

AAOIFI Financial Accounting Standard 39

Financial Reporting for Zakah

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AAOIFI Financial Accounting Standard (FAS) 39 “Financial Reporting for Zakah” is set out in paragraphs 01-18. All the paragraphs have equal authority. This standard should be read in the context of its objective and the Conceptual Framework for Financial Reporting as endorsed by AAOIFI.

All AAOIFI FASs shall be read in conjunction with the definitions, Shari’ah principles and rules and key considerations provided by AAOIFI Shari’ah Standards (SS) in respect of such products and matters. This standard shall be read particularly in conjunction with SS 35 “Zakah”.

Preface

- PR1 Zakah is an important religious duty and one of the pillars of an Islamic economic system. The accounting treatment of Zakah and the way it affects the financial statements is an important consideration for the users of the financial statements, in making their decisions. The importance of standardisation of such practices cannot be undermined. AAOIFI earlier had issued Financial Accounting Standard (FAS) 9 “Zakah” to streamline the application of the different methods used by Islamic financial institutions (the institutions) in respect of accounting for Zakah and its presentation in the financial statements.
- PR2 The comprehensive revision of FAS 9 “Zakah” commenced in July 2016. The initial part of the project included the overall identification of issues in the existing standard and the need to provide specific guidance. Initial discussions identified major areas of accounting for Zakah that are not addressed in the existing standard and the revision was agreed to include a broader scope. This was also done keeping in view the additional accounting and computations related matters mentioned in AAOIFI Shari'ah Standard (SS) 35 “Zakah”.
- PR3 It is expected that this revised standard will improve the overall accounting and financial reporting practices of the Islamic finance industry.
- PR4 This standard is to be read together with SS 35 “Zakah” and supersedes the earlier FAS 9 “Zakah”.

Introduction

Overview

- IN1 This standard improves upon and supersedes AAOIFI Financial Accounting Standard (FAS) 9 “Zakah” issued previously. This standard aims at setting out the accounting treatment of Zakah in the books of an Islamic financial institution (the institution), including the presentation and disclosure in its financial statements.
- IN2 The standard describes the financial reporting principles applicable, depending upon the institution’s obligation to pay Zakah. In addition, where an institution is not required by law or by virtue of its constitution documents to pay Zakah, it is still required to identify and disclose the amount of Zakah due in respect of the various stakeholders.

Rationale for issuing this standard

- IN3 The newly appointed AAOIFI Accounting Board (AAB / the board), after its constitution in 2015, approved a strategy and plan for improvements in and revisions of a number of existing FASs. Later, the board in its unwavering pursuit to develop comprehensive financial accounting standards for the global Islamic finance industry, initiated a project to revisit existing FASs. The project was designed to review and revise existing AAOIFI FASs, including detailed analysis of each standard and benchmarking against other comparable global standards and best practices to identify and recommend areas of improvement or a complete overhaul, if required. The need for the revision of FAS 9 “Zakah” was highlighted through the industry-wide survey conducted during the project (although the project for revision had already been initiated at that time).
- IN4 A further review of FAS 9 “Zakah” and the preliminary study identified that there is need for improvement, as well as, a need to ensure consistency with the respective Shari’ah standard (and avoiding duplication with the same). In particular, FAS 9 “Zakah” while being an accounting standard, addressed certain aspects of computation for Zakah, which in the absence of a Shari’ah standard was relevant at that time.
- IN5 The initial preliminary study was developed to identify the areas that may require revisions based on existing gaps and industry practices and recommend limited improvements to the standard. During this phase, it appeared that the standard was obsolete on several accounts and limited improvements would not be sufficient. The board concluded to accordingly revise FAS 9 “Zakah” and issue a standard in line with the Shariah standard 35 “Zakah”, global good accounting practices and industry needs. A fresh round of consultation process was initiated with a broader view of improving the standards objective, scope and guidance to cater to the needs of the industry and possibly all relevant stakeholders for Zakah purposes. This broader review scope included bringing consistency in various FASs, particularly with regard to the presentation and reporting of Zakah.

Significant changes from previous standard

- IN6 This standard (FAS 39 “Financial Reporting for Zakah”) brings significant changes from its predecessor standard (FAS 9 “Zakah”), inter-alia, in the following aspects:
- a. the revised standard is primarily a presentation and disclosure standard and does not cover the computation and measurement;

- b. the revised standard provides guidance on two main categories of institutions namely “institutions obliged to pay Zakah” and “institutions not obliged to pay Zakah”;
- c. the accounting and financial reporting requirements such as recognition, presentation and disclosure requirements of this standard shall apply to institutions that are obliged to pay Zakah on behalf of certain or all stakeholders. Institutions that are not obliged to pay Zakah shall apply the disclosure requirements of this standard for certain or all stakeholders, as relevant;
- d. under the revised standard, the recognition, presentation and disclosure requirements for Zakah shall apply to all relevant stakeholders (not limited to shareholders) such as participatory stakeholders, unit holders of various pools, Sukuk-holders;
- e. general rulings of Shari’ah related to Zakah including the computation guidance that are already covered in SS 35 “Zakah” are not reproduced in this standard;
- f. this standard provides guidance on annual Zakah base specific to the institution which includes the net amount subject to Zakah on annual basis. The annual Zakah base for the purpose of this standard shall not apply to those items that are not subject to Zakah on an annual basis such as agriculture produce;
- g. the revised standard provides illustrative examples of the disclosure of calculation and attribution of the Zakah base¹ using the net asset methods; and
- h. this standard uses only the net assets method for illustration of the Zakah base to make it aligned with the relevant Shari’ah standard and to enable adequate disclosures for Zakah applicable to different stakeholders (see paragraphs BC13-14)², without disregarding the possibility to apply any other suitable method.

¹ See Appendix B (i) and (ii)

² AAB decided to issue guidelines on computation of Zakah in line with the requirements of relevant Shari’ah standards (with due collaboration of AAOIFI Shari’ah Board)

AAOIFI Financial Accounting Standard 39

Financial Reporting for Zakah

Objective of the standard

1. The objective of this standard is to establish the principles of financial reporting related to Zakah attributable to different stakeholders of an Islamic financial institution (the institution).

Scope

2. This standard shall apply to an institution with regard to the recognition, presentation and disclosure of Zakah attributable to relevant stakeholders. While computation of Zakah shall be generally applicable individually to each institution (or entity) within a group, this standard shall be applicable on all consolidated and separate / stand-alone financial statements of an institution.
3. This standard does not prescribe the method for determining the Zakah base and measuring Zakah due for a period. [Explanation: An institution shall refer to applicable relevant authoritative guidance (e.g., AAOIFI Shariah Standard (SS) 35 “Zakah”, regulatory requirements or guidance from the institution’s Shari’ah supervisory board, as applicable) to determine the Zakah base and to measure Zakah due for a period].
4. The standard does not specifically address the issues relating to the Zakah on certain produce, including agricultural produce, which according to Shari’ah is due on produce and not on annual basis. In respect of such Zakah, an institution shall develop its own accounting policy, and present necessary disclosures with regard to the reconciliation of computation of Zakah, as well as, shall follow the requirements of this standard, insofar as practicable.

Definitions

5. For the purpose of interpreting and applying this standard, the following short definitions are relevant:
 - a. Advance Zakah (at times referred to as early paid Zakah) – is the amount paid as Zakah over and above the Zakah expense recognised in the income statement, as well as, excess Zakah paid through adjustment to equity for the current and prior years;
 - b. Annual Zakah base – is the total net amount subject to Zakah at the end of an annual period (maybe, but not necessarily coinciding with the financial reporting date of an institution), but does not include the value of agriculture produce or any other produce which is not subject to Zakah on an annual basis;
 - c. Institutions not obliged to pay Zakah – are the institutions other than the institutions which are obliged to pay Zakah [Explanation: These include institutions which are not obliged to pay Zakah on behalf of one or certain classes of stakeholders, to the extent of Zakah applicable to such stakeholders];
 - d. Institutions obliged to pay Zakah – are such institutions that are required to pay Zakah on net assets pertaining to certain or all relevant stakeholders whereby one or more of the following conditions is / are met:

- i. when the law or regulation requires the institution to pay the Zakah obligation;
 - ii. when the institution by virtue of its constitution documents is required to pay the Zakah obligation;
 - iii. when the general assembly of shareholders has passed a resolution requiring the institution to pay the Zakah obligation; or
 - iv. where the contract with certain stakeholders requires the institution to pay the Zakah obligation;
- e. Realisable value – is the entity-specific value, at which the institution is able to sell the relevant asset (i.e., convert the asset to cash);
 - f. Relevant stakeholders (for Zakah purposes) – include, but are not limited, to all those who provide capital in different capacities such as shareholders, participatory stakeholders etc.;
 - g. Zakah – is a right³ (a religious responsibility on a Muslim) which becomes due in certain types of wealth, and disbursable to specific categories of recipients in respect of the current annual period. Subject to different institutions' legal environment, it may be an expense to the institution or an obligation of the individual shareholders or other stakeholders;
 - h. Zakatable assets – are those assets that are subject to Zakah in line with the Shari'ah requirements on an annual basis;
 - i. Zakah liability – is the unpaid amount of current and prior years Zakah due; and
 - j. Zakah rate⁴ – is the rate applied to Zakah base in order to calculate Zakah.

Institutions obliged to pay Zakah

Recognition of Zakah due and corresponding liability

Recognition of current Zakah due as an expense

- 6. An institution obliged to pay Zakah by law or by virtue of its constitution documents shall recognise current Zakah due for the period as an expense in its financial statements in line with the requirements of paragraph 7.
- 7. Current Zakah due, or reversal thereof, for the current and prior periods shall be recognised as expense (or reversal of expense) and included in profit or loss for the period.

³ Being a specific and conditional right for the eight specific categories of beneficiaries (defined in Al-Quran, at-Tauba:60) on the wealth of Muslims

⁴ See paragraph 3/2/4 of SS 35 "Zakah" for Zakah rate and paragraph 3/2/2 of SS 35 "Zakah" for Nisab (Zakatable wealth stratum)

Recognition of Zakah as adjustment to equity

8. Where Zakah is not required to be paid by law or by virtue of its constitution documents, and where the institution is considered as an agent to pay Zakah on behalf of certain stakeholders, any amount paid in respect of Zakah shall be adjusted with the equity of the relevant stakeholders.
9. In case of insufficient distributable reserves (available in equity) to meet the relevant stakeholders' Zakah obligations, the amount of Zakah due shall be recorded as receivable from respective stakeholders.

Recognition of Zakah liability

10. Current Zakah due shall be recognised as a liability in the statement of financial position of the institution.
11. If the amount already paid in respect of current and / or prior periods Zakah obligations exceeds the amount due for those period(s), the excess shall be recognised as advance Zakah in statement of financial position of the institution.

Institutions not obliged to pay Zakah

12. An institution not obliged to pay Zakah (for certain or all relevant stakeholders) shall disclose the Zakah base and the amount of total Zakah due on that base, as well as, the Zakah per share / unit for the current period, applicable to such stakeholders.

Presentation and disclosure requirements

13. In addition to the presentation and disclosure requirements stated in FAS 1 (Revised 2021) "General Presentation and Disclosures in the Financial Statements", an institution shall disclose the following (as minimum disclosure requirements):
 - a. the method used for determining the Zakah base, the items included in this base and its reconciliation thereof. Appendix B (i) and (ii) provide illustrative disclosures for the same applying the net assets method;
 - b. the relevant authoritative guidance (e.g., AAOIFI Shariah Standard (SS) 35 "Zakah", regulatory requirements, or guidance from the institution's Shari'ah supervisory board) used for determining such method, including the rulings of the Shari'ah supervisory board of the institution on the issues related to Zakah that are not addressed in SS 35 "Zakah";
 - c. Zakah per share and / or per unit for each pool or category of investments whether it is paid by the institution or otherwise;
 - d. a reconciliation between the Zakah liability and expenses presented in the consolidated financial statements and those presented in its subsidiaries' stand-alone or separate financial statements with a brief about the respective subsidiaries' treatment of Zakah, particularly for the amount attributable to parent's respective stakeholders;
 - e. a statement as to whether or not the institution collects and pays Zakah on behalf of participatory stakeholders and other accounts;

- f. in circumstances where Zakah paid to a single person / charitable institution is more than 5% of total Zakah payable, the nature of such payment and details of the recipient;
- g. the difference between amount of Zakah as required by law and Zakah determined voluntarily (for example, in line with the requirements of SS 35 “Zakah” and related guidance), if any;
- h. the amount of Zakah that is due from the equity of participatory stakeholders;
- i. the amount of Zakah allocated or paid for on behalf of certain or all relevant stakeholders [Note: In respect of off-balance-sheet assets under management, relevant disclosures shall be made separately, in line with the disclosure requirements of this standard];
- j. where the institution has agricultural produce etc., the accounting policy for determining Zakah base of such produce along with the amount of Zakah due on the produce (also see paragraph 4);
- k. the Zakah due, transferred from the institution to the Zakah fund, as well as, amounts of Zakah received from other sources of funds duly presented in accordance with FAS 1 (Revised 2021) “General Presentation and Disclosures in the Financial Statements”; and
- l. any dispute between the institution and relevant Zakah authorities about the amount of Zakah payable, including the amount and period to which dispute belongs along with reasons of such dispute.

Zakah fund

- 14. Where the institution has established its Zakah liability, the same (with corresponding assets) shall be transferred to a Zakah fund immediately. Zakah fund shall be treated distinct and separate from the institution (similar to assets under management). Such assets shall not meet the definition of asset of the institution, and hence, shall not be available to the institution even in case of liquidation or bankruptcy.
- 15. Where in rare circumstances, Zakah fund is invested (with the institution or any other institution) or is kept in a current (Qard) account, which shall not be with the institution itself, in accordance with a policy duly approved by the institutions Shari’ah supervisory board, developed in line with Shari’ah principles and rules, particularly AAOIFI SS 35 “Zakah”⁵, the institution shall disclose such amounts and the returns earned from use of such funds. The institution shall also disclose the reason as to why any payment for Zakah is delayed.
- 16. The Illustrative disclosure in respect of “sources and application of Zakah” is attached as Appendix C.

Effective date

- 17. This standard shall be effective for the financial periods beginning on or after 1 January 2023. Early adoption is permitted.

⁵ Paragraph 2/2 & 10/4 of SS 35 “Zakah”

Amendments to other standards

18. This standard supersedes FAS 9 “Zakah”.

Appendices

Appendix A: Adoption of the standard

This standard was presented for the approval in the 26th AAOIFI Accounting Board meeting held on 28-29 Rabi' II 1443H, corresponding to 3-4 December 2021 and was duly approved.

Members of the board

1. Mr. Hamad Abdulla Al Oqab (chairman)
2. Mr. Syed Najmul Hussain (deputy chairman)
3. Mr. Abdelhalim Elsayed Elamin
4. Mr. Abdulmalik Alsuwayni
5. Dr. Abdulrahman M. Alrazeen
6. Ms. Amal Al Masri
7. Dr. Bello Lawal Danbatta
8. Mr. Firas Hamdan
9. Mr. Hondamir Nusratkhujaev
10. Mr. Imtiaz Ibrahim
11. Mr. Irshad Mahmood
12. Dr. Mohammed Albeltagi
13. Mr. Samet Arslan
14. Mr. Saud Al Busaidi
15. Mr. Yusuf Ibrahim Hassan

Reservation

The standard was approved unanimously.

Working group members

1. Mr. Mohamed Bouya Ould Mohamed Fall (chairman)
2. Dr. Abdulrahman M. Alrazeen
3. Mr. Kamran Malik
4. Mr. Abdel Rahman Eltoum Ahmed Alkando

Executive team

1. Mr. Omar Mustafa Ansari (AAOIFI)
2. Mr. Mohammad Majd Bakir (AAOIFI)
3. Ms. Farida Cassim (AAOIFI)
4. Mr. Atif Rashid (Executive Assistant)

Appendix B(i): Illustrative⁶ disclosure⁷ of calculation and attribution of Zakah⁸

| Total assets / liabilities | Basis of valuation | | Attribution | | | Basis of valuation | | Attribution | | |
|--|---|--------------------------------|-------------|------------------|--------------|---|-------------------------------|-------------|-------|--------------|
| | For accounting purposes (illustrative only) | Accounting carrying value (CU) | Equity | NCI ⁹ | Quasi-equity | For Zakah purposes (illustrative only) | Value for Zakah purposes (CU) | Equity | NCI | Quasi-equity |
| Cash and cash equivalents | Historical cost / fair value | xxxxx | xxxxx | xxxxx | xxxxx | Realisable value | xxxxx | xxxxx | xxxxx | xxxxx |
| Receivables | Par value less unamortised deferred profit – net of allowance for credit losses | xxxxx | xxxxx | xxxxx | xxxxx | Par value – net of allowance for credit losses | xxxxx | xxxxx | xxxxx | xxxxx |
| Mudaraba investment [if Zakah not being paid by the venture directly] | Historical cost less undistributed losses – net of allowance for impairment | xxxxx | xxxxx | xxxxx | xxxxx | Realisable value / realisable value of net assets subject to Zakah in the Mudaraba venture (preferred) | xxxxx | xxxxx | xxxxx | xxxxx |
| Musharaka investment [if Zakah not being paid by the venture directly] | Historical cost less undistributed losses – net of allowance for impairment (preferred) | xxxxx | xxxxx | xxxxx | xxxxx | Realisable value / realisable value of net assets subject to Zakah in the Musharaka venture (preferred) | xxxxx | xxxxx | xxxxx | xxxxx |
| Salam receivable | Par value | xxxxx | xxxxx | xxxxx | xxxxx | Par value | xxxxx | xxxxx | xxxxx | xxxxx |
| Istisna'a receivable | Par value | xxxxx | xxxxx | xxxxx | xxxxx | Par value | xxxxx | xxxxx | xxxxx | xxxxx |
| Assets for trading | Lower of cost and net realisable value | xxxxx | xxxxx | xxxxx | xxxxx | Realisable value / exempt etc. | xxxxx | xxxxx | xxxxx | xxxxx |

⁶ Note: This illustrative disclosure follows the multi-columnar approach for total values and attribution to different participatory stakeholders. It needs to be clarified that this is for illustration purposes only, and an institution may follow any other suitable disclosure format including single-columnar disclosure identifying values separately for each set of participatory stakeholders (see Appendix B(ii) for an alternative illustrations)

⁷ Any assets and liabilities excluded for the computation in line with relevant Shari'ah principles and rules shall be adequately disclosed

⁸ Note: This (and also Appendix B(ii)) is an illustrative disclosure of the calculation and attribution of Zakah in the financial statements of an institution and shall not be construed as or confused with a computation guidance of Zakah applicable to an institution. Any computation for Zakah shall be performed in line with the SS 35 "Zakah" and any guidelines issued by AAOIFI on the subject

⁹ Non-Controlling Interest

| Total assets / liabilities | Basis of valuation | | Attribution | | | Basis of valuation | | Attribution | | |
|--|--|--------------------------------|---------------|---------------|---------------|---|-------------------------------|---------------|---------------|---------------|
| Assets | For accounting purposes (illustrative only) | Accounting carrying value (CU) | Equity | NCI | Quasi-equity | For Zakah purposes (illustrative only) | Value for Zakah purposes (CU) | Equity | NCI | Quasi-equity |
| Inventories | Lower of cost and net realisable value | xxxxx | xxxxx | xxxxx | xxxxx | Net realisable value | xxxxx | xxxxx | xxxxx | xxxxx |
| Marketable securities | Fair value / amortised cost | xxxxx | xxxxx | xxxxx | xxxxx | Fair value | xxxxx | xxxxx | xxxxx | xxxxx |
| Real estate for sale | Fair value / historical cost less depreciation | xxxxx | xxxxx | xxxxx | xxxxx | Fair value | xxxxx | xxxxx | xxxxx | xxxxx |
| Real estate for rent / own use | Fair value / historical cost less depreciation | xxxxx | xxxxx | xxxxx | xxxxx | N/A | Nil | Nil | Nil | Nil |
| Investment in Sukuk | Fair value / amortised cost | xxxxx | xxxxx | xxxxx | xxxxx | As per intention and nature of underlying assets / net assets | xxxxx | xxxxx | xxxxx | xxxxx |
| Others | As per relevant FAS | xxxxx | xxxxx | xxxxx | xxxxx | Realisable value / exempt etc. | xxxxx | xxxxx | xxxxx | xxxxx |
| Liabilities | | | | | | | | | | |
| Current accounts | Book value = par value less repayments | xxxxx | xxxxx | xxxxx | xxxxx | Book value | xxxxx | xxxxx | xxxxx | xxxxx |
| Payables and other liabilities adjustable for Zakah purposes | Book value = par value less repayments | xxxxx | xxxxx | xxxxx | xxxxx | Book value | xxxxx | xxxxx | xxxxx | xxxxx |
| Payables and other liabilities not adjustable for Zakah purposes | Book value = par value less repayments | xxxxx | xxxxx | xxxxx | xxxxx | N/A | Nil | Nil | Nil | Nil |
| Provisions and constructive obligations | Fair value | xxxxx | xxxxx | xxxxx | xxxxx | N/A | Nil | Nil | Nil | Nil |
| Total | | xxxxxx | xxxxxx | xxxxxx | xxxxxx | | xxxxxx | xxxxxx | xxxxxx | xxxxxx |
| Zakah computed @ __% | | | | | | | xxxxx | xxxxx | xxxxx | xxxxx |
| Other Zakah (if any) * | | | | | | | xxxxx | xxxxx | xxxxx | xxxxx |
| Total Zakah | | | | | | | xxxxxx | xxxxxx | xxxxxx | xxxxxx |
| *other Zakah includes Zakah on assets not subject to normal Zakah (for example Zakah on certain animals, agricultural produce, mineral resources etc.) | | | | | | | | | | |

Appendix B(ii): Illustrative¹⁰ disclosure of calculation and attribution of Zakah

| Assets / liabilities | Basis of valuation for accounting purposes (illustrative only) | Accounting carrying value (CU) | Basis of valuation for Zakah purposes (illustrative only) | Value for Zakah purposes (CU) |
|--|---|--------------------------------|---|-------------------------------|
| Assets | | | | |
| Cash and cash equivalents | Historical cost / fair value | xxxxx | Realisable value | xxxxx |
| Receivables | Par value less unamortised deferred profit – net of allowance for credit losses | xxxxx | Par value – net of allowance for credit losses | xxxxx |
| Mudaraba investment [if Zakah not being paid by the venture directly] | Historical cost less undistributed losses – net of allowance for impairment | xxxxx | Realisable value / realisable value of net assets subject to Zakah in the Mudaraba venture (preferred) | xxxxx |
| Musharaka investment [if Zakah not being paid by the venture directly] | Historical cost less undistributed losses – net of allowance for impairment (preferred) | xxxxx | Realisable value / realisable value of net assets subject to Zakah in the Musharaka venture (preferred) | xxxxx |
| Salam | Par value | xxxxx | Par value | xxxxx |
| Istisna'a | Par value | xxxxx | Par value | xxxxx |
| Assets for trading | Lower of cost and net realisable value | xxxxx | Realisable value / exempt etc. | xxxxx |
| Inventories | Lower of cost and net realisable value | xxxxx | Net realisable value | xxxxx |
| Marketable securities | Fair value / amortised cost | xxxxx | Fair value | xxxxx |
| Real estate for sale | Fair value / historical cost less depreciation | xxxxx | Fair value | xxxxx |
| Real estate for rent / own use | Fair value / historical cost less depreciation | xxxxx | N/A | Nil |
| Investment in Sukuk | Fair value / amortised cost | xxxxx | As per intention and nature of underlying assets / net assets | xxxxx |
| Others | As per relevant AAOIFI FAS | xxxxx | Realisable value / exempt etc. | xxxxx |
| Liabilities | | | | |
| Current accounts | Book value = par value less repayments | xxxxx | Book value | xxxxx |
| Payables and other liabilities adjustable for Zakah purposes | Book value = par value less repayments | xxxxx | Book value | xxxxx |

¹⁰ Note: This illustrative disclosure follows the approach for a single column for total values and attribution to different participatory stakeholders in the end. It needs to be clarified that this is for illustration purposes only

| | | | | |
|--|--|---------------|-----|---------------|
| Payables and other liabilities not adjustable for Zakah purposes | Book value = par value less repayments | xxxxx | N/A | Nil |
| Provisions and constructive obligations | Fair value | xxxxx | N/A | Nil |
| Total | | xxxxxx | | xxxxxx |
| Zakah computed @ __% | | | | xxxxxx |
| Other Zakah (if any) * | | | | xxxxxx |
| Total Zakah | | | | xxxxxx |
| Zakah attributable to: | | | | |
| • Shareholders (total & per share) | | | | xxxxxx |
| • Non-controlling interest | | | | xxxxxx |
| • Different classes of quasi-equity / participatory stakeholders | | | | xxxxxx |
| Total | | | | xxxxxx |
| *other Zakah includes Zakah on assets not subject to normal Zakah (for example Zakah on certain animals, agricultural produce, mineral resources etc.) | | | | |

Appendix C: Illustrative disclosure for sources and application of Zakah

| Sources of Zakah | Current year | Prior year |
|---|--------------|--------------|
| Balance as at the beginning of the period | XXXXX | XXXXX |
| Zakah due from the institution / shareholders of the institution | XXXXX | XXXXX |
| Zakah due from participatory stakeholders (including investment accountholders) | XXXXX | XXXXX |
| Voluntary Zakah | XXXXX | XXXXX |
| Total Zakah available for distribution | XXXXX | XXXXX |
| | | |
| Uses of Zakah fund | | |
| Zakah paid to the government | XXXXX | XXXXX |
| Zakah paid to authorized Zakah institutions | XXXXX | XXXXX |
| Zakah for the poor (may or may not be asking for financial help) | XXXXX | XXXXX |
| Zakah for the needy (but not asking) | XXXXX | XXXXX |
| Zakah for the heart-winning (of non-Muslims) | XXXXX | XXXXX |
| Zakah for freeing of slaves | XXXXX | XXXXX |
| Zakah for travellers (in financial difficulties) | XXXXX | XXXXX |
| Zakah for trustees of Zakah | XXXXX | XXXXX |
| Zakah for the heavily indebted | XXXXX | XXXXX |
| Zakah for the cause of Allah | XXXXX | XXXXX |
| Administration and general expenses – including staff cost | XXXXX | XXXXX |
| Total uses | XXXXX | XXXXX |
| Increase (decrease) of sources over uses | XXXXX | XXXXX |
| Undistributed Zakah fund as at the end of the period | XXXXX | XXXXX |

*The Zakah fund is utilized by making contributions to organizations which are registered with the _____, namely _____.

[Note: Additional details shall be presented in notes as appropriate, based on respective materiality.]

Appendix D: Basis for conclusions

Determination of revised scope and title of the standard

- BC1 The AAOIFI Accounting Board (AAB / the board) deliberated on the need for revision of AAOIFI Financial Accounting Standard (FAS) 9 “Zakah” while developing its strategy in 2015. The board noted that FAS 9 “Zakah” was developed in 1998, whereas AAOIFI Shariah Standard (SS) 35 “Zakah” was issued in 2008. Due to the significant time gap between issuance of the two standards, some contradictions were identified that were reported to the respective boards over the years. For example, FAS 9 “Zakah” provided guidance for shareholders only and was silent on Zakah implications on other stakeholders.
- BC2 The board debated on the contents of the proposed standard. The board noted that industry expectations were about a standard on the computation of Zakah. The board agreed that accounting treatments, financial reporting and presentation fall within the scope of work of the board. On the other hand, the interpretation and explanation for Zakah computations are not in the mandate of the board. The board concluded that to avoid overlap with the mandate of the AAOIFI Shari’ah Board, only the principles of financial reporting shall be provided to the industry through this standard. To alleviate any confusion, and to better reflect the revised scope, the title of the standard was agreed to be changed to “Financial Reporting for Zakah”.
- BC3 AAOIFI SS 35 “Zakah” identifies the Zakah base and the different types of Zakatable assets, liabilities and their allocations. Moreover, the standard defines Zakah rates, disbursements and rulings on its recipients. Noting these facts, the board concluded that the general rulings of Shari’ah such as ownership, Nisaab, Hawl are already provided for in “Conditions for Zakah obligations” paragraph 3/2 of SS 35 “Zakah” and “Applicable Zakah rate” in paragraph 3/3 of SS 35 “Zakah” and therefore will not be reproduced in this FAS.

Institutions who are obliged to pay Zakah and institutions not obliged to pay Zakah

- BC4 During the deliberations of the revised scope, the board considered that certain jurisdictions’ have Zakah as a legal requirement whereas in certain jurisdictions it is not a legal requirement but stakeholders may appoint the institution to act as its agent for Zakah purposes. To ensure that revised standard is applicable to most jurisdictions with minimal implications for the institutions, this standard provides separate guidance for “institutions obliged to pay Zakah” and “institutions not obliged to pay Zakah”. For institutions obliged to pay Zakah, the standard provides guidance on how the institution shall identify, recognise, disclose and discharge the Zakah liability on net assets of certain or all stakeholders. Whereas institutions that are not obliged to pay Zakah on net assets of certain or all stakeholders shall determine and disclose the Zakah obligation for each class of such stakeholders, separately.

Zakah due by virtue of constitution documents

- BC5 During the finalisation of the standard, certain members of the board were of the view that constitution documents are not considered equivalent to the law as these may be modified through a special resolution. Therefore, the payment of Zakah in such case may be considered a delegation from the shareholder’s and regardless of the constitution documents, Zakah should be treated as an adjustment to equity. Moreover, Zakah is a distribution of profit and therefore shall not be expensed. The board voted on the matter, and upheld its initial views in line with the exposure

draft, whereby in such case the treatment as an expense was considered more appropriate. This is because Zakah, in principle, is not computed on the shareholders' equity. Instead, it is computed on the basis of Zakatable assets. Moreover, the requirements of the constitution documents shall be considered a legal requirement for the institution for this purpose.

- BC6 The board also took into consideration the perceived tax benefits for the institutions. It was agreed the standard shall take a tax neutral stance since provisions of tax laws are related to the governing jurisdiction and shall not impact the accounting treatments.

Scope exclusions – Zakah on agriculture produce and minerals

- BC7 Zakah on agriculture produce along with minerals and related items was debated. Various arguments and reasons to include and exclude such items were discussed. The board believed that the standard is principally based on annual Zakah balances at the end of Hawl (Zakah year). In contrast, Zakah on agriculture and minerals are based on 'produce' rather than annual balances. The board concluded that the standard shall not provide guidance on recognition and presentation of Zakah and any other type of Zakah that is not due on an annual basis. For such Zakah due on production basis, e.g., animal, produce or minerals, the institution is required to disclose the accounting policy and provide a reconciliation of Zakah.

Measurement of Zakah

- BC8 This standard primarily deals with the disclosure and presentation in both situations of Zakah – when it is a legal requirement and when it is a voluntary requirement.
- BC9 The board re-evaluated and concluded that the standard should not provide measurement guidance on Zakah due, since this is primarily under the ambit of Shari'ah. Moreover, SS 35 "Zakah" already covers identifying the Zakah base and indicates the different types of Zakatable assets and liabilities, as well as, their allocations and deductions. The Shari'ah standard also illustrates the payable Zakah rates and the specific heads of Zakah disbursements. Furthermore, prescribing accounting treatments may create a difference in Zakah as per AAOIFI and local jurisdiction requirements. The board decided to add a disclosure requirement stating the difference in Zakah amounts that have been computed and paid as per AAOIFI and any other criteria. However, to ensure consistency and comprehensiveness the standard includes references from SS 35 "Zakah" where relevant.
- BC10 The board further considered that the standardisation of the methods and basis used by institutions to calculate Zakah and the disclosure of the same in the institution's financial statements would help provide useful information to users of financial statements. In case of the institutions that are obliged to pay Zakah, the accounting treatment of Zakah affects the determination of the institutions' net income, which is an important indicator used by users of the financial statements in making their decision.
- BC11 The board also discussed as to whether the shareholders are responsible for Zakah of stakeholders, including participatory stakeholders. The board concluded that where an institution is obliged to pay Zakah on all or certain stakeholders, it shall disclose the amount on behalf of such stakeholders and the method used to determine them, which may or may not be equal to the stakeholder's actual liability. Accordingly, the ultimate responsibility shall remain with the stakeholders. However,

in a jurisdiction, if it is required by law that the institution shall deduct and pay Zakah on behalf of such stakeholders, the same shall be accounted for in line with the requirements of this standard.

- BC12 It is also understood that the creditors (including current account depositors) are not considered participatory stakeholders for the purpose of this standard, and hence any Zakah payable related to their balances is not within the scope of this standard.

Methods for determination of Zakah base

- BC13 FAS 9 “Zakah” provided two methods for Zakah determination based on net assets and net invested funds, while SS 35 “Zakah” only provided the net assets method for determining the Zakah base of the institution. Therefore, the board decided to align the revised standard with the Shari’ah standard, whereby the standard provides guidance on recognition, presentation and disclosures of Zakah based on net assets of the relevant stakeholders. Accordingly, the disclosure requirements for Zakah base are based on the net assets method only.
- BC14 However, after considering public comments in favour of allowing the net invested funds method, the board decided not to specifically disallow the same method without specifying any further details. The board reemphasised that the illustrations presented in the standard shall be based on the net assets method as it is aligned with SS 35 “Zakah” and it is the appropriate method to calculate total Zakah for the institution and then allocating it to different stakeholders (for payment, or at least, for the disclosure purposes).

Expected cash value

- BC15 The previous standard on Zakah required trading assets to be valued at cash and cash equivalent value (market selling price). During the discussion, this term was considered inappropriate given the limited scope and a better term for the same was sought. The board decided on using an appropriate definition for ‘realisable value’ which is an entity specific value and is better understood in the accounting terminology.

Sources and application of Zakah

- BC16 During the revision of FAS 1 (Revised 2021) “General Presentation and Disclosures in the Financial Statements”, it was decided that the statement of sources and application of Zakah shall be moved to the notes to the financial statements, rather than being a primary statement. The board, after due discussion decided to provide an illustrative disclosure of the same as an appendix to this standard.

Zakah fund – assets under management but not controlled / owned

- BC17 The board considered that the established Zakah liability and the related assets are no more in the ownership of (and control of) the institution. Accordingly, the established Zakah liability and corresponding assets shall be transferred to Zakah fund which will be distinct and separate from the institution (similar to assets under management). The board considered the views of the committee of the AAOIFI Shari’ah board for review of accounting and governance standards and decided that segregated Zakah funds (net assets of funds) shall not become part of overall asset of the institution even in case of bankruptcy.

Appendix E: Brief history of the preparation of the standard

- H1 The AAOIFI Accounting Board (AAB / the board) 1st meeting convened on 6-7 Jumada II 1437H, corresponding to 15-16 March 2016 after due deliberation it was decided that more disclosure shall be added to the Zakah Standard in line with the Shari'ah Standard on Zakah.
- H2 The AAB held its 6th meeting on 21-22 Shawwal 1438H, corresponding to 15-16 of July 2017 where the the consultation notes were discussed. It was concluded that the calculation of Zakah is a Shari'ah matter, therefore the standard should focus on recognition, presentation and disclosures.
- H3 The 1st working group meeting for the revision of the standard was held on 14 Rajab 1440H, corresponding to 21 March 2019 where the initial draft along with the detailed illustrative examples along with comparison with the AAOIFI Shari'ah Standard was discussed.
- H4 The 2nd working group meeting for the revision of the standard was held on 14 Muharram 1441H, corresponding to 13 September 2019 where the second draft was presented along with discussion on the timeline for the deliverables and way forward. The standard was agreed to be on agenda for the upcoming AAB meeting.
- H5 The AAB held its 15th meeting on 15-16 Muharram 1441H, corresponding to 14-15 September 2019. AAB discussed different aspects of the standard and finalized the scope and broad contents of the standard. It was also advised to the secretariat and the working group that the exposure draft of the standard shall be brought to the next board meeting for finalization.
- H6 The 3rd working group meeting was held on 17 Safar 1441H, corresponding to 17 October 2019 was held to discuss and finalize the draft standard. The working group in this meeting made necessary changes and recommended the draft to be presented to the upcoming AAB meeting, after incorporation of the changes suggested by the working group.
- H7 The AAB held its 16th meeting on 2-3 Rabi' I 1441H, corresponding to 31 October and 1 November 2019 where the exposure draft was presented with working group conclusions. After discussion the draft was principally approved for issuance.
- H8 After incorporating the AAB recommendations and the basis of conclusions and another round of review by the working group, certain observations from the working group was presented to the AAB in its 18th meeting held on 1-2 Dhul-Qa'dah 1441H, corresponding to 22-23 June 2020.
- H9 The exposure draft, after incorporation of changes by the board, was issued on 17 Dhul-Qa'dah 1441H, corresponding to 8 July 2020.
- H10 The committee of the AAOIFI Shari'ah board for review of accounting and governance standards held its 20th meeting on 14 Rabi' I 1442H, corresponding to 29 November 2020 where the standard was duly discussed for conformity with Shari'ah standards.
- H11 The public hearings for the exposure draft were conducted through webinar in November 2020 and April 2021. Another public hearing in Arabic language was conducted in July 2021 through webinar.
- H12 All comments received from the public hearings along with the views and comments received in writing from different industry participants on the exposure draft were presented for discussion at

two working group meetings held on 25 Dhul-Hijjah 1442H, corresponding to 4 August 2021 and 3 Muharram 1443H corresponding to 11 August 2021. After due deliberation, the standard was forwarded to the board for final approval.

- H13 The standard was presented at the 25th AAB meeting held on 25-26 Muharram 1443H, corresponding to 2-3 September 2021. The standard was approved in principle with instructions and suggested changes.
- H14 The standard was presented to the AAOIFI Public Interest Monitoring Consultative Committee (PIMCC) on 27 Rabi' II 1443H, corresponding to 2 December 2021. PIMCC did not raise any concerns on the standard from the public interest perspective.
- H15 The standard was briefly presented again at the 26th AAOIFI Accounting Board meeting held on 28 Rabi' II 1443H, corresponding to 3-4 December 2021 after incorporating instructions and comments of the board. The standard was approved for publishing with no additional changes.
- H16 After due process, the standard was issued on 27 Jumada I 1443H, corresponding to 31 December 2021.