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Development of Islamic Accounting Sustainability Model

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Abstract

Purpose – The model of Islamic accounting development on ESG (Environmental, Social, and Governance) aims to promote sustainable accounting practices that reflect Islamic principles in asset and investment management. ESG emphasizes the social and environmental responsibility of companies, as well as good corporate governance. Design/methodology/approach – Literature research is included in qualitative research methods. To conduct Islamic accounting research in Environmental, Social, and Governance (ESG) literature. This research was conducted by the SLR method or systematic literature review by collecting data through the PRISMA method sourced from the Scopus database. Findings – Finding research era of sustainability and developing sustainable economic and accounting models are increasingly important to create an economy that balances social, economic, and environmental welfare. Sustainable Islamic economics and ESG are two complementary approaches to achieving this goal. In this context, the Islamic accounting model in ESG can be a solution to achieve holistic sustainability goals. Theory implications – The emphasis on environmental, social, and governance aspects in the ESG model expands the scope of Islamic accounting. This model not only focuses on the dimensions of Islamic compliance but also takes into account the social and environmental impacts of business activities. Originality/value- This model integrates Islamic and ESG accounting principles, allowing companies to apply sustainability values in their operations and improve their sustainability performance.

Keywords: *Islamic Accounting, Sustainability, ESG.*

Introduction

The development of Islamic accounting models in ESG stems from demands for sustainability and awareness of the importance of taking into account environmental, social, and governance aspects in business activities (Aldowaiish *et al.*, 2022; Sultana, S., Zulkifli, N., & Zainal, 2018). The concept of ESG has become increasingly important in business and investment, as stakeholders increasingly realize the importance of taking into account non-financial aspects in decision-making (Kotsantonis *et al.*, 2016). On the other hand, Islamic accounting principles have long been the basis for Islamic business practices that prioritize fairness, openness, and transparency in doing business (Kamla, 2009). These principles are also highly relevant to sustainability values, such as social justice, a

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healthy environment, and good governance(Leach *et al.*, 2010).

Therefore, the development of an Islamic accounting model in ESG is an effort to integrate Islamic accounting principles and sustainability values in company operations and investment decision-making(Alazzani *et al.*, 2019; Daugaard, 2020) (Buallay *et al.*, 2020). This model creates a holistic and inclusive framework for measuring a company's sustainability performance and provides stakeholders with complete information on how companies consider environmental, social, and governance aspects in their operations(Adams and Abhayawansa, 2022; Lokuwaduge and Heenetigala, 2017; Muñoz-Torres *et al.*, 2019; Rajesh, 2020). In this context, the development of Islamic accounting models in ESG can help companies to make more sustainable decisions and provide broader benefits to society and the environment(Alkaraan *et al.*, 2022; Arayssi *et al.*, 2020; Dremptic *et al.*, 2020). The model can also promote fairer, transparent, and socially responsible business practices, which are core values in Islamic accounting and ESG(Gangi *et al.*, 2021; Neves, M. E., Santos, A., Proença, C., & Pinho, 2022).

The development of Islamic accounting models in ESG is also an attempt to correct weaknesses in conventional accounting practices, which often ignore or minimize non-financial aspects in a company's financial statements(Al-Haija *et al.*, 2021; Veltri *et al.*, 2023). In conventional accounting models, non-financial aspects are often perceived as irrelevant or insignificant costs in business decision-making (Kotsantonis *et al.*, 2016). However, with the Islamic accounting model in ESG, non-financial aspects are seen as an integral part of a company's operations and should be considered holistically in business decision-making (Tsagas & Villiers, 2020; Mio *et al.*, 2022) This model also places importance on fairness and openness in corporate financial statements. Companies must provide clear and transparent information about their business practices, including how they consider environmental, social, and governance aspects in their operations (Camilleri, 2021)

Yet, the development of Islamic accounting models in ESG also faces challenges, such as difficulties in consistently measuring and objectively measuring a company's sustainability performance consistently and objectively (Khaled *et al.*, 2021) (Alam *et al.*, 2022b). There are also challenges in applying Islamic accounting principles that can vary depending on the interpretation and perspective taken (Mohammed *et al.*, 2019).

Nonetheless, the development of Islamic accounting models in ESG promises great potential in developing more sustainable and socially responsible business practices (Paltrinieri, A., Dreassi, A., Migliavacca, M., & Piserà, 2020; Raghunandan and Rajgopal, 2022). In an increasingly complex and changing business environment, this model can assist companies in better decision-making and assist stakeholders in understanding how companies consider non-financial aspects of their operations(Evangelinos *et al.*, 2015; Wu *et al.*, 2022).

ESG (Environmental, Social, and Governance) is a concept related to measuring company performance in terms of environmental, social, and good governance(Huang, 2021; Mooneeapen

et al., 2022; Puriwat and Tripopsakul, 2022). This covers various aspects such as waste management, occupational health and safety, anti-corruption policies, and corporate social responsibility (Branco and Delgado, 2012; Lindman *et al.*, 2020). ESG concepts are increasingly being applied in investment and finance, as more investors want to invest in companies that perform well, and more companies realize that sustainability is the key to long-term success (Adams and Abhayawansa, 2022; Busch *et al.*, 2016; Sciarelli *et al.*, 2021).

In Islamic accounting, the concept of ESG is in line with the principles of Islamic economics that encourage sustainable economic development and are environmentally and socially oriented (Al-Haija *et al.*, 2021; Khan, 2019). In Islamic accounting, ESG concepts can be applied in several aspects (Lee and Isa, 2023; Ma'ruf *et al.*, 2021): (1) Environment: Islamic accounting principles encourage sustainable and environmentally oriented economic development. Therefore, companies can develop policies and strategies to reduce the environmental impact of their operations, such as reducing greenhouse gas emissions or using renewable energy (Sharmeen *et al.*, 2019). (2) Social: Islamic accounting principles also encourage companies to be socially responsible and contribute to the development of society (Amran *et al.*, 2017). Therefore, companies can develop policies and strategies to improve people's welfare through social programs or donations to charity. (3) Good governance: Islamic accounting principles also emphasize the importance of good governance in a company's operations. Hence, companies must develop good governance policies and practices, such as good anti-corruption, transparency, and accountability (Hopper, 2017; Jamil *et al.*, 2021). In practice, the application of ESG concepts in Islamic accounting can be made through the development of sustainability reports or social and environmental reports, which include company performance in ESG aspects. Manuscripts can help companies monitor and improve their ESG performance and provide more complete and transparent information for investors and other stakeholders. The purpose model of Islamic accounting development on ESG (Environmental, Social, and Governance) aims to promote sustainable accounting practices that reflect Islamic principles in asset and investment management. ESG emphasizes the social and environmental responsibility of companies, as well as good corporate governance.

Method

Literature research is included in qualitative research methods. This method collects data from written sources such as books, journal articles, reports, and other sources related to the research topic (Bowen, 2009; Sileyew, 2019). The literature approach in qualitative research helps obtain a comprehensive understanding of a particular topic, as well as compare research results from previous studies (Nowell, L. S., Norris, J. M., White, D. E., & Moules, 2017). The literature approach is a research method that collects data from written sources such as books, journal articles, reports, and other sources related to the research topic. This approach helps gain a comprehensive understanding of a particular topic and compare research results from previous studies. A systematic approach to identifying, evaluating, and synthesizing relevant research in a particular field. This research was conducted by the SLR method or systematic literature review by

collecting data through the PRISMA method sourced from the Scopus database.

The literature approach in Islamic accounting research is instrumental in gaining a comprehensive understanding of a particular topic, as well as comparing research results from previous studies. However, as mentioned earlier, it is essential to make a selection of relevant and high-quality literature and conduct a critical evaluation of the literature sources used. To conduct Islamic accounting research in Environmental, Social, and Governance (ESG) in literature, several methods can be done 1) Descriptive Literature Study, which involves analysis of literature and publications related to Islamic accounting and ESG. Researchers can evaluate the theories, concepts, and views of experts who have applied Islamic accounting principles in the context of ESG. 2) Document Analysis Method is a method that involves the collection and analysis of documents such as policies, standards, and guidelines related to Islamic accounting and ESG. Researchers can evaluate the extent to which these documents support the application of Islamic accounting principles in the context of ESG.

Results and Discussion

Result

As for the results of processing SLRs using Prisms, the following are obtained:

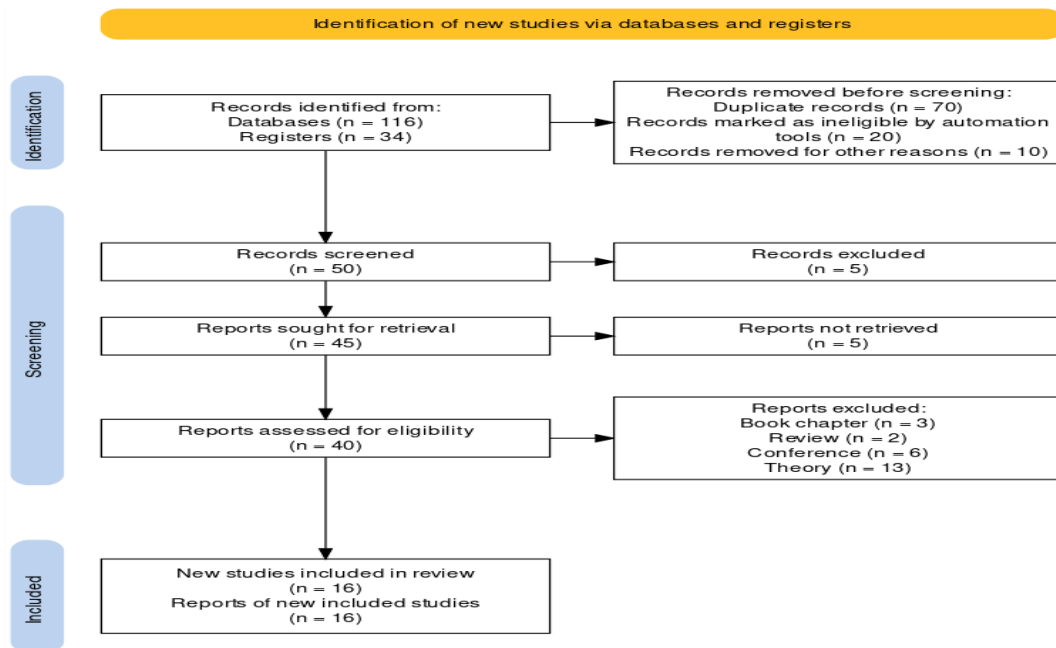


Figure 1

Source: Data processed, 2023

(Haddaway *et al.*, 2022)

SLR with PRISMA

Figure 1 it was obtained that the total number of databases was 150 with the keywords "Islamic", "ESG" and "sustainability". From this data, 100 were excluded because of the existence of 100 duplicates. So that the number of data screened became 50 then stretched to 5 so that it became 45 data then the selection was again issued 5 data so that 40 data were selected, but there were some data for reasons of book chapters, reviews, conferences and theories that did not match the number of 24 then the final number of data was chosen 16 data to be selected.

Discussion

In addition, ESG concepts can also be applied to investments based on Islamic accounting principles, such as investments based on sharia principles or social assets. Investors can choose to invest in companies that have good ESG performance, which is in line with the values and principles held by that investor (Qoyum *et al.*, 2021; Wahab and Naim, 2021). In this regard, Islamic accounting can make a significant contribution to sustainable economic development, by integrating ESG principles into accounting and investment practices (Nasir, N. S. M., & Seman, 2022). That way, companies, and investors can actively participate in sustainable economic development, which can provide long-term environmental, social, and economic benefits (Yang *et al.*, 2021).

However, there are some challenges in integrating ESG concepts into Islamic accounting (Al Ansari and Alanzarouti, 2020). One of the main challenges is the limited information and data available, especially in developing countries or specific industrial sectors. In addition, there are differences in the definition and measurement of ESG performance, which can cause difficulties in comparing companies' performance across industries or countries (Kotsantonis and Serafeim, 2019). To overcome these challenges, more significant efforts are needed in the collection and dissemination of information and data relevant to a company's ESG performance, both by the companies themselves and by third parties such as ESG assessment bodies or audit bodies (Robinson *et al.*, 2023). In addition, consistent standards and frameworks are needed for ESG performance measurement and reporting, which can better facilitate comparing and evaluating company performance.

In the long run, applying ESG concepts in Islamic accounting can significantly benefit sustainable economic development (Qoyum *et al.*, 2021; Wahab and Naim, 2021). By integrating ESG principles into accounting and investment practices, companies and investors can play a more active role in maintaining environmental, social, and economic sustainability, ultimately providing long-term benefits for society and the environment (Alsayegh *et al.*, 2020). ESG concepts can also provide direct benefits to companies, such as improved financial performance, reputation, and access to larger markets and resources (Zumente and Bistrova, 2021). Companies that perform well on ESG tend to be more attractive to investors and customers increasingly concerned with environmental and social issues.

In practice, applying ESG concepts in Islamic accounting can be made in several ways (Lee and Isa, 2023). One way is to integrate ESG principles into Islamic accounting practices, which have become standard practices in the Islamic finance industry. These principles include avoiding investment in sectors considered harams, such as liquor, gambling, or usury, as well as ensuring fairness and transparency in the management of funds and assets (Kamsu, 2013; Ma'ruf *et al.*, 2021). ESG concepts can also be applied in broader social investment practices, where investors allocate their funds to projects that have a positive environmental, social, and economic impact. Social investments include renewable energy, community development, and local economic empowerment (Camilleri, 2021). Overall, the application of ESG concepts in Islamic accounting can provide significant benefits for sustainable economic development by ensuring that companies and investors consider environmental, social, and economic aspects in their decision-making (Alkaraan *et al.*, 2022). This can provide long-term benefits for society and the environment while assisting companies and investors in achieving their financial goals.

To encourage the application of ESG concepts in Islamic accounting, support, and cooperation from various parties are needed, including companies, regulators, financial institutions, ESG assessment institutions, and the wider community (Galletta *et al.*, 2022). Some of the efforts that can be made include (Baid and Jayaraman, 2022; Daugaard and Ding, 2022): (1) Increase awareness and understanding of the concept of ESG and its benefits for sustainable economic development, both among companies, investors, and the wider community. (2) Develop consistent standards and frameworks for ESG performance measurement and reporting, which can better facilitate comparing and evaluating company performance. (3) Strengthen corporate governance and transparency in fund and investment management, by ensuring that environmental, social, and economic interests are considered in decision-making. (4) Integrate ESG principles into Islamic accounting practices and social investments, which can ensure that investment and fund management are carried out considering environmental, social, and economic aspects. (5) Increase access and use of information and data relevant to a company's ESG performance, both by the companies themselves and third parties such as ESG assessment agencies or audit bodies. With these efforts, it is hoped that ESG concepts can become an integral part of Islamic accounting practices and social investment and can help encourage sustainable economic development and improve the welfare of society as a whole.

In addition, further research and development are also needed to strengthen the concept of ESG and its integration with Islamic accounting practices (Daugaard, 2020; Lokuwaduge and Heenetigala, 2017). Some research topics that can be done include (Alkaraan *et al.*, 2022; Xie *et al.*, 2019): (1) An empirical study of the relationship between ESG performance and a company's financial performance, considering factors such as company size, industry sector, and market characteristics. (2) Analysis of the literature on frameworks and standards that have been developed for ESG performance measurement and reporting, as well as the development of frameworks consistent with Islamic accounting principles. (3) Research on the development of financial and

investment products that take into account ESG factors, taking account Islamic accounting views, and social investment principles. (4) Case studies of companies that have applied ESG concepts in Islamic accounting practices to evaluate their effectiveness and challenges.

With continuous research and development, it is expected that the concept of ESG and Islamic accounting can continue to develop and be increasingly relevant to future needs and demands (Daugaard, 2020). It is also necessary to conduct continuous socialization and education to increase awareness and understanding of the concept of ESG and sustainable Islamic accounting, both among accounting practitioners, investors, regulators, and the wider community (Arner *et al.*, 2020; Jan *et al.*, 2021). Some ways that can be done include (Alam *et al.*, 2022a; Townsend, 2020): (1) Conduct seminars, workshops, and training on the concept of ESG and sustainable Islamic accounting, which can be attended by accounting practitioners, investors, regulators, and the general public. (2) Promote case studies and best practices about companies that have successfully implemented ESG concepts in Islamic accounting practices, which can inspire other companies to follow in their footsteps. (3) Using social media and online platforms to disseminate information and education about ESG concepts and sustainable Islamic accounting, which can reach more people quickly and effectively. (4) Conduct joint campaigns and initiatives with relevant institutions, such as financial institutions, ESG assessment agencies, and government agencies, to raise awareness and support for ESG and sustainable Islamic accounting.

With continuous socialization and education efforts, it is hoped that the concept of ESG and sustainable Islamic accounting can be increasingly understood and applied by all stakeholders so as to provide maximum benefits for sustainable economic development and the welfare of society as a whole.

Islamic Accounting Model in ESG

The Islamic accounting model in ESG (Environmental, Social, and Governance) refers to the integration of Islamic accounting principles with ESG principles in financial reporting. This model combines aspects of conventional accounting with Islamic accounting principles that prioritize fairness, transparency, accountability, and sustainability (Qoyum *et al.*, 2021). Some critical elements of the Islamic accounting model in ESG include (Lee and Isa, 2023): (1) Consideration of ethics and social values in financial reporting: In Islamic accounting, ethics and social values play an essential role in decision-making. Therefore, in the Islamic accounting model in ESG, it is necessary to pay attention to how the impact of the company's activities on the environment and surrounding communities, as well as how the company pays attention to the principles of sustainability and social responsibility (Alazzani *et al.*, 2019). (2) Integration of ESG principles in financial statements (Pavlopoulos *et al.*, 2019): The Islamic accounting model in ESG requires companies to consider ESG factors in their financial reporting to be able to provide more complete and accurate information to stakeholders (Alam *et al.*, 2022a). This includes information about environmental performance, social performance, and overall company performance. (3) Use of sharia-based

financial instruments: The Islamic accounting model in ESG promotes the use of sharia-based financial instruments, such as sukuk and Islamic mutual funds, which pay attention to the principles of sustainability and social responsibility in investment management(Goud *et al.*, 2021). (4) Development of an ESG reporting framework consistent with Islamic accounting principles (Abdullah, et al., 2022): The Islamic accounting model in ESG develops an ESG reporting framework that is consistent with Islamic accounting principles, to provide consistent and transparent information to stakeholders(Reber *et al.*, 2022).

Overall, the Islamic accounting model in ESG refers to the integration of Islamic accounting principles with ESG principles in financial reporting. Thus, this model can help companies to pay attention to aspects of sustainability and social responsibility in managing their business to provide more excellent benefits to the community and the surrounding environment. The development of Islamic accounting models in ESG is also expected to help companies to improve their sustainability performance and gain the trust of stakeholders, including investors and consumers who are increasingly paying attention to social and environmental issues in decision-making(Alshurafat *et al.*, 2023). In addition, this model can also assist companies in meeting ESG reporting requirements that are increasingly important in today's global marketplace.

However, the development of Islamic accounting models in ESG also faces several challenges, such as a lack of understanding and awareness regarding the principles of Islamic and ESG accounting, as well as a lack of consistent and transparent standards in ESG reporting(Buallay *et al.*, 2020; Linnenluecke, 2022). Therefore, collaborative efforts between businesses, governments, and communities are needed to strengthen the development of this model and ensure conformity with appropriate Islamic accounting and ESG principles(Goud *et al.*, 2021). Overall, the development of Islamic accounting models in ESG is an essential step in improving corporate social and environmental responsibility and improving their sustainability performance(Liu *et al.*, 2021; Rehman *et al.*, 2020). This model combines Islamic accounting principles with ESG principles to provide more excellent benefits to the community and the surrounding environment and increase the trust of stakeholders.

The development of Islamic accounting models in ESG can also help companies to integrate sustainability principles into their business operations and strengthen transparency and accountability in sustainability reporting(Al Hawaj and Buallay, 2022; Rinaldi *et al.*, 2014). In the context of ESG, sustainability principles related to social, environmental, and corporate governance can be integrated with Islamic accounting principles such as fairness, transparency, and accountability (Jan *et al.*, 2021). Islamic accounting models in ESG can also assist companies in identifying sustainability risks and opportunities and planning sustainable business strategies (Khaled *et al.*, 2021). Through transparent and measurable ESG reporting, companies can communicate their sustainability performance and assure stakeholders they are committed to social and environmental responsibility.

Moreover, the Islamic accounting model in ESG can help in promoting sustainable and inclusive economic growth, where sustainable economic growth should integrate social and environmental aspects and pay attention to fairness in the distribution of benefits (El Khoury *et al.*, 2023). It also aligns with Islamic accounting principles that emphasize fairness in the distribution of wealth and benefits in society. Developing Islamic accounting models in ESG has excellent potential to improve corporate sustainability performance and promote sustainable and inclusive economic growth. However, the development of this model also faces several challenges, such as a need for more understanding and awareness regarding the principles of Islamic accounting and ESG, as well as a need for consistent and transparent standards in ESG reporting. Therefore, collaborative efforts between businesses, governments, and communities are needed to strengthen the development of this model and ensure conformity with appropriate Islamic accounting and ESG principles.

Challenges of Islamic Accounting Models in ESG

The development of Islamic accounting models in ESG is inseparable from various challenges that must be overcome (Hill, 2020). Some of the challenges faced in the development of Islamic accounting models in ESG include (Lee and Isa, 2023): (1) Lack of understanding and awareness of Islamic accounting principles and ESG. The first challenge is the lack of knowledge and awareness of Islamic and ESG accounting principles among business people and the public (Abdullah and Haron, 2022; Bukhari *et al.*, 2019). This may hinder the development and application of Islamic accounting models in ESG as these principles must be better understood. (2) Lack of consistent and transparent standards in ESG reporting. The second challenge is the need for consistent and transparent standards in ESG reporting (Cort and Esty, 2020; Ho, 2022). In the context of ESG, companies must report on their sustainability performance in various aspects, such as environmental, social, and corporate governance. However, the lack of consistent and transparent standards in ESG reporting can prevent companies from producing inconsistent and difficult reports compared to other companies. (3) Technical challenges. The third challenge is the technical challenges in developing Islamic accounting models in ESG. Effective ESG reporting requires technical proficiency in collecting, processing and analyzing sustainability data (Arayssi, M., *et al.*, 2020). In addition, the development of Islamic accounting models in ESG requires particular expertise in Islamic and ESG accounting and the ability to combine the two fields. (4) Lack of support from government and other stakeholders. The final challenge is the need for more support from the government and other stakeholders in developing Islamic accounting models in ESG. With support from governments and other stakeholders, the development and implementation of this model can be easier and more effective.

To address these challenges, collaborative efforts between businesses, governments, and communities are needed to strengthen understanding and awareness of Islamic and ESG accounting principles, as well as improve standards and technical support in ESG reporting (Darnall *et al.*, 2022). In addition, efforts need to be made to address technical challenges in developing

Islamic accounting models in ESG, such as developing technologies that enable more effective and efficient processing of sustainability data. To overcome the lack of support from the government and other stakeholders, efforts are needed to build awareness and educate stakeholders about the benefits and importance of developing Islamic accounting models in ESG (Goud *et al.*, 2021). In addition, the government can provide incentives and policy support to encourage the development of this model.

The role of international organizations can also be critical in the development of Islamic accounting models in ESG, such as the Islamic Development Bank (IDB), the International Islamic Financial Market (IIFM), and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). These organizations can help develop Islamic accounting standards and guidelines for ESG reporting that conform to Islamic accounting principles and sustainability. To encourage the development of Islamic accounting models in ESG, further research and action are also needed to develop a more integrated and holistic model in simultaneously considering the principles of Islamic accounting and ESG.

Expectations of the Islamic Accounting Model in ESG

The hope of developing Islamic accounting models in ESG is to create a more transparent, accountable, and sustainable accounting system (Khaled, R., Ali, H., & Mohamed, E. K., 2021). By integrating Islamic and ESG accounting principles, this model can help build a sustainable and environmentally friendly economy and provide broader social and economic benefits. Islamic accounting models in ESG can help increase stakeholder confidence in sustainability information and company performance, including investors, regulators, and the general public (Khaled *et al.*, 2021; Reber *et al.*, 2022). This can improve a company's access to capital, improve its reputation, and help companies manage risks associated with sustainability issues. In addition, the Islamic accounting model in ESG can help strengthen the contribution of the Islamic finance sector in building a sustainable economy, which can help drive economic growth and improve people's welfare more inclusively and sustainably.

Thus, the development of Islamic accounting models in ESG can be an essential step in promoting sustainable, environmentally friendly, and social-economic growth holistically, which is in line with the principles of Islamic accounting and ESG (Paltrinieri, A., Dreassi, A., Migliavacca, M., & Piserà, 2020). In addition, the development of Islamic accounting models in ESG can also help strengthen a company's financial position by integrating sustainability issues into financial statements, which can assist companies in making better strategic decisions. The development of Islamic accounting models in ESG can also provide benefits for society and the environment (Qoyum *et al.*, 2021). This model can reduce the negative impact of company activities on the environment and society, as well as assist companies in improving their actions in terms of sustainability. It can also encourage companies to take on positive social and environmental activities.

With the Islamic accounting model in ESG, companies are expected to accommodate sustainability

values in their operations and improve their sustainability performance. In the long term, developing this model can help create a more sustainable and inclusive economy that delivers broader social, economic, and environmental benefits. Thus, the expectation of developing Islamic accounting models in ESG is to holistically create a sustainable, environmentally friendly, and social economy that aligns with Islamic accounting principles and ESG. This model is expected to benefit companies, communities, and the environment and encourage sustainable economic growth. This model integrates Islamic and ESG accounting principles, allowing companies to apply sustainability values in their operations and improve their sustainability performance. While many challenges still need to be overcome, the development of Islamic accounting models in ESG has many potential benefits for companies, society, and the environment. In the long term, developing this model can help create a more sustainable and inclusive economy that delivers broader social, economic, and environmental benefits. Therefore, developing Islamic accounting models in ESG is essential to achieve sustainability goals holistically.

Conclusion

In the era of sustainability, developing sustainable economic and accounting models is increasingly important to create an economy balanced between social, economic, and environmental welfare. Sustainable Islamic economics and ESG are two complementary approaches to achieving this goal. In this context, the Islamic accounting model in ESG can be a solution to achieve holistic sustainability goals. This model integrates Islamic and ESG accounting principles, allowing companies to apply sustainability values in their operations and improve their sustainability performance. While many challenges still need to be overcome, the development of Islamic accounting models in ESG has many potential benefits for companies, society, and the environment. In the long term, developing this model can help create a more sustainable and inclusive economy that delivers broader social, economic, and environmental benefits. Therefore, developing Islamic accounting models in ESG is essential to achieve sustainability goals holistically.

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