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## The Effects of Internal Control System, Financial Management and Accountability of NPOs: The Perspective of Mosques in Malaysia

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### Abstract

This study examined the effectiveness of internal control system, financial management and accountability practices of mosques in Malaysia. Based on 500 questionnaires was administered to chairman and treasurer of 250 selected mosques available in Malaysia including Sabah and Sarawak. This study suggests that a proper and accurate recording of financial transaction, enhancing the accountability of chairman and treasurer in order to improve the productivity and performance effectiveness. The inclusion of these variables provides important implications for expanding our understanding of financial management practices in non-profit organizations and creating new research opportunities. The result provides on how Malaysian mosque enhances internal control system and performance to achieve the mission and goals of the mosque. An effective way to improve the productivity and efficiency of financial management practices and management control system in the mosque.

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*Keywords:* budget participation; internal control system; fund usage; accountability; financial management practices; mosque

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### 1. Introduction

The responsibility and the burden on the religious institutions are the interaction with budget participation (Brownell and Dunk, 1991); the embezzlement of funds and a scandal about internal control system of religious organization (Sulaiman et al, 2008). The cases involved in mismanagement of the fund generated by the institutions. Later relate to the mosques. The criticism of the financial management practices is due to poor factors of

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management control system (Sulaiman et al, 2008; Abdul Rasid and Abdul Rahman, 2009, Chenhall et al, 2010; Henri and Journeault, 2010; Wahab, 2008 and Amudo and Inanga, 2009).

Some factors that relate to management control system in the mosque are lack of accountability to manage accounting system, less budget participation in the mosque and improper of recording and reporting of income and effective way to find sources of income in the mosque (Alim and Abdullah, 2010). Consequences, it will reduce the quality of management in which the administration of the mosque is not based on Islamic requirement. In addition, a weak internal control system will increase the risk in managing the mosque performance and influence the internal and external management control system which will affect the financial management practices in the mosque.

Quality financial management in mosques includes steps taken by mosque management to increase the level of management quality in the mosque. For example, by organizing seminars for the public in order to build a better relationship between the public and the mosque's management and the *muzakarah* performed by the managing officer in the mosque at the national level. It follows comprehensive financial management practices, which would directly increase the efficiency, effectiveness and value maximization of the mosque (Wahab, 2008).

Management control system is important to financial management practices in the mosque to ensure efficient and proper financial management practices, to ensure the operation runs smoothly in compliance with rules and regulation, to determine the ability of mosque management in measuring and managing activities effectively and to provide information in making better decisions. Therefore, to have a better mosque management, important person such as chairman and treasurer of mosque need to play a role in ensuring the effectiveness and efficiency of financial management practices in the mosque. Thus, the objective of this study is to examine the effect of management control system which are budget participation, internal control system, fund usage and accountability on financial management practices in the mosque.

The study contributes in a number of ways is the best practices of internal control system. The following sections discuss the literature review, methodology, result and discussion.

## 2. Literature Review and Hypothesis Development

Nowadays, the changes of time make the mosques management become more challenging. Hoyge, M. (2009) found that there are two issues arise from non-profit organization of finance theory which is donations and borrowings. Donations defined as revenue from individuals or corporation supporting non-profit organization. The purpose of receiving donation in mosque is to support and help improving the quality or increasing the quantity of services in mosque. This to ensure the program and activities run smoothly.

The mosque is not only a place of worship, but also a place to gain knowledge. It is also a place for communal gathering of the Islamic community members, as well as a place for holding various religious ceremonies and rituals, such as the *akad nikah* (wedding ceremony)(Abdul Rahman and Ahmad, 1996 and Ismail, 2003).

### 2.1 Budget Participation

The meaning of budget is a financial plan and a list of all planned expenses and revenues. It is a plan for saving, borrowing and spending. Williams et al (1990) had investigated the part of Thompson's general challenge by focusing on dimensions of the budget-related behavior (BRB) of managers in complex, public sector organizations. It has been found that it is an important processual variable in terms of enabling organizations to achieve their goals. Leroux (2009) found in her studies that non-profit organizations which are more heavily dependent on private charitable contributions will be less likely to employ participatory governance practices, whereas on government funding will be more likely to employ participatory governance practices.

Most of the studies, Otley and Pollanen (2000) and Brownell (1991) agree that it is very important to involve budget participation in non-profit organization to ensure performance evaluation and effective management. In order to gain acceptance of budget goals and increase organizational effectiveness (Aranya, 1990), maintaining low levels of both budget participation is instrumental in effective organizational strategy and job performance. Thus, it is expected that for this study, budget participation would enhance the financial management of the mosque. The following hypothesis is presented:

*Hypothesis 1 : Budget participation influenced financial management practices in the mosque*

## 2.2 Accountability

In general, accountability is the concept in ethics and governance with several meanings. This concept is similar to responsibility, answerability, blameworthiness, and liability (London, 2003). As an aspect of governance, it has been central to discussions related to problems in the public sector, non-profit and private (corporate) worlds. This author also stated that in leadership roles, accountability is the acknowledgment and assumption of responsibility for actions, products, decisions, and policies including the administration, governance, and implementation within the scope of the role or employment position and encompassing the obligation to report, explain and be answerable for resulting consequences.

Accountability is generally defined as accepting and meeting one's personal responsibilities, being and feeling obligated to another individual as well as oneself, and having to justify one's actions to others (London, 2003). Accountability has frequently been presented as rational practice to ensure responsibility by individuals and institutions, which should be implemented in all civil societies, economic institutions and organizations (Velayutham and Perera 2004). The traditional tools of accountability are often considered by non-profit organizations as unnecessary formal tasks and excessive bureaucracy, which can have important consequences both organizationally and managerially (Berardi and Rea 2010). According to Rutkowski and Steelman (2005), accountability focuses on the extent to which feedback recipients perceive they are responsible for, utilizing feedback information for development. Thus, the following hypothesis is tested:

*Hypothesis 2 : Accountability influenced financial management practices in the mosque*

## 2.3 Fund Usage

Generally, funds are a source of supply to all organizations, whether profit or non-profit. Based on accounting concepts, accounting systems emphasize accountability rather than profitability. Normally practices by non-profit organizations or government agencies in preparing financial statement and reporting are based on daily transaction rather than profit earned. Thus, it is called fund accounting. However, in an Islamic context, funds should be used according to Islamic law. According to Ahmad et al, 2009 found that most of the mosque committee still needs to improve management efficiency, especially in fund management and property.

Sulaiman et al (2008) also found that nowadays, the embezzlement of funds from religious organizations is more common due to lack of accountability and lack of commitment to accounting. They might misuse the power towards the funds raised. In this case, reporting management system such as budgeting, financial statement and internal control are not accurate. Thus, it will help the effectiveness of financial management practices in nonprofit organizations and reduce administrative burdens. According to the discussion above, the following hypothesis is proposed:

*Hypothesis 3 : Fund usage influenced financial management practices in the mosque.*

## 2.4 Internal Control System

An internal control system is defined as the policies and procedures put in place to ensure the protection of an organization's assets and the reliability of financial reporting (Sulaiman et al, 2008). Internal control can provide only reasonable assurance not absolute assurance regarding the achievement of an organization's objectives. Implementing a proper system will help the organization's operations become more effective and efficient (Sulaiman et al, 2008).

The issue with internal control of organizations is ensuring the efficiency and effectiveness of activities, reliability of information, compliance with applicable laws, and timeliness of financial reports (Jokipii, 2009 and Changchit et al, 2001). A proper internal control system ensures that the organization's managers would utilize the financial resources in a way that will safeguard the interests of the donors and/or contributors (Sulaiman et al, 2008). Internal control structure includes policies and procedures on controls such as withdrawal applications for funds and grant accounts, bank and cash, purchases, payments and monitoring, evaluations and reporting. Thus, to have a successful organization, it requires a proper accounting record and appropriate management control system. Therefore, the following hypothesis is tested:

*Hypothesis 4 : Internal control system influenced financial management in the mosque.*

### 3. Methodology

As summary, if the mosque management perceived to have performance, effectiveness, this will lead to budget participation (H1). The participation in preparing budgets, in other hand will impact the accountability (H2). The management will utilize their accountability for effectiveness managing fund usage (H3). There is also a proper recording and reporting for financial transaction and this leads them to attaining a better internal control system (H4). Figure 1 shows the research framework developed and depicts the four hypotheses to be tested in this study

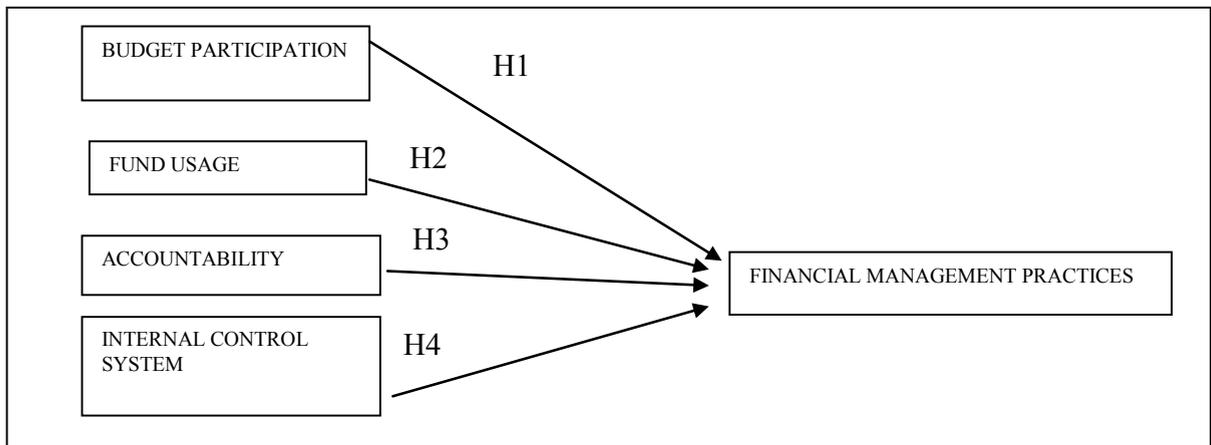


Fig. 1. Framework of the factors influencing the financial management practices

A self-reporting questionnaire is used to collect data from the respondents. A sample is a subset of the population. It comprises of some members selected from the population which are chairman and treasurer. The population of the study comprises of 250 mosques in Malaysia including Sabah and Sarawak. These questionnaires were provided in 2011 and distributed to the respondents when visiting the mosques. The researcher personally collected the completed questionnaires during the visits. 500 questionnaires were distributed and 211 fully answered questionnaires were able to be collected. This represents a 42.2% response rate.

7 items on financial management practices (Abdul Wahab, 2008); 6 items on budget participation (Hamid et al, 2006; Milani, 1975 and Brownell, 1982); 6 items on fund usage (Abdul Wahab, 2008); 6 items on accountability (Hamid et al, 2006) and 6 questions addressed the use of internal control system (Abdul Wahab, 2008 and Maliah et al, 2008). The seven point Liker-type scales ranging from 'strongly disagree' to strongly agree' was employed for all the measurement.

**Control Variables.** Two variables are considered as control variables in this study, namely, the category of the mosque which are (1) district, (2) *qariah*, (3) mukim and (4) private mosque and the average monthly income of the mosque. The present study examined the categories of mosques and monthly incomes of mosques as control variable to determine how management of small or large mosques find sources of their monthly income, whether sources are from private or personel collections, or sources from *wakaf* property or non-*wakaf* property. Furthermore, to determine where the mosque is covered in the survey whether district, *qariah*, private or mukim.

#### 4. Results

Table 1. Summary of the correlation results of the analysis.

	1	2	3	4	5	6	7
Financial Management	1						
Budget Participation	0.313**	1					
Fund Usage	0.359**	0.150*	1				
Internal Control	0.405**	0.130	0.140*	1			
Accountability	0.279**	0.494**	0.138	0.091	1		
Mosque Category	0.090	0.134	-0.014	0.218**	0.026	1	
Monthly Income	0.100	-0.034	0.132	0.304**	0.003	0.163*	1

\*\*\* Correlation is significant at the 0.01 level

\*\* Correlation is significant at the 0.05 level

Table 1 above shows the correlation between all independent variables and dependent variables. There are positive relationships between budget participation, internal control, fund usage and accountability on financial management practices ( $r = 0.313$ ,  $r = 0.359$ ,  $r = 0.405$  and  $r = 0.279$  at  $p < 0.05$ ) respectively.

Table 1.1. Regression Results Financial Management in Mosque

Variables	Coefficients	Std Error	t-stat	p-value	VIF
Constant		0.596	-0.124	0.901	
BUDGET_PART	0.119	0.059	1.681	0.095	1.405
FUND_USAGE	0.278	0.054	4.524	0.000**	1.051
INTERNAL_CTRL	0.316	0.119	5.150	0.000**	1.051
ACCOUNTABILITY	-0.006	0.102	-0.075	0.941	2.009
R	= 0.596				
R <sup>2</sup> (Adjusted R <sup>2</sup> )	= 0.355 (0.334)				
F-statistic (p-value)	= 16.546 (0.000)				
Durbin Watson statistics	= 2.383				

\*\* Significant at 1% level

\* Significant at 5% level

Table 1.1 shows the multiple regressions to determine if the independent variable is significantly associated with the financial management practices in the mosque. Based on the results, the regression was statistically at 10% (16.546,  $p = 0.000$ ). The multiple R ( $R = 0.596$ ) showed a high significant correlation between independent variables and the dependent variables. The  $R^2$  value indicated that about 35.5 percent of the variance in the financial management practices in mosque was explained by the six independent variables. The adjusted  $R^2$  was 0.334 which meant that the regression model explained 33.4 percent of the various variables in the financial management practices in mosque. The Durbin Watson statistics was 2.383, in position two, indicating that the correlation of the residual did not appear to be a problem. According to Pallant (2007), the cut-off points for determining the presence of multicollinearity was the VIF values above 10, representing that there was a possibility of multicollinearity. Therefore in this study, the range of the VIF values was between 1.051 and 2.222. As a result, the multicollinearity assumption was not violated.

In this study, the largest beta coefficient is 0.316 which is for internal control system. This means that the variables make the strongest relationship whereas the beta value for accountability coefficient, -0.006 is lower compared to other variables which means it makes a low relationship with financial management practices. Internal control variable has significant value of less than 0.05 on financial management practices whereas budget participation and accountability variables sig. value > 0.05 on financial management practices, making them insignificant.

Table 1.1 revealed that fund usage and internal control system had a significant relationship on financial management practices. Thus, H2 and H4 were supported. Nevertheless, budget participation, and accountability had no significant relationship on financial management practices.

## 5. Discussion

The primary objective of this study is to examine the effect of management control systems i.e. internal control, budget participation, fund usage and accountability that influenced financial management practices in mosques. The results show that the internal control system plays an important role in ensuring the effectiveness of financial management practices. According to Sulaiman et al (2008), to implement a proper internal control system, management committee must take responsibility which provides assurance that public monies are used and accounted for properly. This is to ensure the financial management practices comply with two rules and regulation. Abdul Wahab (2008) in his study suggests that to improve the financial management in mosque in order to make the mosque institution a success, there should be a various donations, not only in the form of money, but also in the form of physical energy or fruitful ideas.

H1, and H4 consist of budget participation and accountability on financial management practices in the mosque, which does not show any significant result. This is supported by Hamid et al (2006), Aranya (2001) and Brownell (1981) who found that interactive effects of budget participation were only on managerial performance but not on financial management practices. In addition, low levels of budget instrumentality and budget participation will affect the effectiveness of organizational strategy, performance and job satisfactions. Accountability has three (3) aspects, (1) compliance, (2) transparency and (3) responsiveness (Shaoul et al, 2012). It was supported that accountability is not only a financial reporting framework, but also requires disclosure of related non-financial information. Thus, accountability has an insignificant result of financial management practices.

The present study has several limitations that may potentially influence the interpretation of the results. These limitations should be considered when interpreting the results or when applying the method of this study in other research settings:

- 1) The questionnaire was given to members of the mosque committee that manages the mosque. The accuracy and validity of data depend on their honesty in answering the questionnaire. This is because there may be a possibility of them wanting to hide or not disclose their personal or organizational weaknesses. Therefore, observations were also performed by looking at bulletin boards to find the total weekly and monthly collection that was contained in the financial reports of the mosque.
- 2) The 1-7 scale was used in this study. The respondents were asked to state each level of perception and agreement toward the questions that were presented. The use of a 1-7 scale can lead to a polarized response, which is the trend of the respondent to answer automatically when presented a question or query without giving their full attention toward what is being questioned or queried. This problem arises from the differences in interpretation by each individual toward the scale that is given.

Thus, it is highly suggested that future study should attempt to elaborate using only large mosque sample size as it would enhance the external validity of the findings. Respondents are only the mosque committee. Thus, to enhance better outcomes, perhaps, more valid generalizations of the present results could be made relating to the perspective of the *qariah* members and other professional groups. Secondly, future study needs to observe other information in bulletin boards regarding annual activities done in mosques. It is to ensure the result is more transparent and accurate. Thirdly, always explain the details to respondents so as them having a better knowledge in answering the questions. This situation arises because of the attitude of some mosque committee members who do not want to give full cooperation.

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