact of social activities costs on the financial performance of Islamic banks in Bangladesh. In this research, ROA and ROE were considered as financial performance measures for Islamic banks. The results showed that the costs of fulfilling social responsibilities have no effect on the financial performance of Islamic banks .Muflih(2021) article estimates the role of CSR of Islamic banks in influencing customer loyalty, both individually and through the integrated roles of image, trust, satisfaction, and reputation. Empirical analysis of partial least squares structural equation modeling has shown that CSR directly and positively affects loyalty. Indirectly, these two aspects are insignificantly related to each other through the serial roles of image-reputation and satisfaction-reputation, but are significant through the unit role of reputation and the serial role of trust-reputation.

V. Research methodology

This research is of an applied type, and descriptive and inferential statistics have been used in it. In order to evaluate the level of disclosure of social responsibility in the studied sample, descriptive statistics tables have been used. Also, to test the research hypothesis, the analysis of variance method was used and default tests, the use of regression model including the normality test were used to ensure the reliability of the results. To prepare information from Tableau software and to test hypotheses, R software is used. Due to the fact that the data of the banks in the examined sample were analyzed separately by year, as a result, the type of data follows a cross-sectional pattern. Also, in the research literature section, in order to collect information from the library method and in order to collect information to determine the index of social-Islamic responsibility of banks, an international standard checklist has been used. According to the mentioned theoretical foundations and review of the research background, the research hypothesis is formulated as follows:

"There is a significant relationship between the disclosure index of social-Islamic responsibility and financial performance in Iranian banks".

In order to determine the social-Islamic responsibility disclosure index of banks, the international standard checklist has been used as an independent variable, which contains 9 components and

contains 80 items in total. If the bank has disclosed these items in the annual reports, they will be given a number of one and otherwise, a number of zero will be assigned to them. The desired level of social-Islamic responsibility disclosure is achieved when all these items are disclosed in the annual reports of banks. It should be noted that the same index is also used in the descriptive statistics section. Social Responsibility Disclosure Index (CSRDI) is calculated as follows:

$$CSRDI_j = \sum_{i=1}^{n_j} \frac{X_{ij}}{n_j}$$

where in:

X: Checklist items that are assigned a number of one if disclosed and zero if not disclosed.

n: is the total number of checklist items that the bank is required to disclose.

In order to measure financial performance as a dependent variable, the ROA criterion has been used, and to measure it, the net profit is divided by the average total assets (the total value of assets at the beginning of the period plus the total value of assets at the end of the period divided by two).

Model related to hypothesis testing:

$$ROA_t = \beta_0 + \beta_1 CSRDI_t + \varepsilon_t$$

where in:

ROA indicates the return on assets at the end of the period and β is the coefficient of the regression equation.

In this research, all public and private banks were examined, whose reports and financial statements for the years 2020 and 2021 were available on the website of the stock exchange. According to these conditions, 23 banks form the research sample for each of these two years.

VI. Results

Central indices and data dispersion are presented as two main pillars of descriptive statistics in table (1), for which the average index of each bank was used in 2020 and 2021. As can be seen, the average CSRDI is equal to 44.26%. Therefore, it can be concluded that the banks in Iran have a favorable level of social-Islamic responsibility compared to the level expected at the international level (the favorable level of the investigated index is equal to 80, that is, the total items in the checklist have been used) in the annual reports. They do not disclose that this can be attributed to the non-compliance of the interest-free banking law in Iran with the international standards approved for Islamic banks.

Table 1

Central and dispersion indicators of social responsibility for both years 2020 and 2021

Description	CSRDI
At least	30
The first quarter	39/06
Middle	43/75
Average	44/26
The third quarter	49/69
Maximum	75/5
Variance	48/21

Also, the box diagram for the social-Islamic responsibility index shows that 75% of the banks disclose less than 50% of the checklist items, which confirms the lack of disclosure of a desirable level of the social-Islamic responsibility index in Iranian banks; Therefore, it can be concluded that banks in Iran do not adequately disclose their social-Islamic responsibility in their annual reports.

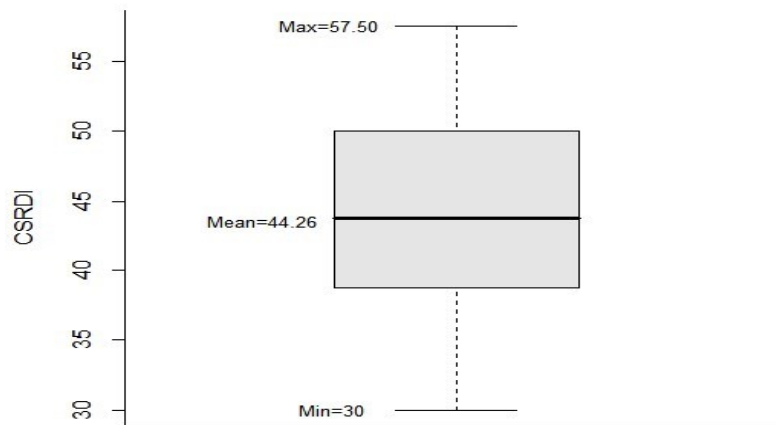


Figure 1 Box plot for CSRD I

Checking the assumption of normality of the data

The assumption of normality of the data was checked using the Shapiro-Wilk statistical test at a significance level of 5%. If the probability value of the test is more than 5%, the normality of the data is confirmed with 95% certainty. After performing this test, the assumption of normality was not established; Therefore, by applying the logarithm transformation, the test results are according to table (2). As seen in table (2), according to the significance level, the hypothesis of logarithm of the data is accepted.

Table 2 Shapiro-Wilk normality test results

ROA logarithm	Fiscal year	
	2020	2021
Average	0/52	0/51
Variance	1/10	0/56
statistics	0/92	0/93
Meaningful level	0/34	0/54

Table (3) shows the size of the Pearson correlation coefficient between the two variables ROA and CSRD I. As can be seen, the correlation coefficient value of 0.1 indicates a weak linear relationship between these two variables.

Table 3 Correlation coefficients and determination of two variables, ROA and CSRD I

Fiscal year	The correlation coefficient	The coefficient of determination	Adjusted coefficient of determination
2020	0/11	0/01	-0/03
2021	0/15	0/02	-0/02

In order to model the relationship between these two variables, a simple linear regression model has been used, the regression coefficients have been estimated and the results of variance analysis are presented in Table (4). As can be seen, the significance level for the variables is more than 5%. This is the conclusion that the null hypothesis is accepted in the analysis of variance, that is, "the coefficients of the variables are zero". Therefore, there is no significant linear relationship between ROA and CSRDI variables.

Table 4 Results of analysis of variance

Variables	Coefficients of variables		t statistic		Meaningful level		F statistic	
	2020	2021	2020	2021	2020	2021	2020	2021
Fiscal year								
Width from the origin	-0/21	-0/31	-0/13	-0/22	0/82	0/72	0/22	0/44
CSRDI	0/02	0/12	0/51	0/63	0/64	0/50		

In this way, the research hypothesis cannot be accepted; That is, "there is no meaningful relationship between the disclosure index of social-Islamic responsibility and financial performance in Iranian banks." Also, according to the size of the determined coefficients calculated in table (3), in 2020, 2 percent and in 2021, 3 percent of the variability of the dependent variable is expressed by the independent variable.

VII. Discussion and conclusions

Islam has provided complete considerations and behavioral rules for all aspects of human life. Therefore, the concept of social responsibility is emphasized in the true essence of holy Islam. According to this concept in Islamic philosophy, banks and financial institutions are encouraged to invest in projects that are both commercially beneficial and to meet the needs of larger societies .In fact, the Islamic banking system should be cautious about choosing the type of investment projects and its transactions and not only pay attention to its profitability component. Social responsibility is the strongest and most critical part in the Islamic banking system, and fulfilling social responsibilities is done for the sake of social welfare instead of only for the bank's interests or due to legal requirements. Therefore, in order to fulfill the goal of Islam regarding the promotion of social welfare, Islamic financial institutions are expected to be responsible towards all their stakeholders and act consciously .In addition to economic responsibilities, the political approach to social responsibility considers legal, ethical and Islamic obligations important for Islamic financial institutions. Of course, the obligation to perform social activities and responsibilities is considered optional for Islamic financial institutions. The results of recent studies in Islamic banking methods indicate that profit and economic efficiency are among the most important motives of Islamic financial institutions, and they are given more attention than the things that are emphasized in Islam, such as justice and social welfare. On the other hand, according to the theory of legitimacy and economic-political paradigm, companies are always trying to show that they act in accordance with the expectations of the society in order to gain a good reputation and credit and have good performance. Also, Islamic banks must adhere to their social-Islamic responsibilities and make appropriate disclosures in this field in order to prove their claim to perform their activities in accordance with the teachings and principles of Islam. These measures will make these financial institutions gain legitimacy and favorable acceptability in the eyes of the society, and as a result, their financial performance will improve with more people referring to these financial institutions.



In this article, we evaluated the level of social-Islamic responsibility disclosure and its relationship with the financial performance of banks in Iran. Due to the fact that according to the statistical studies, no significant relationship was observed between the level of disclosure of social-Islamic responsibility of banks and their financial performance, it is concluded that sufficient and appropriate information regarding the fulfillment of social-Islamic responsibility is not disclosed in the annual reports of Iranian banks, if according to the principles Islam, the disclosure of such cases has been recognized as necessary and necessary to prove the Islamic performance of banks. Of course, the result is consistent with the results of researches such as Rizviet al. (2020) and Herliansyah et al. (2020). In this research, the lack of an optimal level of disclosure can be due to the non-compliance of the usury-free banking law in Iran with international Islamic banking laws.

VIII. Suggestions

According to the results, suggestions can be made in two ranges: executive suggestions and suggestions for future research. The results of this research can be used in the first place by the Central Bank of the Islamic Republic of Iran. Considering that the banks in Iran do not disclose the appropriate level of social-Islamic responsibility in their annual reports, the central bank should develop appropriate requirements to adapt the law of interest-free banking to Islamic banking laws. On the other hand, it is better for bank managers to think of measures to teach the principles and rules of Shariah to the employees. It is also necessary to establish a Shariah supervisory board in banks to closely monitor the work of the employees, and to ensure that the bank's performance is always consistent with the principles of Shariah. The stock exchange organization can also be introduced as the user of the results of this research. This organization can make it a legal requirement for banks and financial institutions to disclose various aspects of the social-Islamic responsibility checklist and consider these issues in determining the disclosure quality index (which this organization determines for stock exchange member companies). Finally, this improves responsiveness to stakeholders and brings benefits to the decision for them.

Regarding the topic of this research, not much internal research has been done; Therefore, it is better to determine the level of social-Islamic responsibility disclosure of banks by applying adjustments and changes in some aspects of the international checklist based on the country's domestic laws, to provide the ground for future research. On the other hand, by preparing a checklist and comparing the index of social-Islamic responsibility disclosure with financial performance for each bank separately, the relationship between these two variables can be examined more precisely in many years.

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