

The Performance of Governance of Nonprofit/Charitable Organizations: The Insight of Malaysian Waqf Institutions

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Abstract

This study seeks the governance performance particularly in the perspective of accounting accountability of non-profit/charitable organizations in Malaysia. The regular business practice or non charitable firms which comply with the Generally Accepted Accounting Procedure (GAAP) have place these firms in the right corporate governance and transparency manner. However, for the non-profit/charitable organizations, various studies show that most of them do not comply to the standard accountability (Cordery and Morley, 2005). The significance to have proper or standard accounting practice is mostly demanded especially in the Islamic organizations mainly waqf. Along with the revival of waqf institutions, the attention to the call for waqf accounting has been emerging. The new and modern waqf management has put greater emphasize on the principles of accountability and transparency. As part of good governance and best practices of waqf institutions accounting is believed to be able to improve the transparency of trustees (mutawalli). Indeed, accounting is a tool for mutawalli to discharge his accountability to many parties such as waqif, waqf board, government and community in large. This paper aims at exploring the performance of accounting practice by waqf administrator such as State Islamic Religion Council (SIRC), Malaysian Waqf Foundation, Department of Waqf and Zakh towards improvement of the accountability and transparency. By comparing the Malaysian waqf with the Statement of Recommended Practices for Charitable (SORP,2005) which been practiced in UK, some improvement could be made to Malaysian waqf institutions.

Keywords: waqf, corporate governance, mutawalli, charitable organizations

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Introduction

The effect of corporate governance towards firms have been debated prior to some corporate collapses such as Polly Peck in 1990 and BCCI in 1991 (UK), Enron in 2001 and WorldCom in 2002 (US) (Abdul Rahman, 2006). In Malaysia, corporate governance did not concern to matter very much until the Asian economic crisis in 1997. There are various reasons that contribute to the governance misconduct such as the accounting responsibility. The accounting accountability is significant in reducing the corporate misconduct. The practice of right corporate governance by firms is most expected which they should comply with GAAP in an ethical manner. Perhaps, the non-profit firms like the charitable organizations also accounted for the corporate responsibility. However, for the non-profit/charitable organizations, various studies show that most of them do not comply to the standard accountability (Cordery and Morley, 2005). They explained that the inefficient of accounting practices in charitable organizations is due to the unused of the standard accounting. Thus, there is no formal accepted definition of accounting in the non-profit organizations industry.

According to Yetman and Yetman (2010), nonprofit firms are conferred with various tax benefits like income, property and sales tax exemption. Therefore donors towards non profits can reduce their taxable income with their donations. In return for the significant benefits, nonprofit organizations are responsible to the public who are in effect financing these tax benefits. To be accountable non profits are needed to make their financial information available to the public. However, there is no standard general audit requirement for nonprofit organizations compared to other public firms which are required to present their audited financial statement public. Instead of conventional nonprofit firms, the Islamic institutions similar to charitable organizations like waqf also affected. A waqf or Islamic endowment also requires accounting standards. These are due to various studies found that there are still an ongoing issue of accountability and transparency of the waqf trustees (Abdul Rahim et al. 1999; Siti Rokyah, 2004).

As a result, Shahul and Hisham (2006), argued that the standard waqf accounting should be enforced to complement the issues. Therefore, the Department of Waqf and Zakh has instructed a committee to go thru the waqf accountability and transparency issues by studying and developing a standard of waqf accounting. To date, all State Islamic Religious Council (SIRC) are under their own state's legislation whereby the practices are differ from state to state.

This conceptual paper is aimed to explore the degree of effectiveness of waqf accounting and management globally and Malaysia particularly towards improving the accountability and transparency. The Statement of Recommended Practices for Charitable (SORP, 2007) seems to be an alternative to enhance and improve the waqf accounting quality.

The Definition of Waqf

A waqf is an Arabic verb “waqafe” which etymologically means to hold, to keep or detain. According to Imam Abu Hanifa waqf is the detention of specific thing in the ownership of waqif (appropriator or waqf founder) and the devoting of its profits or usufruct in charity on the poor or other pious intentions. In other words, a waqf or plural in Arabic called awqaf is an act of holding certain property and preserving it for the confined benefit of certain philanthropy with disallowing any use or disposition of it outside the specific objective (Kahf, 1998). Toraman et al. (2004) depicted that waqf applies to non-perishable property whose benefit can be extracted without consuming the property itself. Similarly, waqf served as a vehicle for financing Islam as a society (Hodgson, 1974).

There is no direct injunction of the Quran about waqf. However, there is a hadith which reported by Ibn Umar, whereby Umer Ibn Al Khitab got land in Khyber thus came to the Prophet Muhammad SAW and seek advice regarding the land. The Prophet mentioned to make the land inalienable and give the profit to the charity. Therefore, waqf signed as the permanent dedication by a Muslim of any property for a good faith purpose as pious and charitable.

In Islam, land was the first waqf. The mosque of Quba’ in Medina was the first mosque in Islamic history which still exists till today which is waqf oriented. Among others that using waqf land are the Al Azhar University in Egypt, University of Cordova Spain, and Al Noori Hospital in Damascus. (Ahmad Zaki et al., 2008). In Malaysia, JCorp has playing a significant roles in practicing waqf for the ummah development. The establishment of Kumpulan Waqf An Nur Bhd. with management support by KPJ Healthcare Bhd. to manage a chain of waqf An Nur Clinics and Malaysia’s first waqf hospital in Pasir Gudang Johor are among the success stories of Malaysian waqf practiced by JCorp. (Hashim, 2009).

Accounting for Charitable Organizations

The aims of Accounting Standard Board (ASB) are to set up and enhance standards of financial accounting and reporting for benefits of customers, and auditors of financial information. To date, ASB provides accounting standards that are primarily applicable to general purpose firm financial statements. In certain industries, a complete guidance is required to implement accounting standard effectively. As such the form of Statements of Recommended of Practice (SORP) is established for the ASB purpose. The SORP board has agreed that it shares the ASB vision of advancing and sustaining standards of financial reporting in the public interest. The Code of Practice sets out procedures to be followed by SORP has been recognized and accepted by ASB to further enhance the accounting transparency.

On the other hand, the SORP introduces the terms restricted and unrestricted to differentiate how charitable donations should be accounted for to reflect the wishes of the donors. These terms are intended to correspond with the terms specific and general used in previous editions of the SORP and have been adopted to help in the clarity of the financial statements. The terms restricted and unrestricted apply to charitable donations only and are not intended to be applied to other sources of funding (SORP, 2007). Charitable donations are assumed as restricted by reference to the facts and conditions regarding the donation. Different accounting treatments will require to be applied to reflect these classifications and it is significant that institutions understand these implications when accepting donations which organizing appeals other fundraising activities.

An endowment is a form of charitable trust which is held on trust to be retained for the benefit of the institution (SORP, 2007). Endowment funds can be sub divided into their capital element and an accumulated income fund. In many conditions, endowment funds are permanent due to governing body like trustees is required to maintain permanently the capital of the endowment fund. Since the endowment is permanent, it will be indicated by the wishes of the donor. This type of endowment fund cannot be spent as though it were income. Income from the endowment funds should be accounted for in the account.

Accounting for Waqf

Waqf has been an important source for Islamic economy. Thus the accountability and transparency of mutawalli (trustees) is important for the equal distributions. In Malaysia, the SIRC is the sole trustee of waqf under the Malaysian Federal Constitution due to religion factor which is under state administration. SIRC function is to organize all the waqf applications by individual or organization whether it is general waqf or special waqf and to maintain all the records, updating, monitoring, registering and developing all the waqf assets especially the general waqf. Hamid (2010) explained that the continuity of waqf management inefficiency such as un-found written record, un-updating and un-registration waqf details has placed SIRC in difficulty in managing the waqf assets.

Baharuddin et al. (2006) stated that the problem in waqf management is also caused by other factors such as lack of professional in managing waqf. Since waqf is a prestige Islamic institution, the demand of professional to cooperate with the mutawalli, new technique and technology oriented method should be utilized so that waqf assets could be managed wisely. This is in line with Paiz Hassan (2008) who agree with the professionalism is required in institution like waqf so that the Islamic image could be enhanced and sustained. He also added that seminar and training are required for waqf administrator so that the waqf administration will be smoothly organized and gave benefits to the appropriate person.

Indeed, waqf accounting standard is required to resolve the issues faced by the waqf trustees to record waqf financial transactions objectively and efficiently. Currently, each SIRC has their own accounting standard. So, there is no uniformity or standard practices like what have been practiced in the UK. The UK SORP on Charity Accounting has been successfully facilitates and give guidelines to administrators to help charities efficiently in preparing their financial statements for the annual report.

The accounting standard is required by the *mutawalli*. The standard here refers to an agreed, repeatable way of doing something. It is a published document that has a technical specification or other stated information designed to be used consistently as a rule, guideline, or definition. The most important standard is its ability to be developed and maintained best practices. Therefore this is required in the waqf accounting to be excelling in the record keeping and sustaining an effective management.

The Waqf Accountability and Transparency

There is a lot has been debated about waqf recently. There are seminars, discussions and talks among professional and public about the indispensable growth of the waqf institutions. Cajee (2008) indicates that there is a lot of international conferences which were held by Islamic Development Bank (IDB) through its subsidiary; the Islamic Research and Training Institute shows an increasing awareness among public towards waqf institution. The call of waqf accounting had been emerged due to the roles play by the mutawalli as parallel with the high demand of the waqf brand. The concepts of accountability and transparency cannot be ignored in this modern waqf management (Cajee, 2008). Adnan et al. (2007) added that proper governance and healthy practice of awqaf institutions especially in accounting practice is believed can enhance the accountability and transparency of *mutawalli*.

Ihsan (2007) explained that the views towards *mutawalli* regarding responsibility and accountability influence the way of *awqaf* institutions produce and disseminate accounting information. Perhaps, Cordery and Morley (2005) also assert that the uncertainty over accounting practices in charitable sectors is not only because of the absence of accounting standards but also because the failure to establish a widely agreed definition of accountability for that industry.

Currently, there is a lack of research has been done related to the current practice of waqf in Malaysia. The previous literatures reveal that there are three main issues have been explored concerning waqf accounting. First of all, waqf accounting is a basic tool to be used as a better practice for corporate governance of waqf institutions. Thus, Marsoof (2004), Pirasteh and Abdolmaleki (2007) and Rashid (2007) explain about the preparation of accounting and auditing standards for awqaf. Secondly, according to Abdul Rahim et al. (1999) and Siti Rokyah (2005), they state that the accounting practices vary among the waqf institution due to the absence of the

accounting standard for waqf. Therefore, the waqf accounting standard (WAS) is needed to standardized the accounting practices among the awqf institutions. Thirdly, the existing standard such as Statement of Recommended Practice (SORP, 2005) for charity or AAOIFI's Statements of Financial Accounting should be used as a guideline to develop accounting concept and standard for awqf institutions since there is no legally waqf accounting standard has been introduced (Ihsan and Shahul, 2007).

By establishing the accounting concept and standard for waqf, thus may improve the accountability and transparency of waqf institutions to the public. The improvement of accounting standard and procedure is the most important element to the betterment of waqf institutions (Marsoof, 2004). Marsoof (2004) found that the management of waqf in Sri Lanka has not been optimized and thus, he suggested that the waqf accounting procedures and standard should be improved and his ideas is consistent with Adnan (2005) who agrees that waqf accounting standard should be developed for accountability and transparency. He also has explained about two alternatives models for waqf accounting which is waqf can be classified as a social organization, as therefore accounting for non-profit organizations will be sufficient to be adopted. The other alternative model has been suggested by Marsoof (2004) is waqf as an organization that intend to maximize its resources through investment activities, thus accounting for commercial organizations can be adopted.

Furthermore, Ihsan et al. (2006) state about the accountability and transparency issues in waqf institutions among Muslim countries. In their study, the findings show there is lack of accountability and transparency in management of waqf assets and also mismanagement by the mutawalli in administering waqf. They also have found four main ideas that can be applied in order to improve the accounting procedures for waqf institutions based on the proposal from the Charity Commission in the UK. The four main ideas are internal financial control, transparency and reporting, management of funds and code of Good Governance. In addition, it must to take into consideration the need in concerning the legal reformation of waqf and the government of Muslim countries should re-evaluate waqf acts for better improvement.

The other issue raised by the previous literature is about the accounting practices vary among awqaf institutions in Malaysia and Indonesia. Abdul Rahim et al. (1999) have pioneered the study on examining the accounting and administration practices among State Islamic Religious Council (SIRC) in Malaysia. Their findings revealed that there was no detailed information about waqf assets, the management was conducted unsystematically and lack of accounting systems for waqf assets, where there is no proper or written procedures to record waqf financial transactions. Abdul Rahim et al. (1999) also mentioned that this situation happened due to no federal authority to coordinate all waqf in Malaysia, therefore they suggested that the waqf department should be established to improve the management of waqf. They also recommended that accounting procedures and standards for waqf should be improved.

Another study on waqf has been done by Siti Rokyah in 2005. Siti Rokyah (2005) examined the status of financial reports and determined the level of waqf disclosed by SIRC in Malaysia. She also analyzed the financial procedures adopted and the relationship between financial procedures and waqf accounting practices. Her findings showed that SIRC's vary in terms of the status on producing the latest annual report. Most of the SIRC's have overdue and outdated financial reporting and most of them showed low level of disclosure in their annual reports. However, her study also revealed that SIRC's with qualified accounting staffs in handling the accounts and reports have higher level of disclosure. Furthermore, the SIRC's that produced the latest annual reports showed higher level of disclosure as compared to SIRC's which have outdated annual reports.

Conclusions

It can be concluded that the growing waqf institutions is very significant towards Muslim society. The roles play by mutawalli should be in line with the growth of the waqf development. Indeed, the technology and professionalism should come in the first place to sustain waqf as competitive as possible. The authority, administrator and the society should also work in hand to make sure that waqf is relevance and widen the awareness of waqf towards all type of life. If the integration of waqf is uphold, the Muslim society will further develop spiritually instead of Islamic economic growth therefore increasing the country sustainability.

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