

# A Zakat Accounting Standard (ZAS) for Malaysian Companies

*Nur Barizah Abu Bakar*

## **Abstract**

This paper focuses on the need to harmonize the practice of zakat on companies throughout Malaysia by implementing a zakat accounting standard (ZAS). The objectives of this paper are fourfold: (1) to highlight the current practice of zakat on companies in Malaysia; (2) discuss the usefulness of AAOIFI FAS 9, MASB FRS *i-1*, and MASB TR *i-1* as guidelines for developing a ZAS; (3) suggest a collaboration by various parties designed to pool initiatives, knowledge, and skills to develop a useful and favorable ZAS; and (4) to demonstrate that without proper education and a strong political will, there is a little hope of making any ZAS a reality.

## **Introduction**

The lack of an applicable standard for corporate zakat has contributed to its diverse practice in Malaysia.<sup>1</sup> This diversity is also partly due to the Malaysian setting of zakat practice that each state governs its own zakat affairs. The absence of an applicable standard may not be noticeable right now, but it may become significant soon, especially when a cursory examination reveals that more companies are becoming aware of and more interested in fulfilling their zakat obligation. The problem is further exacerbated by the fact that the recently announced 2005 Malaysian government budget indirectly included zakat as part of the fiscal system through the tax deduction given to those companies that pay corporate zakat.

---

Nur Barizah Abu Bakar, MA, is a lecturer in the Department of Accounting, Kulliyah of Economics and Management Sciences, the International Islamic University, Kuala Lumpur, Malaysia.

Given the above scenario, I argue that there is an urgent need to develop a zakat accounting standard (ZAS) that companies can adopt and apply nationwide. Several people concerned with this issue are Abdul Rahman,<sup>2</sup> Amin,<sup>3</sup> and Nasir and Hassan.<sup>4</sup> Thus, I detail the benefits and advantages of having a ZAS in place and contribute to the literature by providing some suggestions and insights to the responsible parties who should take charge of making such a standard a reality. While I recognize the importance of standardizing zakat for other types of wealth, I do not elaborate upon this subject here.

My analysis and discussion of the above issues starts by describing the background of Malaysia's zakat practices, with special reference to the constitution. Next, I elaborate upon zakat's conceptual and practical dimensions as regards a company's wealth, focusing primarily on the Malaysian context for the latter. I then discuss the zakat system's dynamism as being in accordance with Islam; explain the applicability and usefulness of AAOFI FAS 9, MASB FRS *i-1*, and MASB TR *i-1* in developing the standard; and spell out the standard's objectives and merits. After commenting on which constituencies need to be involved in developing a ZAS, I conclude with the challenges of making such a standard a reality.

### **The Background of Malaysia's Zakat Practices**

All aspects pertaining to the administration of zakat are handled by the states through their respective Majlis Agama Islam Negeri (State Islamic Religious Councils [SIRCs]). This is attributed to the fact that the ninth schedule of the Malaysian federal constitution recognizes religious affairs as state, rather than federal, matters. Thus, zakat administration comes under the jurisdiction of the respective state or the prerogative of its ruler (sultan). The only exception is the Federal Territory, where the zakat law and administration are governed by the federal government.<sup>5</sup>

In all other states, the federal government's role is restricted to coordinating zakat matters among the states; in no way can it intervene in their religious or, more specifically their zakat, matters. Thus, ultimate power rests with the state government under its respective SIRCs. Even though the Federal Territory did establish a Department of Islamic Development (i.e., JAKIM) under the Prime Minister's Department to coordinate and bring some uniformity to administering Islam in Malaysia, its function remains purely advisory in nature. In addition, the recently established Department of Zakat, Waqaf, and Hajj, which is a unit under the Prime Min-

ister's Department, has a very limited role as regards monitoring the country's zakat practices.<sup>6</sup>

As a result, the practice of zakat varies according to the state's "will." Each state has its own zakat centers.<sup>7</sup> In most states, even the collection and distribution units are separated in order to uphold their independence. A zakat center would normally operate based on the advice and fatwas issued by each SIRC's fatwa council. These fatwa councils also become the point of reference for these zakat centers in carrying out their operations. In addition, each state has its own zakat law, which is considered part of the state enactment. Accordingly, each state formulates its own policy on zakat matters, including the method of collection, disbursement policy, administrative aspects, execution, and the degree of enforcement.

Such a degree of divergence has numerous drawbacks that affect all types of zakat. Therefore, the states need to harmonize their policies for the benefit of the country's Muslim population. In essence, this is my paper's central thesis. However, it has to be stressed here that this paper only focuses on the need to standardize the zakat practice for corporate wealth, although it does recognize that the disadvantages stemming from the lack of harmonization of zakat practices actually applies to all types of *zakatable* wealth. These drawbacks will be addressed indirectly while elaborating upon the benefits of harmonization.

### **Zakat on Corporate Wealth: Its Concept and Malaysian Practice**

Zakat, one of Islam's five pillars, literally means "increase, growth, and purification" as well as "blessings."<sup>8</sup> Its origin is found in Qur'an 9:103: "Of their goods, take alms, so that you might purify and sanctify them." Spiritually, paying zakat purifies and cleanses one from greed, selfishness, and arrogance.<sup>9</sup> Economically, at least in theory, paying zakat will enhance economic prosperity by transferring surplus wealth to the poor. This will increase their purchasing power and, hopefully, lead to a higher demand for goods.<sup>10</sup> Thus, zakat acts as a wealth-distribution mechanism to help close the gap between the rich and the poor.<sup>11</sup> Ideally, it could help establish a more prosperous society.

According to Nasir and Hassan,<sup>12</sup> paying zakat on one's business wealth is based on the Islamic concept of wealth being bestowed by Allah, the real owner of all wealth, as a trust.<sup>13</sup> In 17:26-27, 29-30, Allah enjoins proprietors to fulfill their financial obligations toward their fellow citizens and be mod-

erate in their private spending. According to Abdalati, the owners of wealth are not free to spend their wealth as they please; rather, rules related to spending as well as to earning income and wealth must be followed.<sup>14</sup> Thus, zakat enables those who have sufficient funds to play an important role and fulfill a sacred mission.

More specifically, in the context of corporate wealth, Abdul Rahman points out that Muslim companies are obliged to pay zakat as a contribution to social well-being and to fulfill their social accountability and ultimate accountability to Allah.<sup>15</sup> Bakar states that zakat is due on all valuable items and that the *`illah* for *zakatability* is the richness.<sup>16</sup> The basic principle of zakat on corporate wealth is based on merchandise goods (*`urud al-tijarah*),<sup>17</sup> namely, anything obtained for the purpose of trading to gain a profit.<sup>18</sup> The wealth becomes *zakatable* once it exceeds the *nisab*, which is calculated as the equivalent monetary value of 85 grams of gold. Once this requirement is met, zakat needs to be paid each year at the rate of 2.5 percent.

Based on an exploratory study conducted through interviews by Nasir and Hassan,<sup>19</sup> with zakat officers working at two zakat centers in Malaysia, zakat centers were found to have recommended at least five assessment methods for companies to calculate the amount of their corporate zakat: the net assets (or working capital), net equity (growth model), net profit after tax, combined methods, and dividend methods. These methods have been derived mainly from different interpretations of the relevant Shari`ah provisions. To help them assess this amount, most companies that want to pay it seek advice from the state zakat officers to help them calculate it based on their disclosed financial information.

With regards to recording and presenting this amount, Malaysian companies have also adopted diverse practices.<sup>20</sup> For example, some treat it as part of their non-operating expenses, some treat it as an exception item in the all-inclusive rule, and others regard it as a form of distribution to their shareholders. Given these diverse practices, Malaysian companies need a ZAS. As Nasir and Hassan correctly point out,<sup>21</sup> there must be a standardized method to calculate the zakat base, classify the zakat items, and disclose them in corporate financial statements.

The 2005 Malaysian government budget is one of the contributing factors highlighting this need. For example, the budget document proclaimed that any corporate zakat paid to a SIRC will be considered an allowable deduction. According to the Income Tax Act 1967, Section 44 (11) (A), only 2.5 percent of the aggregate income can be deducted. The percentage of this deduction is not our main concern; rather, our focus here is on the fact that

the zakat collected has been indirectly integrated into Malaysia's fiscal system by means of this special deduction. It follows that being part of the country's fiscal system, although in a very nominal and indirect way, zakat becomes more important. Thus, a proper zakat regulation and monitoring system is required, as is the case with any other component of the fiscal system. Given this orientation, I propose that a ZAS be developed, as a starting point, to serve as an appropriate medium and mechanism for regulating this particular divine system.

### **The Dynamism of the Zakat System**

Understanding and scrutinizing the issue of ZAS from an Islamic perspective is crucial to placing it in the right context and spirit and to ensuring that the noble aims of this divine system are preserved. Given this, we must first understand that since zakat is part of the *mu`amalah* system (economic dealings between people), it is subject to change to suit and remain relevant to humanity's socioeconomic environment,<sup>22</sup> which is based upon a specific time and place. In short, *fiqh al-zakat* (the rules of zakat) is progressive and dynamic, mainly because any society's socioeconomic development is itself dynamic.

The availability of various corporate zakat assessment methods shows that zakat is subject to change and variation. Islam allows considerable flexibility in using reason to solve new problems. In the case of zakat, *ijtihad* could be one of the best ways to devise new rules and regulations to deal with new situations.<sup>23</sup> Among the prime prerequisites of developing new zakat rules is that they benefit the general public (*maslahah`ammah*), avoid harm (*mafsadah*), serve the Shari`ah's objectives (*maqasid al-Shari`ah*),<sup>24</sup> and provide justice (*`adl*) to the majority. Thus, given that Islam allows variation in zakat affairs based on time and place, it would be unduly simplistic to say that it does not allow standardization or harmonization to achieve these same goals.

### **The Accounting Standard**

The term *accounting standard* refers to the accounting guidelines developed to deal with specific financial accounting and reporting issues. The main purpose of having a standard for zakat accounting practices is to narrow the areas of difference among those firms that pay zakat and those zakat authorities who manage zakat as it relates to the methods of disclosure, computation, and presentation of financial information in financial statements.<sup>25</sup>

Adopting a standardized method will improve the quantity and quality of the information found in published financial reports.<sup>26</sup>

### *AAOIFI FAS 9, MASB FRS i-1, and MASB TR i-1*

Based on the preceding discussion, one might reasonably ask whether there is any existing standard now in place that might help us develop a ZAS. To my knowledge, Saudi Arabia has at least one established ZAS. Issued by the Saudi Organization of Certified Public Accountants (SOCPA), it could serve as a model for developing a Malaysian ZAS. While interesting, the Saudi ZAS is beyond the scope of this paper. In the following section, I focus on two other important standards and a technical pronouncement, all of which are believed to have a greater influence upon or relevance to the Malaysian context.

#### **AAOIFI FAS 9 (ON ZAKAT)**

At the international level, the Accounting and Auditing Organization of Islamic Financial Institutions (AAOIFI), a Bahrain-based accounting and auditing standard-setting body, has issued a Financial Accounting Standard for zakat (FAS 9), effective from 1 January 1999 onward. The main focus is on Islamic banks.

This document can be said to represent a relatively comprehensive standard that covers various aspects of zakat accounting for Islamic financial institutions. For the purpose of this paper, its content can be classified into three main areas: determining the zakat base, measuring the items included in the zakat base, and disclosing the amount of zakat in the Islamic bank's financial statements. The following section briefly explains this standard's salient features.

Paragraph 2 of FAS 9 requires the use of different rates depending upon the calendar year used. The standard prescribes a 2.5 percent rate for companies using the lunar calendar and the slightly higher rate of 2.5775 percent for those using the solar calendar. The latter amount is designed to compensate for the fewer number of days per year in the Islamic calendar.

The same paragraph proposes two methods of zakat measurement: the net assets (net current assets) and the net invested funds (net owner equity) methods. The first method considers all cash, receivables net of doubtful debts, assets acquired for trading, and net financing assets (excluding unearned income) to be assets. Fixed assets and long-term investments are excluded. Thus, the *zakatable* amount is all assets minus the fixed assets, intangibles, current liabilities, and long-term investments. Under the second

method, the invested funds include paid-up capital, reserves, general provisions (investment risks), retained earnings, net income, and long-term liabilities. Thus, the *zakatable* amount is all funds minus the net fixed assets, investment not acquired for trading, and any losses.

With regards to assets valuation, paragraph 5 of this standard recommends that the cash equivalent value serve as the basis of valuing *zakatable* assets. As for treating zakat in the Islamic bank's financial statement, the standard requires it to be treated as a non-operating expense and included as a deduction from the net income. Paragraph 9 also recommends that any unpaid zakat should be treated as a liability.

AAOIFI FAS 9 lists eight disclosure requirements in the notes accompanying the financial statements: (1) the methods of zakat measurement used; (2) the ruling of the Islamic bank's Shari'ah supervisory board on zakat-related issues that are not included in this standard; (3) whether the Islamic bank, as a holding company, pays its share of its subsidiaries' zakat obligations; (4) the amount of zakat due from each share, in case the Islamic bank does not pay zakat; (5) the amount of zakat due from the equity of its investment account holders; (6) whether the Islamic bank collects and pays zakat on behalf of those of its holders who have investment and other accounts; (7) restrictions imposed by the Islamic bank's Shari'ah supervisory board in determining the zakat base; and (8) disclosure requirements listed in "Financial Accounting Standard No. 1: General Presentation and Disclosure in the Financial Statements of Islamic Banks and Financial Institutions" shall be observed.

Despite this standard's comprehensiveness, it is disappointing to note that the applicability of AAOIFI FAS 9 is rather limited, at least in the Malaysian context, in two ways. First, as the organization's name and therefore the standard implies, the AAOIFI-issued standard is only applicable to Islamic financial institutions (IFIs); it does not cover such other business entities as limited companies and partnerships.<sup>27</sup> Therefore, AAOIFI FAS 9 may not be immediately applicable to other entities.<sup>28</sup> Essentially, even if IFIs in Malaysia were to adopt it, several modifications would have to be made to bring it in line with the local banking regulatory environment.

Second, the standard's other limitation is attributed to the fact that it has not taken into account (which its formulators were not obliged to do) the unique features of Malaysia's society and legal framework.<sup>29</sup> This means that FAS 9 is not totally applicable to Malaysia due to the required compliance with the respective country's central bank guidelines (BNM) and by-laws, as well as other regulatory requirements and settings. It follows that this stan-

dard is not binding on IFIs in Malaysia as well as in many other Muslim countries.<sup>30</sup> Instead, it serves only as a guideline to which other countries do not have to adhere.

### **MASB FRS *i-1***

At the national level, the effort of the Malaysian Accounting Standard Board (MASB) to develop FRS *i-1* (the “Financial Reporting Standard: Presentation of Financial Statements of Islamic Financial Institutions”) is highly commendable. The MASB is an independent authority tasked with developing and issuing standards related to accounting and financial reporting procedures in Malaysia. It is also responsible for issuing new accounting standards as approved accounting standards as well as for reviewing, revising, or adopting current accounting standards as approved accounting standards. FRS *i-1* is the MASB’s first Islamic accounting standard designed specifically to meet the needs of Islamic financial practices and Malaysia’s regulatory and economic structures.

However, as its name implies, this standard merely focuses on presenting an IFI’s financial statements. Therefore, at least in the corporate sector, the FRS *i-1* standard has two inherent limitations. First, since it focuses on presenting and disclosing the financial statements of IFIs engaged in Islamic banking activities, other matters, especially those related to the assessment, are not included. A closer look reveals that the discussion on zakat only appears at three locations: (1) on page 12, paragraph 6, FRS *i-1*, when zakat is defined as “an obligatory contribution assessed based on certain assets owned by a Muslim that satisfy certain conditions and is to be distributed to specified categories of beneficiaries”; (2) on page 22, paragraph 49, when the information to be presented on the “Face of the Balance Sheet” or “Notes” is to be discussed. Here, it includes the provision of zakat as part of other liabilities; and (3) on page 27, paragraph 72, where it gives a short explanation regarding the need for IFIs to disclose their zakat obligations: “An IFI shall also disclose, where applicable, its responsibility towards payment of zakat on behalf of depositors, shareholders and others.”

Second, this standard is meant only for Islamic financial institutions. As a result, even the presentation and disclosure of zakat data that are made available may not be directly applicable to companies, even though on page 10, paragraph 4, the standard explicitly states that non-IFI institutions are encouraged to comply with it.

### **MASB TR *i-1***

Besides the FRS *i-1*, the MASB also issued an accounting pronouncement for corporate zakat, TR *i-1* (Technical Release *i-1* on “Accounting for Zakat

on Business”), that becomes effective on 1 July 2006. Basically, a “technical release” does not have the same legal force as a “standard.” Unlike a standard, which must be adhered to if required by any law administered by the Securities Commission, the Central Bank, or the Registrar of Companies (according to the Malaysian Financial Reporting [Amendment] Act 2004, part III, section 26[d]), a technical release simply provides guidance on applying generally accepted accounting principles to resolve a particular accounting issue.

According to the MASB, the main reason why it issued a technical release instead of a standard relates to the fact that many business-related zakat issues (e.g., zakat chargeability, calculation, determination of the zakat base, and eligibility of assets and liabilities) are considered to be outside its purview (see paragraph BC16 of TR *i-1*). In other words, they fall under the SIRC’s jurisdiction. As a result, TR *i-1* deals only with financial reporting issues related to a corporation’s zakat; hence, other decisions on a corporation’s zakat made by an entity should be subject to the conclusion reached in cooperation with the relevant zakat center.

This status quo presents the main limitation of TR *i-1*. Although the MASB highlights in the introduction of TR *i-1* (paragraph IN3) that the purpose of having a TR *i-1* is to standardize the recognition, measurement, presentation, and disclosure of a corporation’s zakat, this ideal objective is apparently far from feasible unless a corporation issues a comprehensive and authoritative ZAS based on a mutual agreement with the relevant SIRC, zakat center, and other parties, particularly the regulatory bodies.

### **The Usefulness of AAOIFI FAS 9 in Developing a ZAS**

From the preceding discussion, it can be concluded that Malaysia still has a long way to go before developing a suitable corporate zakat accounting standard. However, these standards and technical pronouncements can at least serve as a guideline for devising an actual ZAS.

AAOIFI FAS 9 offers useful guidance for the ZAS preparer. Abdul Rahman has criticized some of the salient features and guidelines of FAS 9 not only in the context of Malaysian IFIs, but also in the context of the country’s business environment.<sup>31</sup> While highlighting some limitations of the AAOIFI’s FAS 9 through addressing its three main parts (viz., “Scope of the Standard,” “Accounting Treatment of Zakat Base,” and “Disclosure Requirement”), he recommends ways to promulgate a standard that will be in accord

with current Malaysian regulatory requirements. It is believed that the MASB could adopt the AAOIFI FAS 9, albeit with several modifications, as proposed by Abdul Rahman,<sup>32</sup> to ensure the standard's suitability and relevance to local settings.

Quite in line with the above, the MASB has acknowledged the AAOIFI's contribution as instrumental to codifying accounting and auditing norms and rules. The MASB demonstrated this acknowledgment when it explicitly emphasized, in its FRS *i-1* (paragraph IN3, page 7) as well as in TR *i-1* (paragraph IN2), that it had given careful consideration to the substance of the AAOIFI Standards while formulating these and, at the same time, ensured that the former standard would be tailored to the needs of the Malaysian regulatory, legal, and economic structures. Although a discussion of a ZAS' components would make this study more stimulating and comprehensive, it is, unfortunately, beyond the scope of this paper.

### **The Merits of Having a ZAS**

Barjoyai outlines five reasons for developing accounting principles for zakat: (1) to observe a minimum standard of disclosure of financial position and performance to the zakat center as the zakat collector, as well as to the general public as stakeholders for zakat in the companies; (2) to assist the zakat collector determine the amount of zakat to be paid in a more timely and efficient manner; (3) to help companies and shareholders identify zakat obligations and approve zakat payments at the Board of Directors' meeting and the Annual General Meeting; (4) to create homogeneity in the format and presentation of information concerning the zakat potential of the state's companies so that the state can develop appropriate plans for its collection and distribution activities; and (5) in the longer run, when companies are given the power to distribute their zakat to various beneficiaries, disclosing the distribution of zakat payment to the various parties in the companies' financial statements will be important public information.<sup>33</sup> Barjoyai concentrates more on the disclosure perspective and the stakeholders' perspective. I, on the other hand, will elaborate on the above points and expound upon the benefits of having a ZAS.

Having a ZAS may help to reduce the national differences in the practice of zakat accounting. According to Abdul Rahman,<sup>34</sup> the main purpose of having a standard accounting practice is to narrow the differences among those firms that pay zakat and the zakat authorities who manage zakat in the disclosure statement, the method of measurement, and the method of pre-

senting data in financial statements. A ZAS would provide a consistent zakat accounting method, which could reduce confusion among the corporations in assessing their zakat due. This point leads to the following considerations.

The current practice, in which the zakat office helps companies assess their zakat due, seems to be inefficient, ineffective, time consuming, and a less practical approach. Additionally, evidence based on prior research shows that a lack of knowledge about zakat may decrease the company's desire to pay it.<sup>35</sup>

Viewed from this perspective, implementing a ZAS might help people become more knowledgeable about zakat and thus more willing to pay it. A ZAS may also make it easier to identify the applicable assessment method. There is some flexibility at present; however, the lack of a standard allows some room for getting around the relevant Shari'ah regulations. If people were clear on how to determine their zakat due, they might be encouraged to actually pay it. The ultimate benefit of this would be the increased amount of zakat available to benefit Muslim society as a whole. This, apparently, is consistent with the concept of the public good, which Islam strongly favors, in deriving appropriate rules for economic transactions.

Disclosure requirements, which may cover the method of zakat assessment, the amount of zakat paid, and to whom it was paid, may also help stakeholders make informed decisions. These stakeholders, who are mainly the users of the zakat information provided by the company, would include potential and existing investors or shareholders, employees, customers, and the Muslim public at large. They would be better able to value the company's commitment to Islamic precepts and, as a result, the company might be able to project its image in terms of how it is fulfilling its social responsibility.<sup>36</sup> If the stockholders are happy with such information, or with knowing how the company measures its zakat obligation and where it sends this money, the company may actually increase its goodwill capital.

Additionally, a ZAS would be very useful for a zakat center, for it would allow the center's employees to see any trend in the zakat payments made by these companies. A ZAS allows a comparison to be made across several years and across different companies. Hopefully, a ZAS would help these companies adopt a consistent approach in their zakat accounting practices. This comparative information would help zakat centers improve their marketing or strategic planning, both in terms of collection and distribution.

Looking at this issue from the federal government's viewpoint, its employees should realize that this special deduction, regardless of its size,

will affect their collection of the business sector's annual income tax.<sup>37</sup> Thus, it should be of concern to them in ensuring that the special deduction, as claimed by the companies, reflects the true and fair value of the amount of zakat actually payable and paid by the latter, and not otherwise. As for the latter, the companies' zakat information may help them become better informed of the zakat liability and the financial burden placed upon business entities currently paying both the zakat and the income tax.<sup>38</sup> Based on this motivation, the federal government should think about devising a proper regulatory framework for the zakat system that, among other things, can be served by having a ZAS.

The above discussion showed that the goal of having a ZAS is not merely to standardize the zakat practices among companies, but also – and equally important – to serve the stakeholders and/or the public benefit. The parties that a ZAS would serve are wide-ranging: the company involved, its shareholders and stakeholders, the zakat center (i.e., zakat collector), the state and federal governments, the zakat beneficiaries, and the Muslim public at large.

### **Implementing a ZAS**

Admittedly, in order to ensure the feasibility of a ZAS, various constituencies need to be involved and participate. This noble mission may not become a reality if it is no more than just a one-person show. In this paper, I call for the following parties to take an interest and participate in developing a ZAS: the Malaysian Central Bank or the government, the Malaysian Accounting Standard Board (MASB), the state religious councils (SIRCs) or zakat centers, accountants and auditors, academicians and researchers, Muslim jurists, and the Inland Revenue Board (IRB).

The Malaysian government could give moral and financial support to this process. It is argued here that, in line with the concept of *Islam Hadhari* being propagated,<sup>39</sup> the federal government should play a certain role in promoting a regulated and proper zakat system. Throughout Islamic history, zakat was the centerpiece of the Islamic fiscal system. Moreover, this effective tool may contribute to the nation's economic growth by serving as a unique mechanism of compulsory transfer of income and wealth from the haves to the have-nots, thereby ensuring every individual a minimum means of livelihood. This also provides a social security system in an Islamic society.<sup>40</sup> Therefore, zakat can help the government reduce the poverty level, which is part of its agenda. As a result, employment and income will rise,

thereby increasing the people's standard of living. Eventually, this would enhance the aggregate volume of the zakat collected.

The federal government's support for enhancing the collection of zakat has recently become more evident. Prior to the Year Assessment 2005, no tax rebates or deductions were granted to those companies that paid their zakat obligation. (This did not apply to Labuan's offshore companies, which receive a tax rebate subject to a maximum of 3 percent of net profits or RM 20,000.) In the 2005 Malaysian budget, however, it was announced that any corporate zakat paid on business income to the Islamic religious authorities could be deducted when computing the company's income tax. This deduction is granted primarily to reduce the cost of doing business.

This incentive is very commendable, for the deduction, when looked at from the federal government's perspective, removes the collection of the annual income tax from the business sector. This special deduction may not have a large impact on the country's economy, since the allowable deduction is only a mere 2.5 percent of the aggregate income, which is way below the current corporate tax rate of 28 percent.<sup>41</sup> However, the fact that the deduction is granted at all is proof that the federal government has shown some commitment to promoting the zakat collection system.

The Malaysian Central Bank, the country's financial policymaker, can regulate the zakat system as much as it regulates the taxation system. Thus, it could provide a regulatory framework in which the zakat system could work hand-in-hand with the existing taxation system. In addition, the government is expected to provide both financial and non-financial types of resources and support to ensure a proper monitoring mechanism and the coordination of the zakat practice among the companies (in particular) and the state (in general).

The MASB can be considered the most appropriate and important player in implementing a ZAS, since it is Malaysia's accounting standard-setting body. Its initiatives in preparing standards related to Islamic financial institutions (i.e., FRS *i-1*) and the technical pronouncement for zakat on business (i.e., TR *i-1*) are widely acknowledged. Accordingly, it is hoped that the MASB's involvement is an indication that we might see a ZAS in the future. However, this board might be faced with several challenges, such as finding people who are conversant in both accounting and Islamic knowledge, particularly with regard to zakat. For this purpose, it needs to bring accounting academicians and practitioners, Muslim scholars, zakat centers, and other relevant people and institutions together so that they can work as an MASB-monitored team.

SIRCs and state zakat centers can assist in terms of giving their full cooperation to allowing part of their jurisdiction to be transferred to the authorized bodies (i.e., BNM and MASB). While the Malaysian constitution states that all Islamic religious matters are under the state's control, SIRCs and the respective state zakat centers should be thinking about how a ZAS may allow the zakat system to achieve its far greater aims and benefits. They should compromise,<sup>42</sup> since this is not a case of one entity taking over another entity's jurisdiction, but rather a case of benefiting society at large. Moreover, as a matter of fact, this ZAS mainly touches on assessing and collecting zakat, not on distributing it. In other words, these centers may still be left with the right of controlling their respective state's disbursement and allocation of zakat.

Accountants and auditors are believed to have a pivotal role to play in promulgating corporate zakat.<sup>43</sup> According to Abdul Hamid:

Accountants and auditors are actually sitting in the most strategic position to ensure success of increasing zakat collection from business proprietors. Their expertise and knowledge is an asset in conveying and implementing an acceptable zakat deduction schedule for their business clients.<sup>44</sup>

Given this orientation, Nasir and Hassan have suggested that a chain of zakat consultants be set up to calculate the zakat-base according to the standardized method, since this may ensure that the zakat amount is calculated reliably and verified.<sup>45</sup> Beyond this, according to Amin,<sup>46</sup> the accounting community has pledged extra support by initiating the creation of the Malaysian Zakat Accounting Guidelines.

Auditors could play a role in improving zakat governance, which is necessary due to the increasing amount of zakat being collected. As Amin mentions,<sup>47</sup> standards alone are useless if there is no compliance mechanism. And this is where effective monitoring, through both internal and external auditing mechanisms, comes into play. At present, the Jabatan Audit Negara (the National Audit Department) is authorized by law to audit the financial matters of the state religious authorities, as the latter are a form of government agency.<sup>48</sup> In this respect, accountants and auditors should be able to give due support to their related organizations (i.e., MASB and NAD), for instance during the due process, by making suggestions on a ZAS's technical aspects. In addition, in the case of companies that adopt and comply with TR *i-1* in their financial reporting, external auditors would have an additional role and responsibility. Among others, they should ensure that this adoption is being done consistently from one period to another.

Academicians, both in the accounting as well as the religious knowledge fields, should contribute their ideas, especially in providing theoretical inputs to the development of a ZAS. Accounting academicians and professors could share their technical knowledge, experience, and expertise in various aspects of accounting that are related to preparing accounting standards. Similarly, accounting researches may have some points to share based on their research experiences or outputs, both of which could enhance the standard's applicability. Also, a few accounting academicians might have some religious background that could provide some insights to the team on how to prepare this Islamic-related standard. Such academicians and researchers can perhaps be found in Islamic-related higher learning institutions, namely, the International Islamic University - Malaysia, the Islamic Science University of Malaysia, and the Islamic University College. Religious scholars, by sharing their knowledge and expertise of *fiqh al-zakat*, could also add value by giving their opinions on the relevant jurisprudential rulings, including the types of wealth that are zakatable, the zakat base, and its computational basis.

The Inland Revenue Board (IRB), one of the Ministry of Finance's main revenue collecting agencies, could provide moral support for this agenda. It should not wrongly perceive any proposed ZAS as a threat that may negatively impact its collection of taxes and thus reduce its employees' material incentives. Rather, a ZAS should be perceived as a partner, similar in its operation (both collect money from those who are supposed to pay) but substantially different in its goal and aims. While taxation focuses more on one's social obligation, paying one's zakat is a religious obligation.

The IRB also might be of help in terms of providing detailed requirements on what types of zakat will be considered tax deductions. By having a full description of the types of zakat that can be deducted, a ZAS will be tailored not only to serve the public benefit, but also to acquire a reasonable tax deduction. This may even make a ZAS up-to-date and favorable among Muslim corporations.

The Department of Wakaf, Zakat, and Hajj (DWZH), which is a unit of the Islamic Development Department of the Prime Minister's Department, can initiate as well as lead this agenda of developing a ZAS for companies. This is in line with its main functions, which are, among others, to plan, coordinate, and monitor the country's *waqf* and zakat systems. In fact, one of its primary missions is to develop the zakat system in a well-planned, systematic, and integrated manner as well as to enhance the efficiency and effectiveness of the zakat administration. Although zakat comes under the state's jurisdiction, this does not mean that other parties, especially the fed-

eral government, have no role to play in improving the zakat system. The DWZH, in the name of the federal government, can actually submit proposals to the Mesyuarat Majlis Raja-Raja (Royal Council Meeting) on this matter, just like it initiated the recommendation to harmonize the Shari'ah courts nationwide. In the case of a ZAS, the DWZH perhaps can collaborate with all of the above-mentioned parties after it receives the consent of the state's ruler. However, the state government has the ultimate power to decide whether or not to adopt the proposed standard.

### **Conclusion**

The fact that different parties need to pull their resources together to ensure the realization of a ZAS reflects the tough challenges that need to be faced if such a standard is to become a reality. This task is not something that can be done overnight, since it covers both temporal and religious affairs. In addition, its technical parts must be parallel to the existing laws and regulations, and the standard cannot violate any Islamic precepts. Having said that, the priority here is to educate the parties involved about the importance of having such a standard and to make them fully understand the noble aim of having a ZAS in the first place. As Amin points out,<sup>49</sup> education is the key to the business community's acceptance and endorsement of a corporate zakat. Only after this has been accomplished can we go one step further: bring these parties together and seriously discuss the issue as a team in order to promulgate a ZAS.

There may be little hope of achieving a ZAS for Malaysian companies in the near future. I base this on a statement contained in the MASB-issued FRS *i-1* (in paragraph IN1, pg. 6), which implies that the reason why any Islamic accounting standard is needed is simply due to the emergence of Islamic financial institutions and Islamic banking services offered by conventional banks, and not because of more important reasons, such as the religious obligation of increasing the number of Muslim corporate entities in Malaysia. It is thus presumed that in the near future, most of the attention given to developing Islamic standards will be geared toward their usefulness for financial institutions, as opposed to other business entities.

However, many people strongly believe that it is about time that Malaysia has a ZAS in place. All in all, such a development could be feasible if the government found the necessary political will to push the initiative<sup>50</sup> and reform the zakat system so that it will be on the same level as the existing taxation system in various ways, especially as regards its regulation and enforcement.

The most significant limitation of this paper is that it does not suggest a ZAS's components or the methods of zakat recognition and measurement that should be applied to assessing corporate wealth. Thus, it is suggested that future research focus on these matters. Second, this paper is limited in the sense that it lacks empirical evidence to support the argument that a ZAS is urgently needed. It is proposed that future researchers collect data from ZAS stakeholders (i.e., both preparers and users) to gain some insight on how they perceive this issue.

### Endnotes

1. Norita Mohd Nasir and Salleh Hassan, "Zakat on Business in Malaysia: Issues and Current Treatment," in Bala Shanmugam et al. (eds.), *Issues in Islamic Accounting* (Serdang, Malaysia: UPM Press, 2005), 165-78.
2. Abdul Rahim Abdul Rahman, "Zakat Accounting: Creating Business Wealth," *Akauntan Nasional* (September 2002): 11-16.
3. Iszudin Mohd Amin, "Business Zakat Poised for Take-Off," *Akauntan Nasional* (January/February 2003): 18-20.
4. Nasir and Hassan, "Zakat on Business."
5. Mohd Daud Bakar, "The Malaysian Zakat System: Law and Policy Reform" (paper presented at the seminar on Zakat and Taxation, organized by the Kuliyah of Economics and Management, International Islamic University - Malaysia, 8-9 June 1998).
6. Nur Barizah Abu Bakar and Abdul Rahim Abdul Rahman, "Comparative Study of Zakah and Modern Taxation," *Journal of King Abdul Aziz University: Islamic Economics* 20, no. 1 (2007): 25-40.
7. Zakat centers are also called zakat units, zakat boards, and zakat committees.
8. Sabahaddin Zaim, "Recent Interpretations on Economic Aspect of Zakah," in I. A. Intiazi, et al. (eds.), *Management of Zakah in Modern Muslim Society* (Jeddah: IRTI/IDB: Jeddah, 1989), 101-20; Z. Ahmad, *Public Finance in Islam* (International Monetary Fund Working Paper: 1989).
9. Nur Barizah Abu Bakar and Abdul Rahim Abdul Rahman, "In the Wealth of the Affluent There Are Rights of the Poor: A Comparative Study on Islamic Concepts of Zakat and Modern Taxation" (paper presented at the 2005 National Young Scholars Conference, 12-13 December 2005).
10. S. M. Ahmad, *Economics of Islam: A Comparative Study* (Lahore: S.M.A., 1977).
11. Monzer Kahf, *Economics of Zakah* (Jeddah: IRTI/IDB), 1997.
12. Nasir and Hassan, "Zakat on Business."
13. H. Abdalati, *Islam in Focus* (Saudi Arabia: World Assembly of Muslim Youth, 1994), 126-29.
14. Ibid.

15. Abdul Rahim Abdul Rahman, "Zakat on Business Wealth in Malaysia: Corporate Tax Rebate, Accountability and Governance" (paper presented at the Zakat Accounting Conference, Petaling Jaya, Malaysia, 15 October 2002).
16. Refers to *ratio decidendi*. The issue of *'illah* is the most important element in Islamic law as the ruling should be always attributed to *'illah*. Whenever the *'illah* exists the rule of law will also exist; if the *'illah* does not exist the rule of law will also not exist. See Mohd Daud Bakar, "The Malaysian Zakat System: Law and Policy Reform" (paper presented at the seminar on Zakat and Taxation, organized by the Kulliyah of Economics and Management, International Islamic University Malaysia, 8-9 June 1998).
17. Abdul Rahman, "Zakat on Business Wealth in Malaysia."
18. Yusuf al-Qardawi, *Fiqh az-Zakat: A Comparative Study – The Rules, Regulations and Philosophy of Zakat in the Light of the Qur'an and Sunna* (London: Dar Al Taqwa Ltd., 1999).
19. Nasir and Hassan, "Zakat on Business."
20. Ibid.
21. Ibid.
22. Abu Bakar and Abdul Rahman, "In the Wealth of the Affluent."
23. *Ijtihad* refers to a jurist's use of reasoning to find solutions to new problems, keeping in view Islam's intent and spirit. Methods of *ijtihad* include *qiyas*, *istihsan*, and *istislah*.
24. *Maqasid al-Shari'ah* refers to the preservation of five rights, namely, religion, life, intellect, lineage, and wealth.
25. Abdul Rahman, "Zakat on Business Wealth in Malaysia."
26. E. S. Hendriksen and M. F. V. Breda, *Accounting Theory*, 5th ed. (USA: McGrawHill, 1992).
27. Abdul Rahim Abdul Rahman, "Zakat Accounting," 11-16; Nasir and Hassan, "Zakat on Business."
28. Certain necessary items in Malaysia's banking environment are not addressed in AAOIFI FAS 9, for instance, statutory deposits with the Malaysian Central Bank.
29. Abdul Rahman, "Zakat Accounting."
30. AAOIFI is binding, at least on Bahraini banks.
31. Abdul Rahman, "Zakat Accounting."
32. Ibid.
33. Barjoyai, in Amin, "Business Zakat Poised for Take-Off."
34. Abdul Rahman, "Zakat on Business Wealth in Malaysia."
35. Nur Azura Sanusi, Norazlina Abd. Wahab, and Nor Fadzlin Mohammad Bahar, "Gelagat Kepatuhan Pembayaran Zakat Pendapatan," Seminar Ekonomi dan Kewangan Islam (29-30 August 2005), 275-87; Hasan Bahrom and Mohd Sahnaz Saidu, "Kajian Terhadap Faktor Yang Mempengaruhi Pembayaran Zakat Perniagaan di Kalangan Usahawan: Kes Kajian Terengganu," Seminar Ekonomi dan Kewangan Islam (29-30 August 2005), 289-96.

36. Abdul Rahman, "Zakat Accounting."
37. Amin, "Business Zakat Poised for Take-Off."
38. Abdul Rahman, "Zakat Accounting."
39. *Islam Hadhari* emphasizes development that is consistent with Islam's tenets and focused on enhancing the quality of life. It is being promoted by Prime Minister Abdullah Ahmad Badawi. It consists of ten fundamental principles: (1) faith and piety in Allah, (2) a just and trustworthy government, (3) freedom and independence for the people, (4) a mastery of knowledge, (5) balanced and comprehensive economic development, (6) a good quality of life for all, (7) protection of the rights of minority groups and women, (8) cultural and moral integrity, (9) protection of the environment, and (10) a strong defence policy.
40. Muhammad Solaiman Miah. "A Study on Distribution of Income and Wealth in Islam with Special Reference to the Institution of Zakat" (Ph.D. diss., International Islamic University - Malaysia, 1992).
41. Mohd Safri, in Amin, "Business Zakat Poised for Take-Off."
42. In the case of standardizing the Shari`ah courts, they managed to sacrifice their rights for the public benefit. Zakat is also one of the areas that need a certain extent of standardization and, thus, compromise.
43. In Amin, "Business Zakat Poised for Take-Off."
44. Datuk Abdul Hamid Zainal Abidin, (keynote address delivered at the Zakat Accounting Conference, organized by Pusat Zakat Selangor and the Malaysian Institute of Accountants, 15 October 2002), in *Ibid.* At that time, he was a minister in the Prime Minister's Department.
45. Nasir and Hassan, "Zakat on Business."
46. Amin, "Business Zakat Poised for Take-Off."
47. *Ibid.*
48. Abdul Rahman, "Zakat Accounting."
49. Amin, "Business Zakat Poised for Take-Off."
50. Abdul Rahim Abdul Rahman, "Pre-requisites for Effective Integration of Zakat into the Mainstream Islamic Financial System in Malaysia" (paper presented at the Corporate Zakat Seminar, Petaling Jaya, Malaysia, 22-23 June 2005).