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Mandatory Reporting Issues in Malaysian State Islamic Religious Councils (SIRC): Evidence from Interviews

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Abstract: This study focuses on State Islamic Religious Councils (SIRC) in Malaysia which were established for the social welfare under the purview of state enactments in an Islamic setting. The uniqueness of the political system and social values have affected SIRC including their reporting practices. In the interest of public accountability which respects the public to get access information about SIRC as public entities, this study discusses on the mandatory issue of the annual reporting for SIRC from the eyes of SIRC accountants, regulators, auditors and users by interviewing. It was found that the limits of authority between the federal and state governments can best explain why an annual report is not mandatory. Such as lack of enforcement is the main reason for the inconsistency of the annual report disclosure of SIRC. However, since, most SIRC accountants claim that they are becoming more aggressive in issuing annual reports, it would seem that now is a good time to propose the adoption of best practice reporting framework that meets the expectations of various stakeholders as posits in public accountability notion. As such, this study is able to provide empirical contributions to the Accounting literature on regulatory framework.

Key words: State Islamic Religious Councils (SIRC), public accountability, reporting, regulation, report, claim

INTRODUCTION

State Islamic Religious Councils (SIRC) in Malaysia are sole trustees and responsible for managing the Muslim wealth revenue derived from zakat (alms), waqaf (endowment) and mal (treasury). SIRC are one of the public service entities that were established within the confines of Islamic law. The political and social factors affecting SIRC are unique and this has inspired this study to focus on SIRC. The importance of SIRC is examined from both sides of these religious organisations as administrators of huge funds and from the perspective of public accountability. Public accountability urges the citizenry right for information with regards to public services.

SIRC are state statutory bodies which were established under the state enactments in the respective state (except SIRC1). SIRC1 was recognised as a federal statutory body under the Ministry of Finance (MOF) at federal level. Treasury Circular 4/2007 which was issued by the MOF, provides that an annual report is required by every federal statutory body and this provision applies to SIRC1. This requirement, however, does not apply to other SIRC, however, they were established under the state enactment in the respective state. All SIRC are audited by the National Audit Department or Jabatan Audit Negara (JAN).

Although, they are not required to prepare annual reports (except SIRC1), a financial statement is mandatory and is audited by the JAN. As there is no enforcement on the preparation of a comprehensive annual report in the provision of state enactment an audit certificate is issued based on financial statements, not the annual reports.

Within the banner of public accountability underlying this study, numerous groups of stakeholders had mixed opinions on the mandatory issues of annual reports for SIRC. This study aims to discuss on the mandatory issues of the annual reporting for SIRC from the eyes of accountants, regulators, auditors and academia.

Literature review: In the interests of public accountability which respects the right of the public to have access to information about government entities, this study reviewed related studies on disclosure of public sector. Several studies have been conducted to satisfy the public through providing an external report, so as to discharge accountability of the reporting entity. Some of the studies are Coy *et al.* (1994), Hooks *et al.*

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(2012), Ntim *et al*. (2017), Tooley and Hooks (2010). However, external report, so, called an annual report is not mandatory for some organisations unlike listed companies. Only the audited financial statement is mandatory but not for other parts of the report such as Corporate Social Responsibilities (CSR) and organizational activities and structure, information on board of directors.

Due to the voluntary nature of annual report, previous studies have proven that such limited disclosure (Aly *et al*., 2010; Hussainy *et al*., 2011) and even lack of reporting among the public sector organisations (Abdul-Rahman and Goddard, 1998; Siti-Rokyah, 2005). A review of previous studies showed that there are a growing number of public sector studies that focus on comprehensive reporting in developed countries. However, studies in developing countries such as Malaysia are still scarce. Studies either specifically examined the financial information such as Combs and Tayib or comprehensive reporting of Federal and local government such as Mucciarone and Neilson, Nichol and Taylor.

Tayib limited their study to financial reporting of local authorities. They compared the type of statements presented in annual financial accounts with the Federal Treasury Circular 1/1998. Another comparison was made between the financial accounts and the expectations of taxpayers. The study concluded that there is a wide gap between taxpayer's expectations and reported information provided by the local authorities, due to its voluntary report nature.

Combs and Tayib conducted a comparative study in which they evaluated disclosure in published annual financial reports and accounts of local authorities in the UK and Malaysia. They developed an index based on the Code of Practice for Local Authority Accounting in the UK issued by CIPFA but applied the index to a sample of local authorities from the UK and Malaysia. It was found that local authorities in Malaysia had a lower level of compliance with the CIPFA compared to those in the UK. This was due to the low standard of detailed accounts as compared to the local authorities in the UK. As such, it appears that quality of reporting is open to debate apart from the enforcement.

Considering more comprehensive reporting rather than only financial aspects, Mucciarone and Neilson examined annual reports but only focused on the performance indicators of Malaysian government departments. They conducted interviews to investigate the reporting of service performance indicators in the annual accounts of the departments. It was inferred that a low level of disclosure of efficiency indicators are reported without effectiveness indicators.

On the other hand, Nichol and Taylor examined the annual public accounts of the Malaysian ministries to identify performance reporting in terms of the nature, extent of disclosure of information. They carried out a content analysis using the framework of Hyndman and Anderson. It was found that the public sector performance reforms had no significant impact on the performance and accountability reporting in the Malaysian public sector.

Hooks *et al*. (2012) extended this line of study by developing a disclosure index for local government performance reporting. The performance items include financial performance, non-financial performance and performance indicators while considering the expectations of the broad stakeholders via. a questionnaire survey. While Nichol and Taylor examined the performance and accountability related information using a form-oriented content analysis, Hooks *et al*. (2012) used a self-developed disclosure index to identify the extent and quality of disclosure. However, despite of the non-mandatory of the disclosure, to the best knowledge of researcher, none of the study examining constraints of non-mandatory of disclosure.

Therefore, this study aims to extend the above studies by examining the reasons of non-mandatory disclosure. This study contributes to the literature on regulatory framework of accounting and reporting, especially in public sector. The qualitative approach used in this study could investigate the issue in-depth.

MATERIALS AND METHODS

Semi-structured interviews were conducted to address regulation issue. Specifically, these investigated explaining why annual reports are not mandatory. The interviewee included different groups of stakeholders under the banner of public accountability. They were classified into three groups; preparers (SIRC accountants), regulators (national accountants and auditors who are involved in auditing SIRC) and users (individual contributors cum academics who are actively doing research about SIRC, the public sector and Islamic accounting and zakat (hereinafter, researcher). Those internal interviewees including SIRC accountants in Central (AC1), North (AC2 and AC3) and East Coast (AC4) whereas external interviewees consisting of National Auditors (AU2 and AU3) as the users of annual reports, regulators-Accountant General Department (R1 and R2) and the public/users-contributors and Professor in Accounting, representing the public (C1 and C2).

RESULTS AND DISCUSSION

Arguments against mandatory annual reports: There are a number of constraints on mandatory annual reports for SIRC. Some of the arguments against are based on the boundary of power between Federal and state government, sensitivity to religion, audit requirements and the high burden placed on SIRC in preparing the annual report.

Boundary of power between federal and state government; this main reason as cited by a regulator: "The boundary of power between Federal and state government is the main reason for the annual report not being mandatory" [R1].

If SIRC1 is required to prepare an annual report every year but, it is not applicable to other SIRC. She added that SIRC1 is a federal statutory body whereas other SIRC are state statutory bodies. They are subject to the legal provision within their regional state enactment where they are not obliged to prepare annual report, since, they were established under the Secretary of Government (SUK) at their respective regional state levels.

An Auditor (AU1) explained that audit work is conducted based on the checklist provided as per the state enactment including financial reporting standards, financial management accountability index and decisions made by the Fatwa Council in the SIRC BOD. Another Auditor (AU2) further elaborated on the financial statements which cover only financial implication. However, providing only a financial statement is insufficient to explain accountability of SIRC in comparison with an annual report which is more comprehensive. Despite the limitation, regulator (R1) claimed: "As an auditor, I just audit financial statements of SIRC because it is mandatory. Ideally, the financial statements should be prepared according to the accounting standards. However, the accounting standards do not cover some of activities in SIRC such as zakat, waqaf and baitulmal. In other words, there is no accounting standard them. Alternatively, an auditor will refer to best practices of accounting which have been issued by JAWHAR and JAKIM which was introduced in 2003. Although the best practices of accounting could be used, they are still subject to the SIRC themselves. In fact, the best practices are not very clear in some activities, especially, waqaf" [R1].

She provided an example of the ambiguity of the guidelines. The said guidelines on the reporting for SIRC raised with JAWHAR. "JAWHAR does not make any policy in matters related to roles and responsibilities of SIRC. All matters pertaining to Islamic administration is responsible under the power of state government as provided in Federal Constitution, Schedule Ninth List 2" [R2].

Indeed, the preparation of annual reports is subject to the respective SIRC. She explained that probably, the guidelines referred to the best practices of financial management for SIRC but not specifically for reporting. Therefore, it seems there is no specific provision in relation to annual report preparation and presentation for SIRC. The boundary of power across states has led to the difficulties in coordinating guidelines for reporting at federal level. Hence, greater flexibility of reporting is appropriate due to the uniqueness of enactment in every SIRC.

Sensitivity to religious matters; an annual report is a detailed document explaining the operations of SIRC within the boundaries of Islamic thought, especially in terms of generating funds and their spending. Such information is very crucial to the contributors but provides contributors a sense of funding (Goddard and Assad, 2006). This might include sensitivity to religion as mentioned by Kamla (2007) and it was stressed personally by one Auditor and Regulator (AU1 and R1). This has contributed to the mandatory issuing of annual report for SIRC. An auditor explained: "SIRC are Islamic organisations and any faith-based organisation will be audited by the auditor in the respective religions, although, this is not stated in any legal provisions. As such, it shows the sensitivity of religion is embedded in the auditing process which also might influence the mandatory issue of annual reports for SIRC" [AU1]. In addition, a regulator said: "Personally as Malaysia is a multi-race nation in order to avoid sensitivity that might arise in relation to religion, it is sensible to make the financial statement mandatory. The details of SIRC activities could be circulated to muslims only" [R1].

She added that currently, bulletins on the activities undertaken have been distributed to zakat payers quarterly by the majority of the zakat centres. The centre was established by the respective SIRC themselves, explaining conducted activities. This practice has been supported by two SIRC accountants: "I agree because the public would like to know in detail about SIRC and it is part of the accountability of SIRC to provide such information via. the annual report. Bulletins and internet disclosure are additional mediums but the main is the annual report because it covers a year's activities. If the report is prepared in addition to bulletins, this is much more ideal" [AC1]. Moreover, another SIRC accountant said: "An annual report should be prepared for various stakeholders to inform people. If only financial statements are prepared, they might not understand the entire activities. Therefore, I agree if the comprehensive annual report is prepared and is available to the entire public" [AC4].

Burdensome to SIRC: An Auditor (AU1) believed that preparation of annual report was a burdensome task

(Goddard and Assad, 2006), especially in compiling and writing activities for every department. The challenging part was to coordinate the report which requires cooperation from all departments. He said, that due to the difficulty, SIRC focused on the mandated financial statements. Likewise, another SIRC accountant stated the difficulty in preparing annual report compared to mandated financial statement as follows: "annual report preparation involves all departments to report their activities, so, it is quite difficult to prepare. As for the financial reporting, although, we do not prepare annual reports, we still need to report in DUN state assembly and EXCO every year, ..., for approval" [AC4]. Therefore, he further suggested: "A template to prepare annual reports might encourage SIRC, …, considering non-accounting people, so that, it is understandable" [AU1].

In spite of the constraints of mandatory comprehensive annual reporting in SIRC, a Professor of Accounting (C1), representing users stressed that reporting is about awareness of SIRC on their responsibilities and to be seen to be accountable, through being transparent as agreed by the respondents rather than through enforcement. Indeed, he suggested that an existing practice of an annual report for SIRC could remain non-mandatory. The most important step was to make SIRC aware of their roles as not just government agencies but also as NGOs with religious obligations.

Arguments for mandatory annual reports: An Assistant Professor of Accounting argued: "An annual report for SIRC should be made mandatory by the higher authoritative bodies such as the Prime Minister's Department or the Ministry of Finance or it can be all of them. This is to prove that SIRC are very transparent and are held accountable, ..., so as to preserve a good image of Islam" [C2]. Her argument also cautioned that it was about accountability in Islam which claims to be transparent. Other arguments for mandatory annual reporting for SIRC were as follows.

Accountability discharge: An auditor highlighted the importance of making annual reporting mandatory, so as to encourage the public discharging of the accountability of SIRC. He mentioned: "An annual report should be provided to the public, especially, zakat payers to explain the activities of SIRC. To accounting people, surplus SIRC fund indicates positive financial management and these can be used to finance other activities. However, this gives issue to NPOs in which inquiries about the accountability discharge of SIRC might be raised in distributing the collected zakat which is not for profit oriented, the usage of funds and reasons for the increase and decrease of collection and distribution of funds" [AU1].

The above statement highlights several inquiries in SIRC that might be raised in the absence of a comprehensive report. An accountant in SIRC elaborated on the surplus of zakat by giving an example: "Let's say we received zakat funds on 10/2/2015 for RM1000. The money should be distributed at the latest by 9/2/2016 to fit a-year (haul) period. Why was there a surplus in the financial statement? This is because the accounting period covers the period from 1/1/2015-31/12/2015 and zakat payers usually pay zakat during Ramadhan or before the end of December every year. When they pay at the end of the year while we close our office at 5 pm, any payment received by 4.30 pm is accepted but definitely we are unable to distribute it and for that reason there is a surplus in the zakat reporting" [AC2].

In that instance, having a clear explanation from a particular SIRC would avoid any misunderstanding on the SIRC's accountability in distributing the zakat collection. An annual report is one of the mechanisms to resolve such negative inquiries into the SIRC accountability. The comprehensiveness of annual reports could explain both financial and non-financial matters as suggests by Ntim *et al*. (2017) which would eventually support the mandatory requirement for annual reports. This would facilitate understanding of financial positions and operations of SIRC to different backgrounds of users.

Preservation of Islamic image: According to an Assistant Professor in Accounting (C2), SIRC are known as Islamic organisations which mark them as one of Islam's ambassador's in Malaysia. This requires proper accountability and transparency, so that, the public will respect Islam as a religion. In particular, how Islam upholds the principles of integrity, transparency and justice should be complied with Shariah rules in terms of the management of SIRC funds. As for what SIRC are doing, this is being observed by all Muslims and non-Muslims. She additionally claimed: "if anything went wrong, people might pick up on this and see Islam as a not good religion which supports others who have already tarnished the image in our country" [C2]. An accountant, representing preparer in SIRC4 (AC2) added that an annual report could avoid any negative perceptions about a SIRC as an Islamic organisation. He took an example by stating that, although, there were a huge number of zakat collections, there were still many Muslims in Malaysia who requested fund assistance from churches and temples. For that reason, the public started questioning the role of SIRC in managing zakat distribution to those Muslims in need. Consequently, the scenario might tarnish the image of Islam in the eyes of non-Muslims. This indicates that the lack of transparency in SIRC might raise dissatisfaction among the muslims public; the more viral this impression becomes in the media the more the image of Islam will be tarnished and lead to the failure of SIRC being a good ambassadors of Islam. The reputation of SIRC as a mirror of the image of Islam has been put forward and should be brought to the attention of the top management of SIRC. For instance, the SIRC Accountant (AC2) highlighted that in 2014, the CEO of SIRC2, announced in the local media how much zakat collection and disbursements and other activities were undertaken. This was to prove to the public that SIRC had not used zakat collection funds but that they had been distributed through proper channels to the correct zakat recipients. The detailed report in terms of zakat collection and distribution to the numerous categories of recipients was reported in the board meeting which was their main concern. This is consistent with the stakeholder theory that suggests SIRC to meet the expectation of stakeholders (Masruki *et al*., 2016). They are held accountable to the SIRC board of directors for performance accountability as posits by Stewart (1984).

Being trustworthy: The final argument for mandatory annual reporting is to encourage the publication of annual reports without any excuse. Importantly such a report was believed by respondents to enhance trust from the public. Lee (2004) asserts that a vigorous public reporting could increase the confidence of the public in their activites. An accountant in SIRC11 said: "in order to increase trust of the public, we have to disclose our activities for the year to public" [AC4].

Another Accountant (AC1) stressed the public accountability which explicates the right for the information about the reporting entity and this has been also highlighted by Masruki *et al.* (2016). An accountant in SIRC 4 added that if the public would like to know about the SIRC, an annual report could be provided without hesitation because the report had been gazetted in the State Assembly (DUN). In the case of the absence of an annual report, only financial statements could be provided.

The financial statements are limited to figures explaining financial aspects and are not comprehensive. In this case, trust is less likely to be obtained given the limited information dissemination about the extent to which the SIRC are held accountable. As a result, many examples of negative inquiries about SIRC have been reported in several local media. Therefore, enhancing trustworthiness is important for the non-profit organisations (Iyer and Watkins, 2008) like SIRC.

The issue of mandatory reporting in SIRC is pointed out by a Professor in Accounting (C1). He stated: "whether an annual report should be mandatory to me is secondary. I think what should drive SIRC is not rules and regulations; what should drive it is accountability; that's number one. Secondly, it is actually the education aspect; it should be part of their responsibility as well and I believe if we focus too much on annual reports as a mandatory requirement then they have to do it and they will do it" [C1].

This implies that understanding the responsibility of SIRC is more important than enforcement of the annual report. The discussion on reporting should be treated as promoting the Islamic accountability (Rahman, 1998) rather than a regulatory debate. Another user, C1 further argued that the voluntary nature of zakat payment in Malaysia without incurring a penalty for not paying zakat is unlike tax, explaining why the annual report mandatory is inappropriate.

Apart from the mixed opinions on the mandatory nature of annual reports for SIRC, an accountant in SIRC3 highlighted: "any activity implemented through distribution of zakat funds is to seek confidence from the public. We try our level best to fully distribute the funds to all asnaf and in fact our CEO together with other state government agencies are also involved. They went to the rural area for delivering the zakat funds and the activities were published on our facebook. We inform our activities on our facebook and as a result, our zakat collection has increased and this indicates the public, especially, zakat payers, do trust us" [AC3]. The key finding here is that, although, SIRC have played their roles, these roles should be reported to the public to obtain the public's trust. An Assistant Professor, also a researcher stated: "there is nothing that should be confidential about SIRC. So, why not just disclose and disseminate the information. Even in Islam, we have the issue of whether we should be avoiding fitnah (defamation)" [C2].

The above argument is consistent with the element of Islamic accountability as stressed by user, C1. Anoterh user, C2 elaborated that if any information is the public's concern which has been questioned for some time, it is ideal for SIRC to publish that information, so as to avoid fitnah for better perception on SIRC. This supports the theme of this study under the banner of public accountability in particular to identify information expectations of the Muslim public as the SIRC' stakeholders.

CONCLUSION

From the above discussion, there are three arguments: boundary of power between federal and state government; sensitivity of religious matters and the high burden of preparing annual reports which could elaborate the reasons of the non-mandatory nature of the annual report. However, it is still sensible to highlight that an annual report is essential in addition to the mandated financial statements. More potential funding contributors would be attracted to SIRC due to better discharge accountability and preserve the Islam image through the trustworthy.

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