

**Accounting and Accountability of *Waqf*,
Zakat and *Baitul Mal (WZB)* in Malaysia:
A Review of Literature**

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Abstract

This article reviews literature on accounting and reporting for *waqf*, *zakat* and *baitul mal* (WZB). Given that WZB are under the purview of the State Islamic Religious Councils (SIRCs), the structure of the administrative machinery of Islamic affairs is discussed and how this gives rise to the unique demarcation in powers and authority on policies pertaining to Islam between the Federal and state governments is clarified. The notion of accountability as is generally understood in the West is elaborated and subsequently compared with the concept of accountability from Islam's perspective. Prior studies on *waqf* and *zakat* examining the accounting and reporting aspects were reviewed. Issues such as poor documentation and record keeping, absence of sound accounting system, limited disclosure on the level and types of information, absence of separate financial statements are some of the pertinent findings of such studies. The paper also raises important questions about the validity of the current accounting practices of WZB and put forth various suggestions for future research. Finally, the initiative by the Accountant General's Department (AGD) to develop a financial accounting and reporting framework and standards for WZB is indeed laudable, timely and significant for the proper development of annual performance initiative should involve reporting of SIRCs.

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However, such an initiative should involve regulatory bodies such as the Jabatan Kemajuan Islam Malaysia (JAKIM), SIRCs as well as academics. Expertise from both accounting and Sharia should also be involved in this endeavour.

Key words: Accountability, State Islamic Religious Councils (SIRCs), *waqf*, *zakat*, *baitul mal*

**Accounting and Accountability of *Waqf*,
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Introduction

This paper is a review of the literature on accounting and accountability of *waqf*, *zakat* and *baitul mal* (WZB) in Malaysia with the primary aim of ascertaining the extent relevant information is disclosed and how accounting is practiced in such organizations. This would be the precursor to the empirical work that will be subsequently undertaken. Much has been written on the mismanagement of religious organizations and the need for such organizations to discharge accountability satisfactorily (e.g. Sapongi et al, 2014;, 2014; Hamdan and Osman, 2016). Given that accountability, to some extent, is manifested in the accounting and reporting aspects, prior studies examining the institutions of WZB have also focused on these areas in addition to examining the efficiency and effectiveness of such organizations. Studies focusing on performance measurement of WZB have indirectly also dealt with issues pertaining to accounting and reporting primarily because performance measures generally rely on accounting figures. Accordingly, the review of literature on accounting and accountability of WZB will also include those studies focusing on performance measurement. Specifically, this paper will focus on three pertinent issues. The first is the concept of accountability as it relates to WZB.

Second is a review of accounting practices and finally the reasons and challenges faced by these organizations. The paper will be organized as follows. Given that *waqf*, *zakat* and *baitul mal* are under the purview of the State Islamic Religious Councils (SIRCs), section 2 provides a discussion on the role of SIRCs in the management of WZB. Section 3 elaborates on the concept of accountability in Islam while section 4 focuses on the accounting for WZB and its related challenges. Finally, section 5 concludes with some recommendations for future research so as to bring the accounting and accountability of WZB to a higher level than what it is, presently.

The State Islamic Religious Councils (SIRCs)

It is important to understand the structure of the administrative machinery of Islamic affairs before a full discussion of WZB is undertaken. In Malaysia, the administration of Islamic affairs in each state is laid out in Article 3 of the Malaysian Constitution. Specifically, the Constitution states that the powers on matters pertaining to religious affairs and Malay customs are vested in the Malay rulers and their respective state governments. Thus, each state government enacts its respective laws to govern the administration of Islam and its affairs. This has given rise to varied interpretation and hence the implementation of Islamic religious practices between states. An interesting and pertinent point to note here is that there is a unique demarcation in powers and authority in policies on Islam and Malay customs between the Federal and state governments. The Federal government machinery and its mechanisms have no legislative authority on matters pertaining to religious affairs and Malay customs. Given this, Islamic institutions (such as *Jabatan Zakat*, *Waqf* and *Haji-JAWHAR* and *Jabatan Kemajuan Islam Malaysia-JAKIM*) set up by the Federal government have no power to

impose their policies on state governments thus creating an implicit tension between the Federal agencies and state agencies.

The present administrative structure of Islam and its affairs at the state level consists primarily of the State Islamic Religious Council (SIRC) and the State Islamic Religious Department (SIRD). The former formulates policies for the administration of Islam and its affairs, while the latter is responsible for carrying out such policies developed by the SIRC (Mahamood, 2006). Presently, the SIRD forms part of the state government's administrative structure and its primary role is to implement policies on the development and advancement of Islam that have been laid out by the SIRC. Its varied roles include overseeing the running of the Shari'ah Courts in each of the respective states, providing religious (Islamic) education through schools, courses and seminars, as well as the monitoring of religious activities undertaken by mosques and related agencies. It is important to note here that while *baitul mal* is an all-encompassing terminology that refers to the public treasury of the Islamic state, in our paper, *baitul mal* are funds other than the *waqf* and *zakat* funds collected by the SIRCs. This is primarily due to the important fact that *waqf* and *zakat* funds are generally handled by specific departments of the SIRC and accounted for separately due in part, to the large amounts received. Thus, in reporting its activities, each SIRC would have to account for all three funds, *waqf*, *zakat* and *baitul mal* respectively.

Accountability as the Foundation of Accounting

A discussion on the concept of accountability naturally precedes any description on the accounting practices of any organization as accountability and accounting is very much related. Sinclair (1995), writing from a managerial view, categorises accountability

into categories accountability into 3 forms: fiscal accountability, process accountability and programme accountability. The first measures the actual application of resources against predetermined standards while the second relates to the deployment of particular processes. Finally, programme accountability focuses on the achievement of the outcomes of pre-agreed or pre-determined targets. Viewed from a managerial perspective, accountability is considered discharged once it fulfills the target set (i.e. employing a standard process with appropriate funds and achieving the programmed output. Gray, et al. (1987), looking at accountability from an accounting perspective, argue that accountability refers to “the onus, requirement or responsibility to provide an account (by no means necessarily a financial account) or the reckoning of the actions for which one is responsible” (p. 2).

This necessitates the need for some form of a feedback-loop to indicate the discharge of accountability. From an accounting perspective accountability may be discharged through providing in information in the form of a report. This “accountability report” may include financial and non-financial information and may, to some extent, be verbal (i.e. orally discharged¹). In Islam, accountability flows from the concept of *amanah* (trust) (Faruqi, 1992) and *amanah* is related to another important concept in Islam, *khilafah* (vicegerency). Thus, the Islamic notion of accountability is different from that which is generally understood in the West. In Islam, accountability is viewed from two different perspectives: man’s accountability to God, and man’s accountability to other men (i.e. society). Thus, an individual worships God and executes all his duties as a *khalifah* (vicegerent). This constitutes his primary accountability. Secondary accountability is established through a contract between people. More importantly, the individual’s relationship with other individuals mirrors his

relationship with God (Sulaiman, 1997). The transcendent accountability to God constitutes the ‘vertical’ accountability and the accountability to other individuals as the ‘horizontal’ accountability. Essentially, agency contracts between owners and managers, contracts between employers and employees or contracts between superiors and subordinates would constitute the ‘horizontal’ accountability (Ibrahim, 2000). More importantly, the concept of *khilafah* regards the ownership of resources as a God-given trust or *amanah* given to every human being. In the context of WZB what it means is that any financial resource made available to WZB is made in the form of a trust (*amanah*). Thus, each SIRC is recognized as a trustee for *waqf*, *zakat* and *baitul mal* funds received. The importance of each SIRC in fulfilling that *amanah* (of the funds entrusted to them) is imperative. The types of information (both financial and non-financial) disclosed by each SIRC in its annual report may reflect on the extent it discharges its secondary accountability.

According to Zakari (2013), from the perspective of charities and non-profit organizations, three types of accountability are pertinent: upward, downward and holistic accountabilities. Upward accountability is basically accountability to donors, funders and oversight bodies (Christensen and Ebrahim, 2006). Downward accountability concerns accountability to beneficiaries (Kilby, 2006). Such an accountability is less institutionalised and depends more on felt responsibility (Christensen and Ebrahim, 2006). Christensen and Ebrahim (2006) asserted that more often than not downward accountability is neglected or, at best, less emphasized. This may be due in part to the fact that such organisations are normally not required by law to offer to their constituents the needed control for genuine accountability (Kilby, 2006). The focus on discharging downward accountability should not be at the

¹See O’Dwyer & Unerman (2008, p.85)

expense of upward accountability. Hence, there is a need for an integration of the two forms of accountability which is subsequently termed holistic accountability. Holistic accountability encompasses broader forms of accountability (O'Dwyer and Unerman, 2008) as it is implicitly ingrained with stakeholder engagement and participation that seeks to balance upward and downward accountability (Osman, 2010).

In summary, the Islamic concept of accountability, *taklif* (Abdul-Rahman & Goddard, 2007) offers a holistic approach to understanding the accountability relationships in the management of and accounting for WZB in Malaysia. Additionally, the accountability framework premised on the principal-agent relationship can also clarify the concept of trusteeship in SIRC towards the WZB resources received. Embracing its primary accountability to God and secondary accountability to contractual parties and supervisory agencies is likely to prompt a high standard of reporting thus minimising the costs of asymmetric information resulting from the principal-agent relationship. Given this, each SIRC is held accountable for the efficient and effective management of these resources. Herein lies the need for a proper accounting system to be in place. Gray and Jenkins (1993) support this contention somewhat when they argued that accounting is an information system that should be judged on its contribution to management effectiveness. More importantly, providing relevant accounting information may improve the effectiveness of an entity's management. Thus, prior research examining the performance of WZB rely to a great extent on the accounting and reporting of such organizations. Hence, as alluded to earlier, the review of literature on accounting practices of WZB cannot discount those studies examining the performance of these institutions.

Accounting for WZB

Baitul mal, as it is traditionally understood, refers to the public treasury of the Islamic state. As alluded to earlier, in Malaysia however, the term *baitul mal* takes on a slightly different perspective. Funds of the SIRC that are other than *waqf* and *zakat* are regarded as *baitul mal* funds. Given that each SIRC has an important mandate to supervise and manage funds pertaining to WZB funds in Malaysia, a study examining the accounting practices of WZB would refer to the accounting practices of the SIRC.

The dissemination of accounting information can be regarded as an important mechanism through which major elements of accountability may be discharged (Ebrahim, 2003). Carnegie and West (2005) support this contention when they argued that communicating accounting information has the primary aim of enabling appropriate evaluation of accountability. Thus, through proper accounting and reporting, the stakeholders could monitor how an institution such as the SIRC are managing the *waqf*, *zakat* and *baitul mal* funds entrusted to them in a satisfactory manner. Consequently, this reflects on the accountability of these organizations (Masruki and Shafii, 2013).

According to Palmer and Vinten (1998), the key issue in charity-related reporting is the readability and comprehensibility of the information being reported. Generally, readers of such organizations seek information on the utilisation of resources and the movement of charity funds during the year. Similarly, the stakeholders of WZB would also require information on how much resources were received, the types of resources as well as the manner in which it has been used. However, Patton (1992) argued that the extent of information reported in the financial statements is dependent upon the nature of the relationship between the accountant and the accountee.

Prior research focusing on the accounting and reporting practices of SIRC's or *baitul mal* is rather limited. If such studies were undertaken, it was with a view to examine, more specifically, the accounting and reporting practices of *waqf* and/or *zakat*. Given this, the review of literature will generally focus more on the accounting of these two types of funds. Additionally, studies investigating performance of *waqf* and *zakat* are also reviewed as performance measurement generally rely on accounting and reporting practices and most importantly, the reliability of such studies is dependent on the quality and quantity of information disclosed.

Accounting for Waqf

Budiman (2010) and Haneef (2010) classified prior studies on *waqf* into its history, management and administrative challenges, *waqf* development, *fiqh* issues, laws of *waqf*, *waqf* deed, types of *waqf*, women and *waqf*, socio-economic and political role of *waqf*, *waqf* accounting and financing, comparative studies and country cases (e.g. Cajee 2007, 2008; Pirasteh and Abdolmaleki, 2007; Rashid, 2007; Hasan, 2007; Cizakca, 1998; Hoexter, 1998; Shatzmiller, 2001; Rashid, 2002; Mustaq, 2005; Toraman, 2007; Qasmi, 2002; Mahamood, 2006 and Mahmud & Haneef, 2010). Specific to accounting for *waqf* the focus of prior research includes record-keeping and documentation, the need for the development of *waqf* accounting standards, accountability and transparency issues as well as performance of *waqf* institutions.

Abdul-Rahman et al. (1999) explored the accounting and administrative practices relating to *waqf* of all SIRC's in Malaysia. Their study found, among other things, evidence of poor documentation and record keeping, absence of sound accounting system and seemingly chronic accountability lapses. Marsoof (2004)'s study on *waqf* administration in Sri Lanka found evidence of

poor management of *waqf* assets. Extending the preliminary study of Abdul-Rahman et al. (1999), Mohd-Zain (2005) investigated the disclosure practices on *waqfs* for all 14 SIRC's in Malaysia. She then compared the results with that of Abdul-Rahman et al (1999). There appeared to be very minimal improvement on the level and type of information disclosed from 1999 to 2005. The level of disclosure was still low. Additionally, SIRC's did not maintain proper *waqf* assets accounts and that annual reports were not prepared on a timely basis. The majority of the SIRC's had outdated reports. Generally, there were no allocation for depreciation of *waqf* assets and no evidence of separate accounts for specific and general *waqfs*.

Yaacob's (2006) study, again examining *waqf* accounting practices, focused on just one SIRC, that of the Federal Territory. The results of his exploratory and descriptive study revealed some degree of improvement in record keeping although there was no specific financial statement dedicated for *waqf*. There was also no attempt to report on the different types of *waqf*, separately. Concerned with the same accounting and managerial issues of *waqf*, a replication of this study was undertaken a year later by Ihsan (2007). He scrutinised the accounting practices of two Indonesian *waqf* institutions, Dompot Dhuafa and *Badan Wakaf Universitas Islam Indonesia* (UII *Waqf* Foundation). There appeared to be a lack of uniform accounting practices between the two organizations. Additionally, each of the organizations discharged its public accountability and transparency according to how they have interpreted their responsibility and accountability towards their constituents.

Yaacob and Nahar (2011) recently undertook a study to investigate the accounting, reporting and management practices of a Malaysian cash *awqaf* management institution over a six-year period, from 2000 to 2005.

While they found the management of the institution has discharged its accountability satisfactorily, they felt that there was still room for improvement. Sulaiman, et al. (2009) using the International Islamic University *Waqf* Fund (IIUMWF) as a case study, suggested three key performance yardsticks of *waqfs*; efficiency, economy and effectiveness. Although these three measures were proposed, they could only determine the efficiency criterion as information disclosed was not adequate to determine the economy and effectiveness of the IIUMWF. A more recent study undertaken by Chowdhury et al. (2012) is not so much on accounting but more on performance assessment. From a synthesis of past studies they put forth a myriad of problems in *waqf* administration in Malaysia and subsequently provided recommendations for improvement.

Accounting for zakat

Specific to *zakat*, various studies have investigated the effectiveness and efficiency of *zakat* institutions in managing *zakat* funds (e.g. Ali, 1990; Ismail, 2000; Noor et al., 2004; Dollah et al., 2004; Halidan, 2006; Ismail, 2006; Kamil, 2005; Abu-Bakar et al., 2006; Zainal Abidin, 2006). Most have found that disclosure of information on amount disbursed and to whom it was expended was clearly lacking (Wahid and Kader, 2010). Additionally, the large amount of *zakat* funds not disbursed at the end of the accounting period was another contentious issue. As alluded to elsewhere in the paper, the type of information to be reported is an essential issue for WZB. Given this, it is important, in the first instance, to identify the types of information users consider relevant. Determining who the stakeholders are will have a bearing on the types of information to be disclosed (Connolly and Hyndman, 2013). Similarly, Zainon et al. (2014) supported this contention somewhat when they argued that

it was necessary to identify the information needs of stakeholders of charities in order to ensure that information disclosed are relevant. This is important as disclosure of information that meets the needs of the stakeholders could strengthen and sustain the charity's positive relationship with its donors. They went on to suggest a checklist of items that could assist preparers to undertake reporting for charity so as to satisfy the stakeholders' need for useful and relevant information. Consistent with the preceding argument, Sapongi, et al. (2014) developed a disclosure index to enable one to determine the quality of information disclosed by *zakat* institutions.

Challenges

The lack of systematic accounting system, the nonexistence of detailed public information and the relative lack of coordination of these institutions by the federal authority in Malaysia are some of the reasons affecting the quality and quantity of information disclosure of WZB (e.g. Abdul-Rahman et al., 1999; Nahar and Yaacob, 2011; Yaacob and Ibrahim, 2006; Siraj, 2012; Mohd-Zain, 2005). Further, the lack of enforcement and experienced accountants have also contributed to the less than satisfactory accounting and reporting practices of SIRC's. Specific to *waqf*, Adnan et al. (2007) argue that the fundamental problem that has led to the inconsistencies in recording and reporting of *waqf* in Malaysia is the absence of a conceptual framework for financial reporting of *waqf*. Hamdan & Osman (2016) specifically argued that such a framework must have accountability as the primary objective and decision usefulness an ancillary objective. Adding to the discourse and specific to *zakat*, Nahar and Yaacob (2011) argue that the use of commercial enterprises accounting prescriptions is inconsistent with the underlying objective of the SIRC, which is nonprofit in nature. The information reported in the financial statements that use such accounting

prescriptions does not truly reflect the reality of *zakat* transactions.

Given that information disclosed in the financial reports of SIRC is indeed important as it enables *waqf* donors and *zakat* payers to assess the entity's performance, there is thus an urgent need to ensure that information disclosed should reflect a true and fair view of the state of affairs of the organization. Specifically, stakeholders are interested to determine if funds entrusted to the SIRC have been properly managed. Discharging accountability satisfactorily through greater transparency in reporting would enable the SIRC to gain public trust and confidence. Abdul-Rahman et al (1999) suggested that proper accounting procedures be established at each SIRC. A similar contention is echoed by Mohd-Zain (2005) when she proposed that proper guidelines and a procedures manual be developed to account for *waqf* assets. Additionally, she suggested that SIRC employ experienced accountants since such accountants, in her opinion, will be able to help SIRC in maintaining *waqf* accounts. However, having experienced accounts does not necessarily translate to better reporting as these accountants may just perpetuate what is currently being practiced and what is presently done may not be adequate to meet the needs of relevant stakeholders. This has led Adnan and Abu Bakar (2009) to recommend that a conceptual framework for financial reporting of *waqfs* be developed as the absence of a framework is the primary reason for the inconsistent and varied reporting of *waqfs* in Malaysia. Similarly, a conceptual framework for the accounting for *zakat* and *baitul mal* should also be developed.

Yaacob (2006) and Nahar and Yaacob (2011) take a different stand. They proposed that SIRC should adopt the UK Statement of Recommended Practices for charities (SORP 2005) for reporting purposes. Their

suggestion stems from the fact that since *waqf* and SIRC are basically non-profit oriented, adopting the accounting and reporting practices of commercial enterprises would not be appropriate (Nahar and Yaacob al. 2011). Adnan (2005), on the other hand, argues that *waqf* can operate both as a social (non-profit) organization as well as a commercial enterprise. Given this, he asserts that for the former, one can apply accounting for non-profit organisations while for the latter, accounting for commercial organizations can be used. This seems to suggest that in generating income for *waqf* assets, one should adopt the accounting practices of any business organization thus implying that a separate set of accounts specific for the accounting of *waqfs* should be in place at each SIRC. The same goes for *zakat* and *baitul mal*. Subsequently, these WZB accounts will be consolidated. Accounting for WZB separately before undertaking consolidation at the level of the SIRC will enable each SIRC to address the accountability and transparency lapses in the management and accounting for WZB.

Conclusion and Future Research

On the basis of the literature just reviewed, there seems to be a general consensus amongst authors of prior research that the level of information disclosed by WZB in Malaysia is less than satisfactory. Accordingly, this appears to imply to the less than adequate discharge of accountability by SIRC. Prior studies appear to have made very general suggestions on what WZB institutions should do to discharge accountability satisfactorily. These include the need to have a proper accounting system, better and greater disclosure of information and more effective and efficient management of these organizations. Clearly, what is needed is a prescription on the specifics of what form accounting for WZB should take and the types of information that should be

disclosed. For example, how should *zakat* funds be treated in the books of the SIRC's? Is it correct for such funds to be treated as income of the SIRC as is currently done? What about expenses charged to WZB funds? Should only direct expenses be matched with those funds? Should separate books be kept for *waqf*, *zakat* and *baitul mal*? In line with this, should fund accounting be adopted by SIRC's so that information gathered for each type of funds become more transparent? Specific for *waqf*, should general and specific *waqf* be accounted for separately? While authors of prior research have argued for the need of a conceptual framework, how that framework should be developed and the form it should take was not discussed in their paper. Should the conceptual framework be developed by establishing objectives (and concepts) based on the principles of Islam and its teachings and consider these objectives relative to contemporary accounting thought? Alternatively, should we start with the objectives established in contemporary accounting thought and test those against the dictates of the *Sharia*².

Most importantly, the questions just raised cannot be answered only by accountants. Experts from both accounting and *Sharia* need to work together so that the accounting and reporting aspects are aligned with the *Sharia*. Perhaps what the second caliph, Umar, is reported to have said on how public monies should be accounted for is relevant when developing a conceptual framework on accounting for WZB. He was reported to have said:

"In my opinion, there are only three things to be done with respect to public money: it should be collected with due right, it should be given to whom it is due, and it should be denied from improper use. My position vis-a-vis public money is similar to that of the guardian

*that of the guardian of an orphan. If I can afford it, I will take nothing out of it, if I need it I will take only what is customarily required"*³

Thus, the above can act as a general guideline on how an accounting system for WZB should be developed. It is important for there to be a proper accounting system that can be used across all SIRC's as this will serve as a means of assessing and comparing the performance of each SIRC. Herein lies the importance of promulgating standards. The initiative by the Accountant General's Department (AGD) in collaboration with University Kebangsaan Malaysia (UKM), University Utara Malaysia (UUM) and International Islamic University Malaysia (IIUM) to develop a financial accounting and reporting framework and standards for WZB is indeed timely and significant for the proper development of annual performance reporting of SIRC's (Bernama, 2016). Needless to say, such an endeavour would also enable each SIRC to fulfil a basic but important level of accountability before they could advance to a higher level of accountability. A higher level of accountability generally means that both quantitative and qualitative information are reported and outcome and results based information are disclosed. This is indeed significant since a *waqf* donor, a *zakat* payer or the beneficiaries for that matter, need to be kept informed as to the purpose for which the funds have been used and how well the funds have been employed to yield optimum benefit. For WZB, its perpetual existence lies in its financial strength. Thus determining its performance is crucial. What is indeed most pertinent is that performance measurement can only be undertaken satisfactorily if the information disclosed is reliable and adequate.

²Conceptual Framework for Financial Reporting by Islamic Financial Institutions

³AbĒ YĒsuf, KitĒb al-KharĒj, (Cairo: Maktabah al-Salafiyah, 1397), 127.

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