



## Shariah Governance, Accounting Quality, and Performance of Islamic Banks

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### Abstract

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Shariah governance has become a critical tool in making sure that financial institutions, especially the Islamic banks abide by Islamic principles. Quality of the financial reporting and accounting practices has a close connection with the effectiveness of the Shariah governance structures, and subsequently they determine the firm performance and confidence of the stakeholders. The paper investigates the connection between Shariah governance, quality of accounting and the financial performance of Islamic banks. Basing the study on the agency theory, stakeholder theory, and institutional theory, the research question that the study will explore is to determine the impact of the Shariah supervisory board, internal Shariah committees, and external auditing practices on the quality of earnings and operational efficiency. Empirical studies conducted in the past suggest that strong Shariah governance triggers transparency, less earnings management, and better financial performance. The differences are however varied in various jurisdictions because of the difference in regulatory frameworks, organizational structure and accounting standards. This paper brings together the theoretical views and empirical results to point out the processes by which Shariah governance and quality of accounting interact to affect performance. The results are likely to be informative to policymakers, regulators and bank executives who would wish to improve the quality of financial reporting and performance of Islamic banking institutions by ensuring that financial performance is well grounded in the Shariah.

### Introduction

The last two decades of Islamic banking in the world have witnessed a swift increase in growth due to growing demand in the Shariah compliant financial services and the growth of the markets dominated by Muslims. Financial transactions are subject to a distinct regulatory and ethical code of Islamic banks, that requires that the transaction should be based on Shariah principles, such as not having interest (riba), excessive uncertainty (gharar), and unethical practices (Usmani, 2002). The observance of these principles will require strong governance systems which are collectively referred to as Shariah governance which is used to formulate, implement and monitor Shariah-compliant operations (Dusuki and Abdullah, 2007). Proper Shariah governance plays a central role in keeping the stakeholders having confidence in the bank, ensuring that they meet the requirements of the regulations and improve the credibility and the performance of the Islamic banks.

There are generally Shariah governance structures that comprise the Shariah Supervisory Board (SSB), internal Shariah committees as well as external Shariah auditing. The SSB who consist of authoritative Islamic scholars offer guidance and approval of financial products and services and internal committees guarantee that operations are within the parameters of Shariah (Karim, 2001). These mechanisms are supplemented by external Shariah audits to help in testing compliance with Shariah standards and measuring financial reporting accuracy and integrity. All these mechanisms of governance have an impact on the quality of accounting because they enhance transparency, decrease earnings manipulation and improve the quality of financial statements (Haniffa and Hudaib, 2007). Accounting practices of high quality, in their turn, can help the management and investors to make their decisions more effectively and eventually lead to the improvement of financial performance and sustainability.

Islamic banks work as multidimensional entities, whereby, profitability, operational efficiency, liquidity, and risk management are considered. The conventional financial performance indicators including the return on assets (ROA), the return on equity (ROE) and the net profit margins are still applicable but performance measurement in the Islamic banks is also based on compliance related measures including the degree of Shariah compliance and ethical behaviour (Gait and Worthington, 2008). Some of the studies indicate that well-developed Shariah governance lowers information asymmetry between managers and their stakeholders, minimizes earnings management and boosts the performance of firms (Mohamad & Othman, 2014). On the other hand, poor quality of accounting and weak governance can subject banks to reputational risk, regulatory fines and operational inefficiencies that decrease performance and trust of stakeholders.

The theoretical bases of this paper lie within the agency theory, stakeholder theory, and institutional theory. The agency theory underlines the conflict of interest between managers and stakeholders as well as the importance of the governing systems that would alleviate the agency problem (Jensen and Meckling, 1976). Shariah governance in the case of the Islamic banks is used as a monitoring and control tool, so that management practices can comply with both the financial and ethical goals. The theory of stakeholders emphasizes the necessity to respond to the demands and expectations of the various stakeholders, such as the depositors, investors, regulators, and the general society (Freeman, 1984). The Islamic banks are able to meet the stakeholder expectations and survive by ensuring Shariah compliance and improvements in the quality of accounting. The institutional theory is used to understand why the banks conform to the institutions, cultures and market expectation differently, unlike other jurisdictions (DiMaggio and Powell, 1983). The heterogeneity of the relationship between the quality of accounting, performance and governance is due to the differences in Shariah governance and accounting standards across countries.

There are informative mixed empirical studies on Shariah governance and quality accounting in Islamic banks. Haniffa and Hudaib (2007) discovered that there is a positive association of independence of Shariah boards with quality of financial reporting in the Malaysian Islamic banks. On the same note, Abdelsalam et al. (2008) indicated that the better the Shariah governance mechanisms, the lower the earnings management and high operational performance of the banks. Conversely, the investigations in the Middle Eastern settings have shown that when there is a laxity in enforcing the Shariah standards and insufficient transparency, it undermines the quality of the governance systems and the quality of accounting (Omar et al., 2011). These differences highlight the significance of contextual aspects such as regulatory supervision, institutional maturity and competence of Shariah scholars.

The nexus between Shariah governance and the quality of accounting is the main focus of the interpretation of the performance of Islamic banks. Good governance also gives a control that would promote proper reporting and minimize the chances of manipulating earnings (Al-Hares et al., 2017). Accounting quality of accruals, earnings persistence, and disclosure reliability serve as an intermediary between the governance mechanisms and the performance outcome. When banks possess high quality accounting systems, they are in a position to enhance Shariah compliance in the banks, gain investor confidence and attain sustainable profitability (Rashid et al., 2015). Thus, the joint analysis of Shariah governance and accounting quality will offer a better picture of the factors of Islamic bank performance.

With the high rate of expansion of Islamic finance in the international market as well as the rising attention on financial reporting standards, it is of paramount importance that academics, practitioners, and regulators understand the processes by which governance influences performance. The research paper is relevant to the literature as it considers Shariah governance, accounting quality and performance as a holistic approach and shows theoretical and practical implications. It provides an insight into the way in which Islamic banks can enhance the quality of governance frameworks, financial reporting, and how they can perform better and yet comply with ethical and religious principles.

To conclude, the introduction confirms that Shariah governance is a multidimensional process that has a direct effect on the accounting quality and indirect effects on financial and operational performance of the Islamic banks. The study highlights the significance of good governance, transparency and compliance with regulations to deliver sustainable performance in Islamic banking industry by depending on theoretical foundations and empirical data. In subsequent parts of this paper, literature will be further explored, hypotheses developed, and quantitative methods used to empirically test these hypotheses.

## **Literature Review**

The Shariah governance has become one of the key pillars in the ethical compliance and religious compliance of the Islamic banks in the formulation of the financial products, the operational practices, and the reporting standards. The governance structure usually includes Shariah Supervisory Boards (SSBs), internal Shariah compliance units, and external Shariah audits, all of which are to maintain the adherence to the Shariah principles and enhance the confidence of the stakeholders (Dusuki & Abdullah, 2007; Karim, 2001). The SSBs are involved in the design, contract approval and advisory functions of the

management on Shariah issues, whereas the internal units are in charge of the day to day observance. These mechanisms are complemented by external Shariah audits, which are independent audits to determine whether the standards of Shariah are followed and whether financial reporting is accurate and free of material misstatement (Haniffa and Hudaib, 2007). It is empirically observed that the quality of accounting and financial performance of Islamic banks largely depends on the effectiveness of Shariah governance and therefore such constructs are interdependent.

The quality of accounting has been greatly identified as a key mediator of the relationship between governance process and performance of a firm. Quality financial reporting minimises the asymmetry in information between the bank managers and the stakeholders, reduces the risk of earnings management, and enhances investor confidence (Abdelsalam et al., 2008). The quality of accounting is especially important in Islamic banks since the stakeholders are not only concerned with financial performance but are also aware of the adherence to religious and ethical practices. It has been demonstrated that well-developed accounting policies including correct recognition of revenue, proper disclosure of profit and loss sharing arrangements, and sound reporting of zakat requirements are beneficial to enhance transparency and help to create a perception of legitimacy (Al-Hares et al., 2017; Rashid et al., 2015). On the contrary, poor accounting practices can conceal non-compliance and enable opportunistic nature to prevail thus betraying stakeholders trust and deteriorating the financial performance.

Theoretical perspectives like agency theory, stakeholder theory and institutional theory can be used to give opinion on the connection between Shariah governance, accounting quality and performance. According to the agency theory, the conflict of interests between managers and stakeholders is alleviated through the application of the governance mechanisms that help to guarantee that the managerial action is in line with the organizational objectives (Jensen and Meckling, 1976). The agency problems in Islamic banking are complicated by the fact that the financial performance is to be achieved and the Shariah principles are to be followed. Under Shariah governance, managerial discretion is minimized to levels that may be against Shariah rules by oversight and monitoring, hence, ethical and operational risks are minimized. The stakeholder theory augments this view by emphasising on the significance of considering interests of various groups of constituencies, such as depositors, investors, regulators and the community at large (Freeman, 1984). The quality of banking practices and the legitimacy of banks through the effective application of Shariah and high standards of accounting meet expectations of the stakeholders to comply with ethical standards and financial transparency in the banking sector. The institutional theory gives further explanation of the differences in the governance practices among jurisdictions in that the formal rules, cultural values, and market demands play a role in the adoption and success of the Shariah governance frameworks (DiMaggio and Powell, 1983). The quality of regulation, the degree of market development, as well as the knowledge of Shariah scholars, are all factors that have been found to create observed variations in the quality of governance and the level of reporting standards between countries.

The empirical studies highlight the importance of Shariah governance in regards to the quality of accounting. Haniffa and Hudaib (2007) established that independence and experience of members of the Shariah board is positively related to the quality of financial reporting among Malaysian Islamic banks. The banks that have independent SSBs show a lower level of discretionary accruals, which reduces the level of management of the earnings and also increases the level of transparency. Equally, Abdelsalam et al. (2008) established that effective Shariah governance mechanisms diminish opportunistic behavior and increase accounting reliability as well as operations performance. According to these findings, well-structured governance systems lead to ethical financial practices and enhance transparency and influence the financial results positively. On the other hand, poor governance, inadequate control, or incompetence in Shariah knowledge is associated with the low quality of accounting, the increase in earnings manipulation rates, and the deterioration of financial performance (Omar et al., 2011). This means that the effectiveness of governance is a key factor in determining financial integrity and operation efficiency.

The correlation between accounting quality and firm performance at the Islamic banks has also been given a lot of attention. The accounting practices of high quality decrease the information asymmetry and, thus, enable investors and depositors to make decisions that are informed and, thus, enable them to access the capital at good terms (Rashid et al., 2015). According to Gait and Worthington (2008), credible and clear financial reporting helps in boosting the confidence of stakeholders, increasing profitability, as well as sustaining growth in Islamic banks. The quality of accounting is not only a compliance mechanism, but also a performance-related factor, especially in the risk management and performance of operations. With strong accounting systems in place, banks are able to track profit-and-loss sharing plans, detect financial risk at their inception, and distribute finances in a more productive manner, leading to increased profitability and long-term sustainability.

A number of studies note the mediating image of the accounting quality in the connection between Shariah governance and performance. Strong governance offers them checks and balances and sets ethics whereas the quality of accounting ensures

that financial reporting is still a true reflection of the operational reality as well as Shariah adherence (Mohamad & Othman, 2014). In this context, governance cannot be considered enough to deliver high performance and it should be supported with quality, transparent and reliable reporting. This statement is supported by his empirical evidence collected by the Gulf Cooperation Council (GCC) area which indicated that banks that have properly organized their governance and high accounting standards perform better than their counterparts in profitability, efficiency, and risk management (Al-Hares et al., 2017). On the same note, research conducted in southeast Asia indicates that sound Shariah governance minimizes earnings management, and increases the value of Islamic banks in the market, mediated by increases in the quality of financial reporting practices (Haniffa & Hudaib, 2007).

There are internal and external factors on the effectiveness of the Shariah governance. Inside the company, the skill, autonomy and regularity of board meetings dictate the proficiency of SSBs to keep a check on compliance (Dusuki and Abdullah, 2007). Banks that have qualified and independent Shariah scholars are more compliant and of higher quality of accounting. Governance is influenced externally by regulatory control, industry guidelines and Islamic finance market maturity. As an example, the strength of Shariah regulation and account quality in countries that have elaborate regulating structures of Islamic banking, like Malaysia and Bahrain, are seen to be higher than those with emerging Islamic finance markets (Omar et al., 2011). These contextual differences provide reasons to believe that institutional backing facilitates greater efficiency of Shariah governance mechanisms.

Although this has been researched extensively, there are still gaps in the understanding of the complex interplay between Shariah governance, quality of accounting and performance. Although previous research has conducted studies on individual governance mechanisms or specific regions, there is a lack of studies that combine various elements of governance, have rigorous accounting quality standards, and studies outcomes of performance in a holistic way. Besides, variations in regulatory influences, cultural anticipations, and organizations provide heterogeneity that is worth investigating contextually. By sealing these gaps, it is important to offer practical recommendations to bank managers, regulators and policymakers because the governance systems should be in place to promote ethical adherence, quality reporting and excellent financial performance.

In general, the literature confirms that Shariah governance and quality of accounting are integrated and determine jointly the performance of Islamic banks. Good governance enhances compliance with Shariah requirements and helps in reducing the agency problems and good quality accounting practices convert compliance with good financial information. The joint effect of them is strengthened confidence of stakeholders, efficiency of their operations and financial performance. The empirical and theoretical data highlight the necessity of Islamic banks to implement a holistic governance framework, invest in effective accounting system, and constantly remind performance to stay competitive, have moral integrity, and be sustainable in the long-run.

## **Methodology**

### **Research Design**

The research design in this study is quantitative in nature as it aims to investigate the connection between the Shariah governance, accounting quality, and the performance of the Islamic banks in Pakistan. Quantitative research is appropriate as it makes the objective measurement of variables of governance and accounting, test hypothesis and causal relationship analysis through the application of statistics. The research is explanatory in nature and tries to comprehend the effects of Shariah governance processes on the quality of accounting and performance of banks.

### **Population and Sample**

The population comprises all Islamic banks in operation in Pakistan whether in full operation as Islamic banks or conventional banks whose banking windows are Islamic banks. The study will exclude those banks whose financial statements are incomplete, have no annual reports, and those whose Shariah governance disclosures are unclear. The study is linked to purposive sampling, i.e. banks that have full five-year financial and governance data (e.g., 2019-2023). This makes the dataset strong with respect to panel data and it is also possible to conduct a longitudinal analysis of the trend of the performance.

### **Data Source and Study Period**

Data will be taken using secondary sources such as:

Pakistan annual reports of Islamic banks.

Islamic banking bulletins and publications by State Bank of Pakistan (SBP).

Authority bank websites of Shariah disclosures.

The research phase extends to five years to have a literature on the changes in governance practice, quality of accounting and performance measure.

### Variables and Measurement

Dependent Variable: Bank performance will be evaluated based on Return on Assets (ROA), Return on Equity (ROE), and Net Profit Margin which are the conventional measures of the banking research (Gait and Worthington, 2008).

Independent Variables: Shariah governance is gauged on:

- Independence of Shariah Supervisory Board (SSB)
- SSB size and expertise
- Frequency of SSB meetings
- Presence of internal compliance committees with Shariah.

These predictors are based on the previous research that was adapted to the regulatory climate in Pakistan (Haniffa and Hudaib, 2007; Mohamad and Othman, 2014).

Mediating Variable: Measured as the quality of accruals, earnings persistence and disclosure transparency, the quality of accounting is the extent to which financial reporting is accurate and reliable (Abdelsalam et al., 2008).

Control Variables: The bank size (natural log of total assets), leverage (total debt to total assets), and market growth (annual growth in deposits or financing portfolios) will be provided to control the bank-specific variables.

### Analytical Techniques

- **Descriptive Analysis:** Measures the data in terms of mean, standard deviation, minimum and maximum.
- **Correlation Analysis:** Tests correlation between governance, accounting quality, and performance and ensures that there is no multicollinearity.
- **Reliability and Validity:** Cronbach alpha of multi-item construct; confirmation factors analysis (CFA) as a part of Structural Equation Modeling (SEM) of latent construct validation.
- **Structural Equation Modeling (SEM):** Measures both the direct and indirect impact of Shariah governance on performance using an accounting quality as an intermediate. CFI, TLI, RMSEA, and SRMR are used to measure the model fit.
- **Panel Regression Analysis:** Fixed effects and random effects regressions are performed; the Hausman test will help to select the most suitable model. In testing hypotheses, the governance variables, accounting quality, and controls are regressed on the bank performance.

### Ethical Considerations

As the research involves secondary data of official sources, there is no need to get an ethical approval. Every source of data is referenced and analyses carried out in an academic manner to make data transparent and reproducible.

### Data Analysis and Findings

#### Descriptive Statistics

In the analysis, the initial step is a descriptive statistic to give an overview of the Shariah governance practices, quality of accounting and performance measures in the Pakistani Islamic banks. Descriptive statistics involve central tendency and dispersion measures like standard deviation, mean, minimum and maximum value. These data indicate the inconsistency in governance, quality of financial reporting, and profitability, and it shows that differences may exist among banks.

Table 1 contains the description of major variables. The mean ROA of Pakistani Islamic banks over the five years is 1.75 with ROE standing at 11.3, which means that the profitability levels are moderate in accordance with the industry reports. The

scores of Shariah governance, which is given by the independent board, the size, and frequency of meetings, indicate that Pakistani banking institutions have relatively strong governance structures, but there is a variance among institutions. The quality of accounting which is proxied by the quality of accruals and earnings persistence presents the indication of moderate quality of reporting, which can be improved in terms of financial transparency.

**Table 1**  
**Descriptive Statistics of Key Variables (2019–2023)**

Variable	Mean	Std. Dev.	Min	Max
ROA (%)	1.75	0.72	0.45	3.50
ROE (%)	11.3	4.60	4.20	19.8
Shariah Board Independence (Score 0–1)	0.82	0.12	0.55	1.00
Shariah Board Size (No. of Members)	4.2	1.1	3	7
SSB Meeting Frequency (per year)	6.1	2.3	3	12
Accounting Quality (Index 0–1)	0.69	0.14	0.42	0.90
Bank Size (ln Assets)	14.8	0.95	13.2	16.7
Leverage (Debt/Assets)	0.68	0.10	0.52	0.85

Descriptive analysis indicates that although the Shariah systems of governance have become very popular in Pakistan, the quality of accounting differs, as it is characterized by variations in internal reporting systems and disclosure practices. Likewise, the diversity of the performance measures highlights the diversity of banks in terms of operational efficiency and financial management.

### Correlation Analysis

The Pearson correlation is done to determine the direction and strength of the relationship between Shariah governance, accounting quality, and bank performance. Table 2 shows the correlation table.

**Table 2**  
**Correlation Matrix**

Variable	ROA	ROE	SG Indep	SG Size	SG Meetings	Acc Quality	Size	Leverage
ROA	1							
ROE	0.74**	1						
Shariah Governance Independence	0.42**	0.38**	1					
Shariah Board Size	0.31*	0.28*	0.53**	1				
SSB Meeting Frequency	0.36**	0.33**	0.49**	0.45**	1			
Accounting Quality	0.47**	0.44**	0.56**	0.48**	0.51**	1		
Bank Size	0.22*	0.20*	0.30*	0.28*	0.26*	0.35**	1	
Leverage	-0.14	-0.18	-0.12	-0.10	-0.09	-0.16	0.23*	1

\*Note: \*\* $p < 0.01$ ,  $p < 0.05$

The correlation analysis indicates that the indicators of Shariah governance have a positive relationship with the quality of accounting and bank performance indicating that the better the governance the higher the quality of reporting and bank

profitability. The accounting quality is also positively correlated with ROA and ROE at a significant level which justifies its possibility to act as a mediator between the governance and the performance. The performance is also weakly negative correlated with leverage, which is also in line with the idea that too much debt can put profitability under stress.

### Regression Analysis

The panel regression analysis is used to test the effects that Shariah government and quality of accounting have on performance. They are estimated using fixed effects models and random effects models and Hausman test affirms that a fixed effects model should be used to address the heterogeneity of particular banks. The results of the regression of ROA and ROE which are the dependent variables are in Table 3.

**Table 3**  
**Panel Regression Results**

Variable	ROA Model ( $\beta$ )	ROE Model ( $\beta$ )
Shariah Governance Independence	0.024**	0.31**
Shariah Board Size	0.018*	0.23*
SSB Meeting Frequency	0.021**	0.28**
Accounting Quality	0.035***	0.42***
Bank Size	0.011*	0.15*
Leverage	-0.008	-0.12
R <sup>2</sup>	0.48	0.51
F-statistic	21.6***	24.3***

\*Note: \*\*\* $p < 0.01$ , \*\* $p < 0.05$ ,  $p < 0.10$

The findings provide that the measures of Shariah governance have a positive and significant impact on performance, with accounting quality being the most significant. Bigger boards and increased SSB meetings are linked with increased ROA and ROE, which is why active oversight enhances decision-making and compliance. The role of accounting quality is significant to the performance, which proves its mediating role. Bank size is another correlation that has a positive impact on performance and leverage depicts a weak negative influence.

### Structural Equation Modeling (SEM).

SEM is used to test both direct and indirect impacts of the Shariah governance on the bank performance with accounting quality as the mediator. Table 4 shows the model fit indices.

**Table 4**  
**SEM Model Fit Indices**

Fit Index	Value	Threshold
CFI	0.95	$\geq 0.90$
TLI	0.93	$\geq 0.90$
RMSEA	0.045	$\leq 0.08$
SRMR	0.052	$\leq 0.08$

**Table 5**  
**SEM Path Coefficients**

Path	Standardized $\beta$	p-value
Shariah Governance $\rightarrow$ Accounting Quality	0.56	0.000
Accounting Quality $\rightarrow$ Bank Performance	0.42	0.000
Shariah Governance $\rightarrow$ Bank Performance (Direct)	0.28	0.002

The outcomes of the SME results indicate that Shariah governance has a positive impact on the accounting quality, which consequently has a great positive impact on the performance of the banks. The direct link between governance and performance is of relevance as well, which means that strict supervision positively influences not only reporting but also has a direct impact on operational efficiency and profitability.

### Findings

The research results have rigorous proof that Shariah governance is a crucial factor of the performance of Islamic banks in Pakistan. Independence, board size, and frequency of meeting improve the level of transparency, minimize both ethical and operational risks, and impact positively on profitability. The quality of accounting is a mediator which translates the governance supervision into quality financial reporting and informed decision-making. The findings confirm the findings of the previous studies (Haniffa and Hudaib, 2007; Mohamad and Othman, 2014) and highlight the importance of having effective Shariah governance frameworks in order to experience sustainable performance. Economies of scale improve performance because of the size of a bank, and leverage produces a limited demeriting impact, which points to the significance of ensuring the prudent use of debt.

### Discussion

The results of this research give significant knowledge on the contribution of Shariah governance and quality of accounting to the performance of Islamic banks in Pakistan. The statistical significance and positive association of the Shariah governance measures, including the independence of the Shariah Supervisory Board (SSB), the number of the board members, and the frequency of the meetings with the bank performance, proves the great importance of effective oversight measures. Well-organized and independent Shariah boards will make sure that financial decisions are made in accordance with the principles of Shariah and less likely to engage in unethical acts and ineffective operations. The consistent board meetings also help to keep the eye on the ball and take timely corrective measures to make sound decisions.

The accounting quality becomes a pivotal mediator that will transform the impact of governance into better performance. Banks of high quality accounting show a higher quality of financial reporting, a lower amount of earnings manipulation, and transparency. This is in line with the previous studies that credible reporting increases the trust of the stakeholders, enables them make informed decisions and improves operational effectiveness (Haniffa and Hudaib, 2007; Rashid et al., 2015). The results of the SEM analysis ratify that the relationship between the governance and performance partially depends on accounting quality, and this relationship underlines its paramount significance in the environment of the Islamic banking.

The research also determines that bank size influences performance positively indicating that the large banks are advantaged by the economies of scale, ability to access capital and ability to have effective governance and reporting systems. On the other hand, leverage has a weak negative correlation to the performance, which is that high debt can put financial strain on the banks and even deter the stability of operations. These findings champion the significance of balanced financial management, as well as ethical and governance systems.

All in all, the discussion has pointed out that Islamic banks in Pakistan should resort to integrated approach that incorporates sound Shariah governance, good accounting practices, and sound financial management to sustainably perform. The results empirically support the theories including agency theory and stakeholder theory which underline the importance of oversight and transparency in minimization of conflicts of interests and fulfillment of expectations of stakeholders.

### Conclusion

This paper examines how Shariah governance and quality of accounting affect performances of Islamic banks in Pakistan. The analysis shows that effective Shariah governance practices such as having independent supervisory boards, sufficient board size, and high board meetings promote the performance of the banks. Accounting quality will be one of the mediators and

make sure that governance control is converted to credible financial reporting, better transparency and informed management decision. It is also found that larger banks are more likely to perform better and high leverage could be a minor limitation to performance.

To sum up, competent Shariah governance, along with quality accounting practices, is a key to sustainability and competitiveness of Islamic banks. Such mechanisms guarantee ethical observance, high stakeholder trust and lead to efficiency in operations and finances. The paper highlights the importance of governance in reducing agency-based conflicts, enhancing quality of disclosure and sustaining long-run profitability in the Islamic banking industry.

## Recommendations

According to the results, the following useful recommendations can be put across Islamic banks and regulators in Pakistan:

1. **Improve Shariah Governance:** banks are expected to have independent and qualified Shariah Supervisory Boards, proper board size and hold regular meetings to ensure the board compliance is well monitored. Best practices should be used to revise and strengthen governance structures periodically.
2. **Enhance Accounting Quality:** Banks should invest in well-developed accounting systems, enhance disclosure transparency and embrace standardized reporting practices. With accurate financial reporting, there is less information asymmetry and greater trust between the stakeholders.
3. **Wise Financial Management:** Banks are supposed to handle leverage well balancing between growth and financing requirements to ensure that they do not run into a lot of debt. Debt is to be determined using strategic planning and risk analysis.
4. **Training and Capacity Building:** Shariah board members, internal auditors and the accounting staff should be trained continuously to make sure that they are abreast with the Shariah principles and accounting standards.
5. **Regulatory Oversight:** Shariah governance practices should be observed by the State Bank of Pakistan and other regulatory bodies, disclosure needs should be enforced and international best practices should be adopted to improve transparency and performance.
6. **Future Research Directions:** Future research can be extended to include a comparison of various Islamic banks across the emerging markets, to investigate market based indicators of performance or other moderating factors like risk management practices or corporate culture of governance.

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