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Determinants of ethical identity disclosure among Malaysian and Bahrain Islamic banks

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Abstract - In Islam, the practice of transparent and adequate disclosure is stressed and recommended, especially with regard to the ethical identity of Islamic institutions. This is to ensure that the business activities are in line with *Shariah* principles since *Shariah* is the main component and the foremost salient feature in Islamic banks, which differentiate them from conventional banks. Thus, this study examines the ethical identity disclosure of sixteen (16) Malaysian and five (5) Bahrain Islamic banks for five consecutive years, 2007 to 2011. The study further identifies the determinants affecting the ethical identity disclosure in both countries. The ethical identity disclosure index developed for measuring the level of ethical identity disclosure comprises nine dimensions consisting of 81 constructs. The results indicate that the overall disclosure level in both countries is 51.6%, which suggests a low level of ethical identity disclosure. Room for improvement includes information on vision and mission statement product; *Zakat*, charity and benevolent loans; community; environment, and *Shariah* Supervisory Board. In examining the determinants affecting the ethical identity disclosure, the results show that independent directors do not affect the level of ethical disclosure. However, board size, *Shariah* supervisory board and investment account holders significantly influence the disclosure level by both banking industries. Hence, contrary to the agency theory, the results indicate that independent directors in both Malaysian and Bahrain Islamic banks are not effective or competent in performing their role in monitoring the performance and activities of the management of Islamic banks. However, in line with the institutional theory, having greater monitoring by the board of directors, *Shariah* supervisory Board and investment account holders could enhance the disclosure compliance by Malaysian and Bahrain Islamic banks, and, thus, could attract more Muslim investors to participate in the Islamic banking industry.

Keywords: ethical identity disclosure, Islamic banks, Malaysia, Bahrain

1. Introduction

Islamic Banks, similar to conventional banks, are profitable organizations that aim to gain profit. However, in doing so, Islamic banks avoid interest and other aspects that are prohibited by Islam, which therefore characterizes Islamic banks as having an ethical identity (Gray and Balmer, 2001; Haniffa and Hudaib, 2007). Islamic banks need to disclose ethical information (both qualitative and quantitative) based on the Islamic ethical business and *Shariah* framework, which is vital in assisting the stakeholder in making economic religious decisions as well as assisting the management, *Shariah* Supervisory Board and external auditor in demonstrating the accountability to society. Since one of the aims of Islamic Banks is to promote and develop the application of Islamic principles, laws and traditions concerning transactions of financial, banking and related business affairs, they should exhibit their own ethical identity in setting them apart from other types of organization.

In Islam, the practice of transparency and adequate disclosure is highly recommended, especially in business dealings. This is to ensure that the business transaction is free from any form of exploitation. In Al Quran, numerous verses have emphasized the demand for fair, transparent and ethical behavior in all business transactions. For example, in Chapter 2 *Surah Al Baqarah*, Verse 282, Muslims are required to have contracts written by a scribe as well as to have witnesses comprising at least two men or one man and two women in the business transaction. This is to ensure that the obligation and transactions are executed clearly without any doubt from any party. From this verse, it is

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clear that transparency should be the hallmark of Islamic institutions, as it will ensure justice to all parties involved in the transaction.

Kayed and Hassan (2011) further implied that having adequate and consistent disclosure is necessary for the Islamic banking industry to remain relatively positive and resilient. To ensure the financial stability of the Islamic financial system, Islamic banks need to ensure that their transparency is proper and consistent, especially with regard to their ethical identity as an Islamic institution. They have to ensure that their activities are in line with *Shariah* principles since *Shariah* is the main component and the foremost salient feature in Islamic banks that differentiates them from conventional banks. Such features include the prohibition of interest and the use of profit sharing investment. Failure to comply with *Shariah* may lead to losses by the Islamic banks since they might not able to recognize the income (IFSB, 2005). The greatest loss that they need to consider is the possibility of losing their investors and investment account holders, who are mostly Muslims, who are really particular about *Shariah* compliance issues and the ethical identity in their dealings.

In addition, a bank's ability to maintain its capital at a sufficient level, as well as its ability to realize rates of return equal to the assumed investment risk is a means of measurement to both shareholders and investment account holders (Mohd Ariffin, Archer and Abdel Karim, 2009). These criteria are important for their evaluation and confidence in making decisions. The lack of such confidence may stop any Muslim from having a business deal with the Islamic banks. In order to prevent the possibility of such incidence, proper disclosure is needed in the financial reports of Islamic banks, which are prepared according to the standards applicable to Islamic banks. As such, studies assessing the strength of the communicated ethical identity of Islamic banks are important since Islamic banks are accountable not only to society but also to God. In addition, transparency in the ethical identity of Islamic banks is essential to society, as it is one of the approaches to ensure the ethical and social activities of Islamic banks. For example, matters pertaining to Islamic bank products, financing activities and community activities.

Due to the extensive and progressive approach to Islamic banking and finance, the Kingdom of Bahrain is chosen for this study as it is acknowledged to be the hub of Islamic banking worldwide and represents the best practice of Islamic banks (Hidayat and Abduh, 2012). Bahrain established its first Islamic bank, Bahrain Islamic Bank, in 1979, and, currently, has 26 Islamic banks, which comprise 6 retail Islamic banks and 20 (twenty) wholesale Islamic banks registered under the Central Bank of Bahrain (Central Bank of Bahrain, 2012). Similarly, Malaysia has also observed progressive and robust development of Islamic banking since 1986 in order to serve the needs of the Malaysian economy as well as enhance the sustainable and economic growth of Malaysia (Bank Negara Malaysia, 2012). Therefore, by comparing the ethical identity disclosure of Malaysian Islamic banks with Bahrain Islamic banks, the position of Malaysian Islamic banks could be identified when compared to the pioneer of Islamic banking. Examining the level of ethical disclosure among Islamic Banks in Malaysia and Bahrain can fill the gap from previous studies where the focus was more on corporate social responsibility disclosure.

Besides determining the level of communicated ethical identity disclosure among Islamic Banks in Malaysia and Islamic banks in Bahrain, this study also examines the determinants of the level of ethical identity disclosure (board size, board independence, *Shariah* Supervisory Board and Investment Account Holders). Therefore, by exploring the ethical identity in Islamic banks, this study would be of interest to the stakeholders since they would perceive banks with higher ethical indent disclosure as being more favorable, especially for Muslim stakeholders as they are very particular about the source of investment.

The remainder of this paper is organized as follows. The next section reviews the relevant literature, which discusses corporate ethical identity. The third section discusses hypothesis development, sampling methodology, data collection and data analysis followed by discussion on the research findings in the fourth section. Finally, the paper ends with a summary and conclusion of the research.

2. Literature review and hypotheses development

Berrone *et al.* (2005) argued that ethical identity is a good investment in business as it can produce a positive environment and have a good impact on the organization, for instance, by exercizing and implementing an ethical code of conduct in the organization, the head of the organization can instill and influence the ethical behavior of the employees. Hosmer (1994) and Jones (1995) claimed that ethical identity could generate a positive atmosphere in the organization like the sense of trust and commitment, and, thus, it can attract more investors as they believe that the ethical identity of the organization is one of the important pillars in order to have successful performance. Further, an organization with a strong ethical identity can maximize the satisfaction of the stakeholder, which would lead to greater achievement by the organization.

Accordingly, Haniffa and Hudaib (2007) argued that Islamic banks have ethical identity, and, therefore, such an institution needs to attain not only its financial goal, but also its social goal since the foundation of Islamic banks is based on religious and *Shariah* principles, the ultimate goal of which is for the betterment of society. In addressing the practice of social reporting, the ethical identity disclosure in Islamic banks should be different from that of conventional banks since the emphasis and the underlying principles in these two banks are different (Haniffa, 2002). In conventional banks, the disclosure of their identity only considers the material and moral aspects, while, in contrast, the Islamic banks need to include the material and moral aspects together with the *Shariah* framework and ensure their alignment with Islamic principles.

By referring to the previous studies, empirically, this study used corporate governance characteristics as a determinant in assessing the factors affecting the ethical disclosure of the Islamic banks. Specifically, the board composition, which comprises three perspectives, namely, board size (Said *et al.*, 2009), board independence (Khan, 2010; Bhasin, Makarov and Orazalin, 2012) and *Shariah* Supervisory Board, as well as Investment Account Holders (Farook, Hassan and Lanis, 2011) are used to assess the ethical identity disclosure of Islamic banks, thus relating each variable to the theoretical assumption.

3. Board size

The board of directors is one of the important elements in corporate governance and is responsible for supervising and overseeing the organization to ensure it is being properly managed. According to Jensen (1993), the larger the number of board members, the more ineffective the communication and coordination of the board and the more likely it is controlled by the CEO. This argument is supported by the agency theory, which proposes that large boards can be costly to the organization due to the increase in the potential conflict and operational complexity among board members, which lead to poor decision making (Lipton and Lorsch, 1992; Jensen, 1993). Ning, Davidson and Wang (2010) suggested that an increase in board size would likely cause an increase in agency problems, which would contribute to internal conflict as well as the free-riding problem among the directors. Said *et al.* (2009) also acknowledged that ineffective communication and inefficiency in decision-making would lead to the low quality of disclosure in financial reporting since the board is not able to perform their role efficiently.

However, Clemente and Labat (2009) claimed that large board size would increase the monitoring capabilities. Due to a significant relationship between the organization and their stakeholder, they tend to increase their disclosure level and release more information, as suggested by the stakeholder theory. In a study by Akhtaruddin, Hossain, Hossain, and Yao (2009), they found that board size is a significant predictor of the voluntary disclosure in Malaysian listed firms, as they found that large board size produced a greater level of voluntary disclosure. Moreover, in Rouf (2011), who studied how corporate characteristics and governance attributes would affect the voluntary disclosure in Bangladeshi firms, the study found there is a significantly positive connection between board size and voluntarily disclosure.In a study concerning the impact of corporate governance on social and environmental information disclosure in Malaysian banks by Htay, Ab. Rashid, Adnan and Mydin Meera (2012), it was found that board size has a positive significant impact on the social and environmental information disclosure as large board size seems to produce a better effect on disclosure in the banking sector. Thus, based on the stakeholder theory, this study expects that there is a positive relationship between board size and disclosure level, which leads to the hypothesis which states:

H1 (a): There is a positive significant relationship between board size and ethical identity disclosure.

4. Board independence

In Jensen and Meckling (1976), according to the agency theory, boards need to be observed and supervized by another party because of the nature of their opportunistic behavior. As the decision experts, independent directors are the ones who suit the role of monitoring and controlling the management performance since they have to be professional and have a positive influence over the director's decision (Fama and Jensen, 1983; Weisbach, 1988). Lim, Matolcsy and Chow (2007) found that independent directors would influence the disclosure level of firms concerning corporate information, as they are a part of the decision making by the board. On the other hand, Ho and Wong (2001) found no significant association between board independence and disclosure due to the low level of compliance in Chinese firms even with the presence of independent directors. In addition, it also supported the findings by Mohd Ghazali and Weetman (2006) who found that board independence has no significant relationship with voluntary disclosure as they discovered that the existence of independent directors on the board of directors could not influence the voluntary disclosure of Malaysian listed companies.

The findings from Mohd Ghazali (2007) and Hossain (2008) showed that board independence is significantly positive towards the disclosure level of the organization, which is consistent with the suggestion by the agency theory that claims that involvement from the board of directors is necessary in order to monitor any self-interest activities by managers. In addition, this theory suggests that a high proportion of independent directors will be able to monitor any self-interest action by the management, and, thus, may encourage the management to disclose more information (Williams, Duncan, Ginter and Shewchuk, 2006). This is consistent with the study by Bhasin *et al*. (2012) who examined the voluntary disclosure determinants in the banking sector of Kazakhstan, and found that board composition has a positive significant impact on the voluntary disclosure by Kazakhstan banks. This is supported by the findings by Htay, Ab. Rashid, Adnan and Mydin Meera (2011) who found that independent directors are one of the significant factors affecting the voluntary disclosure in Malaysian listed banks as they can provide more sources of information to the dependent directors. Consequently, based on the stakeholder and agency theory, this study expects that Malaysian and Bahrain Islamic banks tend to disclose more information on ethical identity with the presence of independent directors as board members:

H1 (b): There is a positive significant relationship between board independence and ethical identity disclosure

5. *Shariah* supervisory board

In this study, the *Shariah* Supervisory Board is included, as the board is one of the corporate elements in Islamic banks and is considered as crucial concerning the level of disclosure in Islamic banks. The *Shariah* Supervisory Board is a unique element in the governance of Islamic banks. In Scott (2004), he explained that the institutional theory is a kind of social structure that has been set up as an authoritative guideline, which consists of schemes, norms and routines to structure the social behavior. Based on this theory, in his paper, Hasan (2009) mentions that the *Shariah* Supervisory Board institution plays a vital role in ensuring that the activities of Islamic banks harmonize with *Shariah* ethics and principles. As the institution that governs the Islamic banks, the *Shariah* board is responsible for guiding and controlling the behavior of organizations so that the interests of society can be protected. Karim (1995) stressed in his paper that the authority of the *Shariah*

Supervisory Board is equal to other conventional auditors since they need to "investigate" whether the Islamic banks adhere to Islamic ethics and *Shariah* principles. According to Farook *et al*. (2011), the nature of *Shariah* compliance is not only based on the assurance of compliance through the *Shariah* Supervisory Board report but also on the greater involvement in social activities as well as the social disclosure. Thus, it is expected that the existence of the *Shariah* Supervisory Board in the governance of Islamic banks would lead to the greater disclosure level of Islamic banks itself.

Farook *et al*. (2011) also stated that the higher the number of the members of the *Shariah* Supervisory Board, the greater the disclosure level of Islamic banks since the ability of the *Shariah* Supervisory Board to monitor the Islamic banks governance also increases. Their study, which examines the *Shariah* Supervisory Board as one of the factors that may influence the corporate social responsibility disclosures in Islamic banks, found that the *Shariah* Supervisory Board is the most significant factor that affects the level of corporate social disclosure. As suggested by the institutional theory, the *Shariah* Supervisory institution plays an important role in influencing the level of disclosure of Islamic banks, as they are a part of the *Shariah* governance, which governs the *Shariah* matters in Islamic banks. Hence, applying the institutional theory, this study proposes that disclosure is positively related to the *Shariah* Supervisory Board of Islamic banks, which can be formulated in the following hypothesis:

H1(c): There is a positive significant relationship between the Shariah Supervisory Board and ethical identity disclosure.

6. Investment account holders

Farook *et al.* (2011) argued that Muslim investors would prefer to make an investment as investment account holders rather than invest their funds as shareholders. This is because they are usually interested in the services offered by Islamic banks compared to the share ownership of that particular bank. However, Archer and Karim (1997) argued with regard to the agency theory that the form of profit sharing loss contract used by Islamic banks in managing and mobilizing the investment account holder's fund might lead to agency problems. Since Islamic banks act as the agent of the shareholders as well as for the Investment Account Holders, this relationship would increase the possibility of having a conflict of interest in dealing with the investment account holders' funds (Archer *et al*., 1998). Pertaining to the Islamic banks risk, *Shariah* compliance is one the important elements in Islamic banks. Therefore, the investment account holders might face the risk of non-compliance with *Shariah*, which may contribute to the agency problem in Islamic banks when the banks fail to meet the obligation of *Shariah* principles (Bank Negara Malaysia, 2010). Therefore, in order to solve these agency problems, adequate disclosure of reporting information, especially information with regard to the *Shariah* compliance, might reduce the occurrence of the agency problem among the investment account holders, since they have enough information to assess the risk (Karim 2001).

Karim (1990) also stated that in the context of the *Shariah* Supervisory Board report, if Islamic banks are going to publish a negative report, the group of investment account holders would begin to doubt the management's commitment towards *Shariah* and they may start to avoid dealing with that particular Islamic bank. As the investment account holders are more interested in the *Shariah* compliance issues in the Islamic banks, the presence of investment account holders could have greater influence concerning the extent of disclosure. Further, in a study by Farook *et al*. (2011), which examines investment account holders as one of the factors that may influence corporate social responsibility disclosure in Islamic banks, it was found that investment account holders are among the significant factors that affect the level of corporate social disclosure. This is consistent with the stakeholder theory that claims the responsibility of Islamic banks towards the investment account holders. As investment account holders are the backbone in the operation of Islamic banks, the banks should strive to meet and maintain the expectation of the investment account holders through ethical identity disclosure. Thus, the final proposition on the relationship between the investment account holder and ethical identity disclosure level could be hypothesized as below:

H2: There is a positive significant relationship between investment account holders and ethical identity disclosure.

7. Research methodology

The sample size of this study consists of 16 Malaysian Islamic banks, which are registered under the Central Bank of Malaysia, and 5 Bahrain retail Islamic banks, which are licensed under the Central Bank of Bahrain (Bank Negara Malaysia, 2011). Currently, the Kingdom of Bahrain has 26 Islamic banks, which comprise 6 retail Islamic banks and 20 wholesale Islamic banks, in which the operation of the retail banks is more towards commercial banks and the wholesale Islamic banks is similar to that of investment banks, merchant banks and other financial institutions that deal with larger institutions. Since Bahrain only has six retail banks, this study only considered five banks because one bank just started their Islamic bank operation in 2010 (Central Bank of Bahrain, 2012).

The main source of this study is based on secondary data that were obtained from the annual reports of Islamic banks from 2007 to 2011, as annual reports are significant and relevant sources, which may communicate the information to all types of stakeholders and enable them to understand the information easily. The list of licensed Islamic banks in Malaysia was obtained from the website of the Central Bank of Malaysia, which lists sixteen Islamic banks comprising ten Islamic local banks and six Islamic foreign banks (Bank Negara Malaysia, 2011). Whereas for the Islamic banks in Bahrain, the list of registered Islamic Banks was obtained from the website of the Central Bank of Bahrain (Central Bank of Bahrain, 2012).

The study used content analysis to identify the items for measuring the ethical identity disclosure practices of Islamic banks. Content analysis is a method of compressing and codifying the text and putting it into various categories based on the criteria for coding (Haniffa and Hudaib, 2007; Weber, 1990; Krippendoff, 2004; Stemler, 2001). The items and categories for the research instrument chosen takes into account the disclosure requirement by the Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI, 1997) and is similar to that developed by Haniffa and Hudaib (2007), and Zubairu, Sakariyau, and Dauda (2011). The Ethical Identity Index developed comprises nine dimensions that consist of 80 constructs, which are Vision and Mission Statement, Board of Directors and Top Management, Product, Zakat, Charity and Benevolent Loan, Employees, Debtors, Community, Environment and *Shariah* Supervisory Board. The possible total score obtained by each of the banks amounts to 80 points.

As for the independent variables, board size is measured according to the number of directors on the board (Said *et al.*, 2009; Akhtaruddin *et al.*, 2009), board independence is measured by looking at the percentage of independent directors to the total number of directors (Chau and Gray, 2010; Huafang and Jianguo, 2007). While the *Shariah* Supervisory Board is measured by looking at the number of members on the *Shariah* Supervisory Board (Farook *et al.*, 2011) and investment account holders (IAH) is measured by dividing the IAH funds to the paid up capital in shareholders' equity (Farook *et al.*, 2011).

The current study also used a control variable, in which the bank's size is measured based on the logarithm of the total assets of the banks at the end of the reporting year (Fungacova and Weill, 2009). According to Heflin and Shaw (2000), in minimizing and reducing the impact of heteroscedasticity and extreme values when analysing the data, the total assets of the banks need to be in the form of natural logarithm (ln). For the second controlled variable, banks' profitability is measured through the return on equity (ROE) of the Islamic banks (Berger and Black, 2011). Finally, the third control variable, country, is measured using a dummy variable where 0 represents Malaysian Islamic banks while 1 represents Bahrain Islamic banks. The usage of country as a control variable was employed in the study of Bashir (2001).

Since content analysis will be used as the method for determining the disclosure level of ethical identity in Islamic banks, the total score for Islamic bank disclosure is computed and expressed in the form of an ethical identity index, as follows (Haniffa and Hudaib, 2007; Zubairu, Sakariyau, and Dauda, 2011):

Model 1:

$$EIIj = \frac{\sum Xij}{nj}$$

where EIIj = Ethical Identity Index

Xij = 1 if *i*th construct is disclosed, 0 if *i*th construct is not disclosed

nj = Number of constructs to be disclosed by banks

Multiple Linear Regression equation analysis is also developed in this study to test whether the four variables chosen could influence the disclosure level of ethical identity disclosure. The relationship between the independent and dependant variables is determined by using this model (Khan, 2010; Farook *et al.*, 2011)

Model 2:

$$EID = \beta 0 + \beta 1BSIZE + \beta 2BINDE + + \beta 3SSB + \beta 4IAH + \beta 5SIZE + \beta 6PROFIT + \beta 7COUN + \varepsilon$$

where

EID = Ethical Identity Disclosure
BSIZE = Board's size
BINDE = Board's independence
SSB = *Shariah* Supervisory Board
IAH = Investment Account Holder
SIZE = Banks' size
PROFIT = Banks' profit
COUN = Country
Bi = Parameter to be estimated
i = 1, 2, 3, 4, 5, 6, 7
ε = Error term

8. Results and discussion

Ethical identity disclosure analysis

Table 1 presents the ethical identity disclosure index for nine dimensions for both the Malaysian and Bahrain Islamic banks. It shows that the overall disclosure for ethical identity for both countries is only 51.7%, which suggests that there is low level of disclosure for both countries.

Table 1. Ethical identity disclosure index.

Ethical identity index	Malaysia	Bahrain	Total mean	Sig.
Vision and Mission statement	47.1%	56%	51.6%	0.001
BOD and top management	62%	76.6%	69.3%	0.000
Product	36.8%	53.6%	45.2%	0.000
Zakāt, charity and benevolent loans	30.1%	49.8%	39.9%	0.000
Employees	62.5%	75%	68.8%	0.000
Debtors	84.4%	71%	77.7%	0.000
Community	38.3%	76.7%	57.5%	0.000
Environment	13.2%	0%	6.6%	0.005
Shariah Supervisory Board	49%	48.7%	48.8%	0.914
Total	**47%**	**56.4%**	**51.7%**	**0.000**

Table 2. Descriptive statistics of ethical identity disclosure determinants.

	Malaysian Islamic Banks		Bahrain Islamic Banks		Total	
Determinants	**Mean**	**Std. Deviation**	**Mean**	**Std. Deviation**	**Mean**	**Sig**
BSIZE (No of member)	7.53	1.646	8.68	1.773	7.8	0.003
BINDE (%)	50.63%	0.133788	48.56%	0.223694	50.14%	0.571
SSB (No of member)	4.20	1.152	4.04	0.935	4.16	0.529
IAH (%)	2001.67%	31.838083	426.73%	3.635097	1626.69%	0.016

Note: EID is Ethical Identity Disclosure. BSIZE is Board Size BINDE is Board Independence. SSB is Shariah Supervisory Board. IAH is Investment Account Holder.

Further, it can be seen that the disclosure of Bahrain Islamic banks is significantly higher (56.4%) than that of the Malaysian Islamic banks (47%). However, even though the level of disclosure of the Bahrain banks is greater than that of the Malaysian banks it is still low as both countries only disclosed about 50% of the disclosure requirements.

Table 1 also illustrates that the most communicated dimension by both banks is the debtors' dimension (77.7%) followed by board of directors and top management dimension (69.3%). While the least communicated dimension is the environmental dimension with 6.6% of disclosure. This implies that neither country prioritizes environmental issues, which, perhaps, is because they considered that environmental issues are not influenced by their operation.

The results further indicated that the Malaysian and Bahrain Islamic banks need to improve their disclosure on vision and mission statement, product, *Zakāt*, charity and benevolent loans, community, environment and *Shariah* Supervisory Board dimension, since the level of disclosure for these dimensions is either below or around 50%.

9. Descriptive statistical analysis

Table 2 shows that, on average, most of the Islamic banks in Malaysia and Bahrain employed about seven to eight members as the members of the board of directors, which is an optimal number for the board size, as having more than that would interfere with the group dynamics (Jensen, 1993). As for the board's independence (BINDE), the mean is 50.14%, which means that half of the board of directors in Islamic banks consists of independent directors. This indicates that the banks have met the corporate governance requirements for Islamic banks. For *Shariah* Supervisory Board (SSB), the results indicate that most of *Shariah* Supervisory Boards in Islamic banks consist of four members. This shows that both countries have complied with the regulators requirement. Finally, the mean for investment account holders of 1626.69% implies that most of the investment account holders in Islamic banks are about sixteen times more than the paid up capital of the Islamic banks.

10. Correlation analysis

Table 3 presents that there is a negative significant correlation between the board size and investment account holders where r is –0.377 at a 1% significance level. This medium relationship indicates that a larger board size would reduce the investment account holders. Table 3 also illustrates that there is a positive significant correlation between board independence and investment account holders, which has a medium strength of relationship, as r is 0.304 at 1% significance. This shows that a large proportion of independent directors would increase the number of investment account holders.

11. Multivariate analysis

In this section, the analysis on the normality test and multicollinearity test will be presented. In order to establish a connection between the independent variables and how

Table 3. Pearson correlation coefficient.

	BSIZE	BINDE	SSB	IAH	SIZE	PROFIT	COUN
BSIZE	1						
BINDE	–0.023	1					
SSB	0.002	0.031	1				
IAH	–0.377**	0.304**	–0.033	1			
SIZE	–0.275**	0.240*	0.336**	0.439**	1		
PROFIT	0.126	0.096	0.019	0.007	–0.137	1	
COUN	0.284**	–0.056	–0.062	–0.236*	–0.809**	0.171	1

**Correlation is significant at the 1% level (2-tailed).
*Correlation is significant at the 5% level (2-tailed).
Note: EID is Ethical Identity Disclosure. BSIZE is Board Size BINDE is Board Independence. SSB is Shariah Supervisory Board. IAH is Investment Account Holder.

they would affect the dependent variable, the multiple linear regression analysis model has been applied in this study as well as the discussion between the independent and dependant variables. Below is the model that has been used in this study together with the regression result.

12. Test of normality

Before running the multiple linear regression analysis, the data was tested for normality and multicollinearity. The Kolmogorov-Smirnov test indicates that the data are not normally distributed. However, according to Pallant (2010), it is common for a large sample size to be abnormally distributed, through which the data violates the assumption of normality, however, it will not cause any serious problem. In addition, according to the Central Limit Theorem, when the sample size is large, more than 30 per group, the sampling distribution will take a normal distribution shape, regardless of the population shape from which the sample is drawn (Field, 2009). Therefore, what can be justified here is that distribution can be converged to the normal distribution for sample study when it involves a large sample size in the study. The data also indicates that there is no collinearity problem as the Variance Inflation Factor (VIF) is not more than ten (Alauddin and Nghiemb, 2010).

Table 4 tabulates the results for Multiple Linear Regression analysis that examines the determinants for ethical identity disclosure. The Durbin-Watson value shows 1.710, which implies that there is no presence of auto-correlation, thereby indicating the data independence between the independent variable and ethical identity disclosure.

Table 4 also highlights that there is a positive significant relationship between the board size (BSIZE) and ethical identity disclosure (EID) of Islamic banks for which the t-value is 2.509 at the 5% significance level, thus accepting hypothesis H1 (a). The finding of this study is supported by Akhtaruddin *et al*. (2009), Rouf (2011) and Htay *et al*. (2012) who found a positive relationship between board size and voluntary disclosure, which suggests that a large board will provide more voluntary disclosure compared to a smaller board.

The findings of this present study are consistent with the stakeholder theory, which claims that the Islamic banks tend to increase their disclosure level and release more information concerning their operations and activities due to the significant relationship between Islamic banks and their stakeholder. Therefore, having a large number of board members would increase the level of disclosure in Islamic banks, which helps the board to satisfy the needs of the stakeholders (Clemente and Labat, 2009). This study implies that board size is one of the important factors in Malaysian and Bahrain Islamic banks as it plays a significant role in influencing the disclosure of the ethical identity by the banks. It can be seen that most of the Malaysian and Bahrain Islamic banks have seven to nine members on the board, which is considered as large enough to have dynamic decision making. Further observation indicates that most of the Islamic banks in Malaysia and Bahrain that have a high-level of disclosure are those banks that have a large board size.

As tabulated in Table 4, the results show that hypothesis H1 (b) is rejected as this study found no significant relationship between the proportion of independent members on the board of directors and ethical identity disclosure. This finding is in contrast with the agency theory that suggests that to influence the decision making as well as monitor and control the opportunistic behavior of management

Table 4. Multiple linear regression analysis: Determinants of ethical identity.

Model	Coefficients	t-value	p-value
(Constant)		−2.855***	0.005
BSIZE	0.196	2.509**	0.014
BINDE	0.025	0.333	0.740
SSB	0.284	3.320***	0.001
IAH	0.235	2.397***	0.008
SIZE	0.609	3.667***	0.000
PROFIT	−0.054	−0.748	0.456
COUN	0.897	6.326***	0.000
R^2		0.529	
Adjusted R^2		0.495	
F-value		15.541	
p-value		0.000	
Durbin-Watson		1.710	
N		105	

*** P-value is significant at the 0.01 level
** P-value is significant at the 0.05 level
Note: Dependent variable - EID is Ethical Identity Disclosure. Independent variables – BSIZE is Board Size BINDE is Board Independence. SSB is Shariah Supervisory Board. IAH is Investment Account Holder. Control variables - SIZE is Banks' Size. PROFIT is Banks' Profit. COUN is Country.

and other board members, independent directors need to be among the board members. This is because, besides incentives, effective monitoring is one of the safeguards that have been proposed to minimize the agency problem that occurs in organizations (Jensen and Meckling, 1976). However, the results corroborate Mohd Ghazali and Weetman (2006), and Khodadadi, Khazami and Aflatooni (2010), as the authors found no significant relationship between board independence and voluntary disclosure in Malaysia and Iranian listed firms. In addition, this study is supported by other findings from Haniffa and Cooke (2002), as they found that the proportion of independent directors could not influence the level of disclosure due to the ineffective monitoring role by the directors.

Hence, the issue that needs to be addressed in the findings of the current study concerns the independence of independent directors as well as their monitoring effectiveness, as most of them are appointed by the Chairman or CEO. This result suggests that most independent directors in Malaysian and Bahrain Islamic banks are not really performing their role effectively and competently in monitoring the performance of Islamic banks. The data collected also show that the proportion of independent directors is similar for most of the banks, and that even banks with the highest and lowest disclosure level are similar in terms of their proportion of independent directors.

Similar to the studies by Hassn (2011), and Farook *et al.* (2011), the regression results in Table 4 further indicate that there is a significant positive relationship between the *Shariah* Supervisory Board and ethical identity disclosure in Malaysian and Bahrain Islamic banks and the relationship, thus accepting hypothesis H1 (c). This finding is consistent with the institutional theory that suggests that to ensure the organization is successful in achieving its goals and objectives, the organizations' corporate governance mechanism must be effective. The institution of the *Shariah* Supervisory Board is responsible for guiding and controlling the conduct and performance of the Islamic banks to ensure that the interests of society are protected. Thus, the existence of the *Shariah* Supervisory Board members may result in greater governance and monitoring, and, consequently, greater compliance with *Shariah* principles by the Islamic banks. Increasing the level of integrity of the *Shariah* Supervisory Board may increase the level of confidence of Muslim society, especially Muslim investors towards the Islamic financial institution.

Similar to the study by Farook *et al.* (2011), further analysis in this study shows that investment account holders (IAH) have a significant positive relationship with ethical identity disclosure in Malaysian and Bahrain Islamic banks; thus, hypothesis H2 is accepted. This finding is consistent with the stakeholder theory, where having greater monitoring by the investment account holders as one of the stakeholders is needed in the Islamic banks to ensure that the investment account holders are managed and mobilized appropriately by the banks. As the Islamic banks need to act as the agent to the investment account holders as well as to the shareholder, the conflict of interest or agency problem would arise. Therefore, the presence of monitoring from investment account holders may reduce the agency problem, and, thus, influence the management of Islamic banks pertaining to the compliance and disclosure issues (Archer *et al.*, 1998). The investment account holders' influence may apply more pressure on the management of Islamic banks to disclose more information as required by the regulators. Thus, by disclosing the ethical identity information, it may establish a connection with the Muslim investor.

13. Summary and conclusion

This study explores the area of ethical identity disclosure, in which emphasis was given to Islamic banks in Malaysia and Bahrain since both countries have a considerably developed Islamic banking industry.Hence, the main objective of this study is to compare the level of ethical identity disclosure of Islamic banks in Malaysia and Bahrain, and also examine the determinants affecting the ethical identity disclosure in these banks.

From the ethical identity index model, it could be seen that the overall disclosure level in both countries is 51.6%, which suggests a low level of disclosure by both countries, since they only disclose 50% of their total disclosure. Further, the overall disclosure shows that the disclosure level of Bahrain Islamic banks is significantly higher (56.4%) than Malaysian Islamic banks (47.1%). The results further indicate that the information in the vision and mission statement; product; *Zakat*, charity and benevolent loans; community; environment; and *Shariah* Supervisory Board dimension need to be emphasized by the regulators as well as the Islamic banks as they are among the least communicated activities by both banks. Since all the dimensions involved in this study portray the identity of Islamic banks as Islamic financial institutions, it needs to be emphasized and highlighted by the management and regulator of Islamic banks. When these dimensions are not appropriately disclosed, it could have a severe impact on the image of Islamic banks as Islamic financial institutions.

Further analysis suggests that independent directors in both Malaysian and Bahrain Islamic banks are not really effective and competent in performing their role in monitoring the performance and activities of the management of Islamic banks, which means the presence of independent directors in Islamic banks does not influence the level of ethical identity disclosure of Islamic banks. While the *Shariah* Supervisory Board is found to be the most significant factor that would influence the level of ethical identity disclosure in Islamic banks. This is consistent with the idea suggested by the institutional theory in which the *Shariah* Supervisory Board is one of the significant means of governance in Islamic banks that needs to supervize and control the Islamic banks activities and performance and ensure that they conform to *Shariah* principles (Hasan, 2009). Thus, the current findings show that the *Shariah* Supervisory Board plays a critical role in influencing the level of ethical identity disclosure in Islamic banks as they could govern the Islamic banks effectively with their expertise.

Further, this study implies that investment account holders are among the monitoring mechanisms that could be applied by the Islamic banks to enhance the disclosure activity of important and relevant information appropriately. As suggested by the stakeholder theory, investment account holders could be a good monitoring tool in observing the activities of Islamic banks. As Muslim investors are particularly interested in the compliance with *Shariah* principles and Islamic law, the management of Islamic banks need to pay extra attention towards this matter, especially when the Muslim investors possess little knowledge about the application of Islamic law in relation to the operation of Islamic banks. Therefore, Islamic banks need to be transparent about this information and let the Islamic investors monitor the banks operation externally. By having this kind of monitoring, greater compliance would be fulfilled by the banks, and, as suggested by Jensen and Meckling (1976), the ownership structure can determine the level of monitoring and thus enhance the level of disclosure. Since Muslim investors are more likely to invest their funds in the *Shariah* investments, the Islamic banks need to carefully manage their operation and ensure that everything is based on *Shariah* law.

Further, board size is found to have a significant influence on the level of ethical identity disclosure in Islamic banks, which is consistent with the stakeholder theory, which claims that the larger the board size, the greater the level of disclosure in Islamic banks; thus the more the stakeholders' needs as well as expectations could be fulfilled by the Islamic banks (Clemente and Labat, 2009).

There are many aspects that could still be explored in future research. As this study used secondary data in examining the level of disclosure in Islamic banks, future research may consider using other methodological approaches, other forms of media as well as improving the research instruments by adding any other aspects that could be used in examining the ethical identity disclosure in Islamic banks. Future studies could also consider comparing the determinants for both countries and identifying which determinants would be more important under different Islamic governance settings.

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