

A Hermeneutic Analysis on ISAK 35: Habermas Perspective

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Abstract

Nonprofit-oriented entities play a critical role in providing social, educational, religious, and humanitarian services, yet face growing demands for transparent and accountable financial reporting. This study examines Interpretation of Financial Accounting Standards (ISAK) 35 on the Presentation of Financial Statements of Nonprofit-Oriented Entities through the lens of Jurgen Habermas's critical hermeneutics. Employing a qualitative approach within an interpretive-critical paradigm, the study analyzes ISAK 35 as a normative accounting text to uncover the meanings, interests, and potential communicative distortions embedded within the standard. The primary data consist of the Exposure Draft of ISAK 35 and supporting documents, including the Conceptual Framework for Financial Reporting and relevant Indonesian Financial Accounting Standards (PSAK), collected through document analysis. Drawing on legitimacy theory and entity theory, the findings indicate that ISAK 35 functions not only as a technical guideline for financial reporting but also as a formal instrument of legitimacy for nonprofit organizations. The separation of net assets with and without restrictions reflects the application of entity theory and aims to enhance transparency and accountability. However, from a critical perspective, the study finds that the emphasis on compliance and technical presentation may reinforce instrumental rationality, potentially limiting dialogical communication between nonprofit entities and their stakeholders, particularly in organizations lacking adequate accounting competence. This study contributes to critical accounting literature by highlighting the need to balance standardization with substantive public accountability and communicative rationality in nonprofit financial reporting.

Keywords: Financial Accounting Standards, Financial Statements, Habermas, Hermeneutic, ISAK 35.

1. Introduction

Nonprofit-oriented entities play an important role in providing social, educational, religious, and humanitarian services. Although they do not aim to maximize profit, nonprofit entities are still required to uphold accountability and transparency in managing resources derived from the public and other stakeholders. Financial statements serve as the primary instrument in this accountability process, as they function as a medium of communication between nonprofit entities and users of financial information (Ebrahim, 2003). Recent scholarly attention has increasingly focused on how nonprofit organizations manage financial reporting to meet stakeholder expectations, with particular emphasis on transparency and the prevention of accounting fraud (Jannah et al., 2025; Nguyen et al., 2025). The growing demand for accountability has prompted regulators in various countries to refine accounting standards for nonprofit entities.



In general, there are three types of organizational orientations: entities that are purely profit-oriented; entities that are not fully profit-oriented (such as hospitals and autonomous public universities, which engage in the sale of goods and services to generate fund balances); and entities that are purely based on public service provision. The need to provide an interpretative accounting standard led to the issuance of ISAK 35 in 2018 to replace PSAK 45, due to the latter's limited ability to accommodate the reporting needs of nonprofit entities other than governmental organizations. Studies on ISAK 35 implementation in various nonprofit contexts, including blood transfusion units and Islamic boarding schools, have revealed practical challenges such as limited human resource capacity and the need for simplified reporting formats that remain compliant with the standard (Salamah & Nasrullah, 2023; Subaeda et al., 2023).

In addition to PSAK 45's inability to adequately address the reporting requirements of nonprofit entities, several other factors motivated the issuance of ISAK 35. PSAK 1 Presentation of Financial Statements, paragraph 05, states that "this Statement uses terminology suitable for profit-oriented entities, including public sector business entities." This implies that if entities with nonprofit activities in either the private or public sector apply PSAK 1, they may need to adjust the descriptions used for certain items in the financial statements as well as the financial statements themselves. Furthermore, PSAK 1 does not provide guidance on how entities with nonprofit activities should present their financial statements. The characteristics of nonprofit-oriented entities also differ from those of profit-oriented business entities, particularly in terms of how nonprofit entities obtain the resources necessary to carry out their operational activities.

The analysis of accounting standards requires a theoretical framework capable of uncovering the deeper meanings and interests embedded within regulatory texts. Jurgen Habermas's critical hermeneutic approach is relevant for analyzing ISAK 35 because it positions language and text as media of communicative action that are inseparable from power relations. Habermas emphasizes that genuine understanding can only be achieved through communication free from domination, referred to as the ideal speech situation. However, in practice, communication is often subject to systemic distortion due to the dominance of instrumental rationality and technocratic interests (Habermas, 1984). In accounting research, Habermas theory has been extensively applied to examine how accounting systems can either enable or distort communication, particularly in non-business organizations such as churches, health services, and educational institutions. Studies have shown that accounting standards are not neutral technical documents but rather political instruments that shape organizational reality and stakeholder relationships (Noël et al., 2010; Power, 2013). Accordingly, accounting standards can be understood as discourses that potentially contain communicative distortions requiring critical examination.

Through the lens of Habermas's critical hermeneutics, ISAK 35 can be examined not only in terms of its structural and normative provisions, but also in terms of how the standard frames the concepts of accountability, transparency, and the public interest. This analysis enables researchers to assess whether ISAK 35 encourages dialogical communicative action between nonprofit entities and their stakeholders, or instead reinforces instrumental action oriented toward compliance and administrative control.

Based on the foregoing discussion, this study aims to analyze ISAK 35 using Jurgen Habermas's critical hermeneutic perspective in order to uncover the meanings, interests, and potential communicative distortions embedded within the standard. This study is expected to contribute theoretically to the development of critical accounting research, as well as

practically by encouraging nonprofit financial reporting practices that are more dialogical, reflective, and oriented toward substantive public accountability.

2. Literature Review

2.1. Legitimacy Theory

Legitimacy theory explains that organizational continuity is largely determined by the degree of societal acceptance of an organization's existence and activities. This theory is grounded in the concept of the social contract, namely an implicit agreement between an organization and society, whereby the organization is granted the right to operate as long as its actions are aligned with prevailing social values, norms, and expectations (Dowling & Pfeffer, 1975). When a discrepancy arises between organizational behavior and societal expectations, organizational legitimacy may be threatened.

From an accounting perspective, legitimacy is viewed as a strategic resource that must be actively managed. Lindblom (1994) argues that organizations deliberately seek to obtain, maintain, or restore legitimacy through various actions, including changes in operational activities and communication strategies. One of the primary means for achieving this objective is reporting and disclosure, both financial and nonfinancial, which are used to shape public perceptions that the organization has acted responsibly. According to legitimacy theory, financial reporting is not merely neutral in nature, but also serves symbolic and political functions (Gray et al., 1996). This implies that society is more likely to positively evaluate and grant legitimacy to nonprofit organizations when they present financial statements that comply with applicable accounting standards.

2.2. Entity Theory

Entity theory views an organization as an independent economic subject that exists separately from its owners, donors, managers, and other interested parties. Under this theory, financial statements are prepared to reflect the financial position and performance of the entity as an autonomous unit, rather than as an extension of the interests of particular individuals or groups (Paton, 1992; Riahi-Belkaoui, 2004). In the context of nonprofit-oriented entities, entity theory serves as an important conceptual foundation because the resources managed are not owned by managers or donors, but are entrusted to the entity to be used in accordance with organizational objectives. ISAK 35 reflects entity theory through the recognition of assets, liabilities, and net assets as belonging to the entity, as well as through the distinction between net assets with restrictions and without restrictions. This separation emphasizes that restrictions on the use of resources arise from external stipulations, rather than from individual ownership.

2.3. ISAK 35

ISAK 35 (Interpretation of Accounting Standard 35) on the Presentation of Financial Statements of Nonprofit-Oriented Entities was issued by the Financial Accounting Standards Board on 26 September 2018. Entities are required to apply this Interpretation for financial years beginning on or after 1 January 2020. An entity uses its judgment to determine whether it qualifies as a nonprofit-oriented entity, regardless of its legal form, in order to apply this Interpretation. Accordingly, the scope of the presentation of financial statements applies to nonprofit-oriented entities irrespective of their legal form.

This Interpretation may also be applied by nonprofit-oriented entities that use the Financial Accounting Standards for Entities without Public Accountability (SAK ETAP). If a nonprofit-oriented entity makes adjustments to the titles of its financial statements, this

Interpretation does not restrict the use of specific titles, provided that the titles used more appropriately reflect the content and function of the financial statements.

The Presentation of Financial Statements of Nonprofit-Oriented Entities does not stipulate specific transitional provisions. Consequently, the Exposure Draft of ISAK 35 applies the general provisions of PSAK 25 on Accounting Policies, Changes in Accounting Estimates, and Errors relating to changes in accounting policies that do not specify transitional requirements. Therefore, such changes in accounting policies are governed and applied retrospectively.

2.4. Critical Hermeneutic

Critical hermeneutics is an interpretive approach that goes beyond understanding the literal or historical meaning of a text, and instead seeks to uncover the interests, ideologies, and power relations embedded within it. This approach emerged as a critique of classical and ontological hermeneutics, which are considered to accept texts too readily without questioning the structures of domination that shape them. In critical hermeneutics, texts are understood as social products that are not neutral and are always situated within specific political, economic, and institutional contexts (Habermas, 1971).

The central figure in critical hermeneutics is Jurgen Habermas, whose work is rooted in the Frankfurt School tradition. Habermas criticizes Gadamerian hermeneutics, which emphasizes dialogue and the fusion of horizons, for being insufficiently sensitive to communicative distortions produced by power and ideology. According to Habermas, understanding cannot be separated from knowledge-constitutive interests, namely technical, practical, and emancipatory interests. Critical hermeneutics operates at the level of emancipatory interests, aiming to liberate subjects from forms of domination concealed within language, symbols, and discourse (Habermas, 1984).

Within the framework of critical hermeneutics, the interpretive process involves two main stages. First, it entails an understanding of the explicit meaning of the text, as practiced in traditional hermeneutics. Second, it involves a reflective critique of the social and structural conditions that allow the text to emerge and be accepted as “natural” or “objective.” Thus, interpretation is not merely interpretive in nature, but also normative and evaluative, as it seeks to assess whether a text reproduces inequality, domination, or the interests of particular groups (Thompson, 1981).

3. Methods

This study adopts a qualitative approach within an interpretive-critical paradigm. The interpretive approach is a qualitative research approach grounded in the assumption that social reality is neither objective nor singular, but is instead constructed through language, symbols, and social interactions. Within this approach, knowledge is not understood as the result of neutral measurement, but rather as the outcome of an interpretive process through which social actors ascribe meaning to particular practices, texts, and institutions (Burrell & Morgan, 2017). This approach is selected because the study aims to understand and critically examine the meanings, interests, and potential communicative distortions embedded in ISAK 35 as a normative accounting text. The study also seeks to interpret and evaluate accounting standards within their broader social and institutional contexts.

Jurgen Habermas’s critical hermeneutic approach is employed as the primary analytical framework. Critical hermeneutics enables the researcher to combine textual understanding with reflective critique of the dominance of instrumental rationality and power relations manifested in the language of accounting standards. The object of this study is the Exposure

Draft of Interpretation of Financial Accounting Standards (ISAK) 35 on the Presentation of Financial Statements of Nonprofit-Oriented Entities, issued by the Indonesian Institute of Accountants. The primary data source consists of the official ISAK 35 document and supporting materials, such as the Conceptual Framework for Financial Reporting and related PSAKs referenced in ISAK 35. The research data are secondary in nature and are collected through a documentation study of the relevant texts.

Data analysis was conducted using the stages of Habermas's critical hermeneutic approach, which comprise the following steps:

- 1) Textual analysis, involving an in-depth reading of ISAK 35 to identify key concepts, core terminology, and normative structures that construct the financial reporting framework for nonprofit-oriented entities. This initial stage aligns with approaches used in studies examining accounting texts as communicative documents that shape organizational reality (Yahya et al., 2023).
- 2) Interpretive analysis, consisting of interpreting the meaning of the text by relating it to entity theory, legitimacy theory, and stakeholder theory in order to understand the assumptions and values institutionalized within the standard. This stage draws on the hermeneutical tradition in accounting research, which positions understanding as emerging through the dynamic interaction between the interpreter and the text (Lehman, 2006). As noted by Power (2013), Laughlin's adaptation of Habermas thought enables researchers to move beyond surface-level description toward deeper organizational and societal meaning.
- 3) Critical analysis, which entails evaluating the potential dominance of instrumental rationality and communicative distortions within ISAK 35 by applying Habermas's theory of communicative action. Recent applications of this approach have been demonstrated in social and environmental accounting contexts (Yahya et al., 2023).
- 4) Emancipatory reflection, involving the derivation of theoretical and practical implications concerning the potential strengthening of substantive accountability and dialogical communication in nonprofit financial reporting. This final stage responds to Habermas's emphasis on critical theory's emancipatory interest, as operationalized in accounting research by Power & Laughlin (1996) and more recently by studies examining how accounting can enable public debate on social issues.

4. Results and Discussion

4.1. Research Results

4.1.1. Separation of Net Assets and Its Purpose in ISAK 35

ISAK 35 emphasizes the separation of net assets with restrictions and without restrictions, which can substantively be understood as a form of "capital" separation within nonprofit entities. This separation is intended to demonstrate limitations on the use of resources in accordance with specific provisions or regulations, as well as to maintain the entity's accountability in managing entrusted funds. A key distinction between net assets in nonprofit organizations and equity in profit-oriented companies lies in the allocation of expenses and revenues, which may function as a tool for assessing the activities of nonprofit organizations. For example, restricted assets may be grouped according to specific activities, with related revenues and expenses separated from those of other activities. This results in differences in the statement of financial position, statement of comprehensive income, statement of changes in net assets, and statement of cash flows when compared to profit-

oriented organizations. These differences are illustrated in the examples provided in the Exposure Draft of ISAK 35.

This approach is consistent with the view of the Financial Accounting Standards Board of the Indonesian Institute of Accountants (DSAK IAI), which considers that the primary difference between nonprofit-oriented entities and profit-oriented business entities lies in how nonprofit entities obtain resources from resource providers who do not expect repayment or economic benefits commensurate with the amount of resources provided. Therefore, the concepts of recognition, measurement, presentation, and disclosure for similar transactions are more appropriately guided by existing provisions within SAK or SAK ETAP. Normatively, the separation of net assets is intended to enhance transparency and prevent the misuse of resources. Within the framework of entity theory, this separation reinforces the notion that resources do not belong to individuals or particular groups, but are managed by the entity to achieve organizational objectives. Accordingly, the separation of net assets functions as a mechanism of control and protection over the social purposes of nonprofit entities.

The Exposure Draft of ISAK 35 also states that differences in the presentation of financial statements within the same group of standards may give rise to regulatory inconsistencies and ambiguity regarding the boundaries between PSAK 1: Presentation of Financial Statements and PSAK 45: Financial Reporting for Nonprofit Entities. The scope of PSAK 45 applies to nonprofit-oriented entities, whereas the scope of PSAK 1 is often perceived as applying solely to profit-oriented business entities. This indicates the need for a deeper accounting understanding to enable the effective application of ISAK 35 to nonprofit organizations, given their atypical organizational characteristics. PSAK 1 on Presentation of Financial Statements, paragraph 05, states that if entities with nonprofit activities in either the private or public sector apply PSAK 1, they may need to adjust the descriptions used for certain items in the financial statements as well as the financial statements themselves. However, from a critical perspective, entity theory may also be understood as a normative construction that has the potential to obscure the social and moral relationships between nonprofit entities and their stakeholders. By positioning the entity as the central locus of accountability, financial reporting practices may shift toward a technical and administrative orientation, thereby reducing the space for reflective dialogue concerning the organization's social objectives.

4.1.2. Legitimacy and Its Purpose in ISAK 35

ISAK 35 functions as a formal instrument of legitimacy for nonprofit entities. The application of this standard enables entities to demonstrate compliance with regulations and professionally recognized accounting practices. Within the framework of legitimacy theory, financial statements prepared in accordance with ISAK 35 serve as symbols of an entity's conformity with prevailing accounting norms.

The absence of specific legislation in Indonesia that clearly defines and delineates the scope of nonprofit-oriented entities has led the Financial Accounting Standards Board of the Indonesian Institute of Accountants (DSAK IAI) to refrain from providing a formal definition or criteria distinguishing nonprofit-oriented entities from profit-oriented business entities. Consequently, nonprofit organizations are required to exercise their own judgment in determining whether an entity qualifies as nonprofit-oriented, regardless of its legal form, in order to apply ISAK 35. Several factors may be considered in this assessment, including whether the entity's resources are derived from resource providers who do not expect repayment or economic benefits commensurate with the amount of resources provided; whether the nonprofit organization produces goods and/or services without the objective of generating profit, and if profits are generated, whether they are not distributed to the founders

or owners of the nonprofit entity; and whether there is an absence of ownership characteristics typical of profit-oriented business entities, in the sense that ownership interests in nonprofit entities cannot be sold, transferred, or redeemed, and do not represent proportional claims on the entity's resources upon liquidation or dissolution.

PSAK 1 on Presentation of Financial Statements, paragraph 05, permits nonprofit-oriented entities to adjust the descriptions used for certain items presented in the financial statements and the titles of the financial statements themselves. However, PSAK 1 does not provide further explanation or illustrative examples regarding such adjustments. In addition, nonprofit-oriented organizations may adapt the descriptions used for certain items in the financial statements. For example, when resources received by a nonprofit entity are subject to conditions imposed by resource providers, the entity may present those resources based on their nature, namely whether they are subject to restrictions or free from restrictions imposed by the providers.

Nonprofit-oriented entities must continue to consider all relevant facts and circumstances in presenting their financial statements, including the notes to the financial statements, so as not to diminish the quality of the information presented. When examined through the lens of Habermas's critical hermeneutics, legitimacy theory is relevant for assessing whether ISAK 35 promotes dialogical communication or instead reproduces instrumental rationality, whereby financial statements function as tools of administrative legitimacy that may reduce the substantive accountability of nonprofit organizations if not accompanied by adequate accounting competence. This risk is further exacerbated when nonprofit organizations lack competent accounting personnel and are required to classify their activities and determine net assets with or without restrictions, potentially resulting in financial statements that do not accurately reflect the underlying realities of the nonprofit organization.

4.2. Discussion

In its implementation, ISAK 35 needs to be supported by competent accounting personnel to ensure that the financial statements prepared properly reflect the actual conditions of nonprofit organizations. The potential risk that financial statements are used merely to fulfill administrative requirements can be minimized through a thorough understanding of PSAK 1, PSAK 5, PSAK 25, and ISAK 35.

Recent empirical studies across Indonesia consistently reveal significant challenges in ISAK 35 implementation due to limited accounting competence. Research on Save the Children Indonesia Foundation found that the foundation had not fully implemented ISAK 35 in its financial statements, lacking required statements of changes in net assets and notes to financial statements (CALK), with discrepancies in terminology usage (Putong et al., 2025). Similarly, a study of Dorkas Orphanage identified that lack of understanding of accounting standards and insufficient training were major factors contributing to poor ISAK 35 implementation, leading to recommendations for enhanced accounting expertise and external support to increase public confidence (Sembiring, 2025).

These findings are reinforced by research at GMIM 4 Tondano Primary School, which revealed that while the institution had begun implementing ISAK 35 principles, it encountered significant challenges related to technical comprehension and human resource capability in creating suitable financial statements (Kossay, 2025). A study of Al-Mustaqim Islamic Boarding School in Parepare found that financial records remained manual and not fully compliant with sharia accounting standards, with obstacles including limited human resources and lack of socialization regarding accounting standards for non-profit organizations (Afifah & Indrayani, 2025).

The pattern of partial implementation is evident across various nonprofit types. Research on Foundation XX showed that while cash flow statements and notes to financial statements adhered to ISAK 35, statements of financial position, comprehensive income, and changes in net assets contained discrepancies due to the absence of certain accounts, reflecting lack of transactions rather than deliberate non-compliance (Ayuntari et al., 2025). Similarly, Ruang Belajar Aqil only began implementing ISAK 35 in 2022, with deficiencies in presenting statements of changes in net assets, cash flows, and details of comprehensive income, requiring improvement to increase transparency and accountability (Aliyah & Andayani, 2023). Mosque financial management studies at Baitul Aqrom Mosque and Nurul Huda Mosque indicate that while managers recognize the importance of ISAK 35, obstacles in understanding and implementation persist, although implementation contributes positively to improving financial statement quality and public trust (Fitria & Ruci, 2025; Indriani, 2025).

These empirical findings from diverse Indonesian nonprofit contexts including foundations, orphanages, schools, Islamic boarding schools, and mosques consistently demonstrate that inadequate accounting competence represents a systemic challenge rather than isolated incidents. The risk that financial statements may not accurately reflect organizational realities is heightened when nonprofit organizations lack personnel capable of properly classifying activities and determining net assets with or without restrictions.

Upon closer examination, the underlying interest of the Financial Accounting Standards Board of the Indonesian Institute of Accountants (DSAK IAI) is to provide standards that are more aligned with the needs of nonprofit organizations, reflecting the evolution of accounting understanding since the issuance of PSAK 45. Nevertheless, the possibility that nonprofit organizations may prepare financial statements that do not fully comply with the standards, or that contain misstatements, may increase in practice. When compared to PSAK 45, PSAK 45 placed greater emphasis on time-based restrictions, resulting in the recognition of temporarily restricted net assets. Under ISAK 35, such amounts are classified as net assets with restrictions, as the balances are designated for specific purposes, leading to the classification of net assets based on activities. According to the author, the development of ISAK 35 is generally consistent with the need to enhance transparency in nonprofit financial reporting. However, the consistent pattern of implementation challenges across multiple studies suggests that standard-setting alone is insufficient. Complementary capacity-building initiatives and tailored guidance are essential to achieve the substantive accountability that ISAK 35 intends to promote.

5. Conclusion

This study analyzes ISAK 35 using Jurgen Habermas's critical hermeneutic perspective to explore how accounting standards for nonprofit-oriented entities construct meanings of accountability, transparency, and legitimacy. The findings suggest that ISAK 35 represents a significant development in nonprofit financial reporting in Indonesia by addressing the limitations of PSAK 45 and providing a framework that better reflects the characteristics of nonprofit entities, particularly through the separation of net assets with and without restrictions. From the standpoint of entity theory, this separation reinforces the notion that resources are entrusted to the entity rather than owned by individuals or donors, thereby supporting accountability and control over the use of resources for social purposes. At the same time, legitimacy theory helps explain how ISAK 35 functions as a formal mechanism through which nonprofit organizations seek societal acceptance by demonstrating compliance with professionally recognized accounting standards. However, when examined critically, the

study reveals the risk that financial reporting under ISAK 35 may become overly technical and administrative, especially when nonprofit organizations lack sufficient accounting expertise. In such cases, financial statements may serve primarily as instruments of administrative legitimacy rather than as media of meaningful, dialogical accountability.

Therefore, this study concludes that while ISAK 35 enhances transparency and standardization in nonprofit financial reporting, its effectiveness in promoting substantive public accountability depends on the accounting competence of nonprofit organizations and their ability to interpret and apply the standard reflectively. Future research is encouraged to examine the practical implementation of ISAK 35 in nonprofit organizations and to explore ways of strengthening dialogical accountability that align accounting practices with the social missions of nonprofit entities. The limitation of this study is the use of the Exposure Draft as the primary research data, which may reflect incomplete or preliminary provisions compared to the finalized standard. Furthermore, given that ISAK 35 is anticipated to be updated to ISAK 335, future researchers are encouraged to use ISAK 335 as the basis for analysis to ensure greater accuracy and relevance. While these technical and administrative constraints are acknowledged, it is equally important to recognize that a reflective and dialogical application of ISAK 35, one that goes beyond mere compliance holds meaningful potential for fostering genuine communicative accountability between nonprofit entities and their stakeholders. Future studies may therefore explore how the transition to ISAK 335 can be approached not only as a technical update, but as an opportunity to embed more participatory and stakeholder-oriented accountability practices within nonprofit financial reporting frameworks.

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