

Business Zakat Reporting of Co-operatives: Case Studies in Malaysia

TEH SUHAILA TAJUDDIN

Accounting and Finance Department, Faculty of Management and Muamalah
International Islamic University College Selangor (KUIS)
tehsuhaila@kuis.edu.my

FADILAH MAT NOR

Business and Management Department, Faculty of Management and Muamalah
International Islamic University College Selangor (KUIS)
fadilahmn@kuis.edu.my

ABSTRACT

Financial reporting of zakat on business is still lacking of guidance. There is no clear guidelines to be followed by business entities such as co-operatives, takaful service providers, banking and finance institutions in reporting the recognition of zakat, measurement for assets and liabilities for zakat, presentation and disclosure of zakat on business. In Malaysia, these institutions are not compulsory to comply with the Malaysian Accounting Standard Board (MASB), *Technical Release i-1: Accounting for Zakat on Business* and Accounting and Auditing of Islamic Financial Institutions (AAOIFI), *Financial Accounting Standard 9: Zakah*. There is inconsistency in the treatment of zakat among entities that pay zakat as no accounting pronouncement issued by the International Accounting Standard Board (IASB). The objectives of this study are to identify the reporting requirements of business zakat for co-operatives and to explore business zakat reporting among co-operatives in Malaysia. A qualitative research methodology is adopted in this study by comparing two co-operatives business zakat reporting. Content analysis on the annual reports of the co-operatives is conducted to identify the presentation and disclosures requirements for co-operatives and to what extent the business zakat accounting have been publicly reported. The outcomes of this study highlight the reporting requirements and current state of business zakat reporting of both co-operatives. Thus, this study provides suggestions for a business zakat reporting standard to provide a comparable and reliable financial information of co-operatives.

Keywords: Business zakat, requirements, assessment and co-operatives.

INTRODUCTION

Business zakat is imposed on net wealth of business at hawl completion. No matter whether the business is making profit or suffering lossess, the obligation to perform business zakat is under the responsibility of the business owners. In Malaysia, two recommended methods for assessing zakat on business are Growth Capital Model (*'urfiyyah* method) and Working Capital Model (*shar'iyah* method) have been introduced by Jabatan Kemajuan Islam Malaysia since 2001. Working Capital Model comprises current assets and current liabilities that subject to zakat is mostly adopted by businesses while Growth Capital Model focuses on non-current liabilities and owners' equity. Businesses are given options to use any of those methods with the resulting zakat payable being the same and some adjustments need to be

considered. Therefore, the assessment on business zakat should be carefully prepared and computed as it involves some technical adjustments on the certain assets and liabilities which are subjected to zakat and some not subjected to zakat.

Financial reporting of zakat on business is still lacking of guidance. There is no clear guidelines to be followed by business entities such as co-operatives, takaful service providers, banking and finance institutions in reporting the recognition of zakat, measurement for assets and liabilities for zakat, presentation and disclosure of zakat on business. In Malaysia, Malaysian Accounting Standard Board (MASB) has issued Technical Release i-1: Accounting for Zakat on Business (TR i-1) on 1 July 2006. It should be noted that TR i-1 deals only with financial reporting issues related to zakat on business. The TR i-1 is used to standardise the recognition, measurement, presentation and disclosure of zakat on business. However, co-operatives and other business entities are not compulsory to comply with TR i-1 and Accounting and Auditing of Islamic Financial Institutions (AAOIFI), Financial Accounting Standard 9: Zakah. As at the date of issuance of the TR i-1, International Accounting Standard Board (IASB) does not issue any accounting pronouncement related to accounting for business zakat. Thus, the treatment of zakat among entities that fulfil zakat is inconsistent and incomparable. The recognition for assets and liabilities which are subject to zakat are treated differently (Zahri, 2014). Thus, it leads to different treatment on current assets and current liabilities that subject to zakat which eventually it will be misleading and causes inaccuracy of the zakat payable computed.

There is a low compliance of business zakat reporting disclosure among selected Shariah companies as stipulated in MASB TR-i in their reports (Noor, Nik Mohd Rashid, & Mastuki, 2011). Business zakat reporting disclosure is encouraged among the Muslim-owned business entities as to give clear picture on how business zakat is computed, what methods used and what is the zakat expense or zakat payable amounts within one accounting period. If the business has fulfilled their zakat obligation, then they should disclose the zakat information on their annual report. Burhanuddin et. al, (2018) found that there is lack of transparency and disclosure practices on business zakat reporting among Islamic Financial Institutions. Therefore, it is timely to have a proper accounting standard for business zakat as it would improve the comparability of reported financial information on zakat.

This study aims to identify the reporting requirements of business zakat for co-operatives and to identify the extent of business zakat reporting between two co-operatives in Malaysia. A qualitative research methodology is adopted in this study by comparing two co-operatives business zakat reporting. By conducting content analysis procedure, Technical Release i- 1 Accounting for Zakat on Business issued by MASB and AAOIFI's FAS 9: Financial Accounting Standard for Zakat are critically analysed. By adopting case studies approach, content analysis on Financial Statements and Notes to the Accounts of two selected co-operatives are also reviewed to identify the presentation and disclosures requirements for co-operatives and to what extent the business zakat accounting have been publicly reported. The outcomes of this study highlighted the reporting requirements and current state of business zakat reporting of both co-operatives. Finally, this study provides suggestions for a business zakat reporting standard to provide such a comparable and reliable financial information of co-operatives.

EVIDENCES RELATED TO BUSINESS ZAKAT OBLIGATION

The obligation of zakat on business is derived from several evidences from al-Quran, al-hadiths, al-ijmak ulama and al-qiyas. The most prominent verse regarding zakat on business is as follows:

Allah S.W.T says, "O you who believe! Spend of the good things which you have earned, and of that which We have produced from the earth for you and do not aim at that which is bad to spend from it, (though) you would not accept it save if you close your eyes and tolerate therein. And know that Allah is Rich (Free of all wants), and Worthy of all praise"

(al-Baqarah : 267)

According to al-Tabari, (Muhammad, 2000), "*spend of the good things which you have earned*" refers to economic activities such as the business sector. Thus, business entities are obligated to perform zakat on what they have put on their efforts in generating income and profit. At the same time, the business entities have to ensure the business assets must be from halal sources and all the business activities too must come from halal activities or services. Imam al Ja'ssas and Imam Abu Bakr ibn al 'Arabi have been reported to assert the same opinion which zakat is obligatory on the trading activities (AI-Qaradawi, 1999: 204).

Hadith from Rasulullah s.a.w as narrated by Abu Dawud reported from Samurah ibn Jundub, **"The Prophet (s.a.w) used to order us to pay the sadaqah (zakat) on what we have prepared for trade (*urud al-tijarah*)"**

(Abu Dawud, 1557)

The above hadith clearly stated that zakat is obligatory on goods or inventories which are ready to be sold. Prophet s.a.w gave an order to perform zakat on business inventory. Many jurists referred business inventory as *urud al-tijarah*, which means any commodities obtained for the purpose of resale for profit (Abu Bakar, Ibrahim & Md Noh, 2014). However, some jurists defined *urud al-tijarah* differently and it has contributed to various business zakat accounting methods used by business entities (Zahri, 2014).

Ijmak ulama related to zakat obligatory is as reported by Aby Ubayd (1991). There is a report from Abu 'Amr ibn Hammas, from his father, who said:

"Umar passed by me and 'said, 'Oh Hammas, pay zakat of your possession (wealth)". I said, I' have nothing except hides and bags. He said, "Determine the price of these things and then pay their zakat"

(Abu 'Ubayd, 1991: 362).

Abu 'Ubayd al-Qasim (1991) reports the ways of calculating zakat as perceived by some of the great followers. He quotes Maymun ibn Mahran as saying,

"When zakat is due, calculate the amount of money, add to it the value of inventory and the amount of debts on customers that you expect to be paid, sum the total, deduct whatever debts you owe to others and pay zakat on the net".

(Kitab al-Amwal, 454, 1185)

TR i -1: PRESENTATION AND DISCLOSURE

In presenting the business zakat disclosure by co-operatives, para 15 specified that the amount of zakat assessed for the current period shall be presented as a line item on the face of the income statement. For disclosing the zakat obligation, Para 16 stated that an entity shall disclose in the notes accompanying the financial statements the (a) method used in the determination of zakat base; (b) its responsibility towards payment of zakat on business; and (c) major components of zakat. Further, para 17 described the components of zakat may include: (a) current zakat expense; (b) zakat payment; (c) zakat liability; and (d) any adjustments recognised in the period for zakat of prior periods. The computation of zakat on business is still remain the same as per calculation reported by Abu 'Ubayd¹. In today's modern businesses, adjustments on certain items of business's assets and liabilities are needed as to arrive at accurate business zakat payable and in compliance with Shariah principle. The analysis on presentation and disclosure of zakat information is discussed in results and discussion.

AAOIFI, FAS 9: FINANCIAL ACCOUNTING STANDARD FOR ZAKAT

The AAOIFI FAS 9 sets out accounting rules related to zakat on business issued in 1999 (Adel, 2013). It is a guideline used by IFIs for the accounting treatments related to determination of the zakat base, measurement of items included in the zakat base and disclosure of zakat in the financial statements of IFIs. The basis of AAOIFI classification is based on the well-known syari'ah classification of trade commodities for the purpose of zakat (A. R. Abdul Rahman, 2003). Para 8 stipulated that to disclose the method used for determining the *zakah* base and the rulings of the *Shari'ah* Supervisory Board (SSB). Para 19 added that disclosure shall be made in the notes accompanying the financial statements of the restrictions imposed by the SSB of the Islamic bank in determining the *zakah* base. AAOIFI FAS 9 could be considered by business entities for adopting the standard in Malaysia. However, it is inappropriate in the Malaysian context due to the accounting treatment prescribed are specific for IFIs; and it might run contrary to state or federal legislation in Malaysia (MASB, 2006).

FINDINGS AND DISCUSSION

As case studies approach is conducted, the co-operatives studied are named anonymously as COOP AB and COOP XY. Both COOP AB and COOP XY are registered under the Suruhanjaya Koperasi Malaysia and among the top 10 co-operatives in Malaysia. Overall, COOP AB are n compliance with MFRS in preparing its annual report. COOP AB presented zakat item in the Statement of Profit or Loss. In addition, there is further zakat reporting presented in the notes to account (2.4: iii) which explains that zakat item represents the business zakat paid by the group and co-operative which is in compliance with Shari'ah principles and it has been approved by the group and cooperative Shari'ah advisory board. COOP AB only presented the zakat paid for the year ended 31 December 2017 without a disclosure on method used in determining the zakat base. Even though the responsibility of paying business zakat has been discharged, the entity receiving the zakat payment is unknown. The components of zakat were not disclosed by the entity.

¹ Abu 'Ubayd al-Qasim (1991), *Kitab al-Amwal*. 454, 1185.

For COOP XY, it is found that the co-operative is in compliance with MPERS and Cooperative Act, 1993. COOP XY presented zakat item on the face of Income Statement. It also presented the method used for business zakat assessment in the notes to account (no: 17). The method used to assess the zakat on business is clearly stated i.e by using working capital model. COOP XY also revealed that all adjustments made on net assets are disclosed completely. In addition, the muslim ownership % and the zakat rate of 2.5% are also presented. COOP XY has reported its zakat payment in a very transparent and full disclosure. The computation of zakat base is clearly presented by using working capital model. The financial statements of Coop XY comprising a high quality information on business zakat reporting. The entity would be able to enhance the comparability of reported financial information on zakat.

CONCLUSION

Since there is no proper accounting standard for zakat on business in Malaysia, the presentation and disclosure practices of zakat are based on voluntary basis. Some entities voluntarily to disclose all information related to business zakat. However, some entities choose to disclose business zakat reporting in incomplete way and not very transparent. Thus, the users are unable to understand on how business zakat is assessed. The full disclosures of financial information should be promoted to zakat paying entity as it would enhance the integrity, transparency, reliability and truthfulness.

The use of different methods in computing business zakat should also be adopted as to ensure zakat computed, in line with the Shariah principles and to avoid zakat gap. is accurately Business zakat sector has shown a huge potential in zakat collection especially in Public Listed Companies (Abdul Wahab & Borhan, 2016). Thus the zakat gap should be narrowed by identifying means and ways to further promote the business zakat compliance among business entities.

This study also found that the integration between zakat assessment and zakat accounting are very crucial. It is known that the financial reporting prepared by entities is meant for various users including tax authorities but not covering for zakat authorities. Therefore, the business entities should furnish additional information for zakat authorities to compute the business zakat. Previous study by Abdullah Ibrahim, Abdul Kadir, & Syed AdwamWafa, (2012) stated that harmonization between zakat assessment and zakat accounting is highly needed.

Voluntary self-assess the business zakat is seen as a way to further increase the business zakat collection. It is almost the same with the self-assessment system implemented by individual or business entities in assessing their individual income tax or corporate income tax. However, to promote a self-assessment system, the shareholders and management of business entities should be equipped with ample zakat knowledge. Finally, the disclosure of zakat reporting should be promoting to Muslim business entities. It gives value-added to the business entity and could enhance the transparency of the entity and produce a good governance.

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