

ISSUES AND METHODS OF DETERMINING ZAKAT ON BUSINESS

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Abstract: *A financial statement is a document prepared by a company to report the current financial position and performance of the business over a period of time. It needs to be prepared according to the accounting standards. These financial statements are important for users to make business and investment decisions. In addition to being important for users to make business and investment decisions, these financial statements are also used to determine the amount of zakat on business. However, there are some differences and interpretations in determining the amount of zakat on business. The objective of this study is to identify the issues in determining the type of assets in zakat calculations for businesses. Furthermore, this study also aims to evaluate the asset classification method for zakat on business applied by zakat institution. This study uses information obtained from several forms of documents, whether in the form of print or online sources, that are available in the public domain. This article raises the possibility of reviewing and enhancing the asset-related accounting framework for zakat in order to better serve zakat's objectives.*

Keywords: *Zakat, Business, Presentation, Disclosure, Financial Statement.*

Introduction

An organization's financial situation and performance are reported in a financial statement. The preparation of this document must adhere to the established accounting standards. In Malaysia, the accounting standards that are applied to other than private entities are known as Malaysian Financial Reporting Standards (MFRS) and took into effect since 1 January 2012. While for private entity companies, starting from 1 January 2016 they need to comply with Malaysian Private Entities Reporting Standards (MPERS). Several steps are involved in issuing the financial statements, namely identifying a transaction or business event, recording, measuring, classifying the transaction and finally presenting the information into a financial statement that reflects the performance and financial position of the business.

The accounting information on business's profit, assets and liabilities are presented in a set of financial statement and they are essential for users in making their business and investment decision (Nogueira, Jorge and Oliver, 2013; Salehi, 2022). Financial statement is a documents

prepared by a business to report their financial position and performance for a financial year. Furthermore, financial statement is significant in providing an overview of the business's operations or responsibilities in carrying out its social duties. When it comes to companies owned by Muslims, it signifies their responsibilities and willingness to carry out their role as a catalyst for the ummah's economic growth. Financial statements that disclose information on zakat practices can be used as a tool to evaluate how well a firm is meeting its religion and social obligations.

It is important to understand that zakat is a religious obligation that must be met and is one of Islam's pillars. This practice entails the distribution of a specified amount of property or wealth from a person to individuals in need, such as the poor and orphans, once certain conditions are met. Zakat is not only a financial transfer from one party to another, but it can also be viewed from the perspectives of social justice and economic equity. Redistributing wealth, for instance, from the rich to the poor, is indeed one way to break free from oppression, greed, and selfishness. Therefore, engaging in zakat activity is symbolic of both financial success and the capacity to cleanse and purify the heart.

Literature Review

As a reference document to determine the amount of zakat payment, the financial preparation process should be done carefully. The process that starts with identifying transactions and ends with the issuance of financial statements must comply with accounting rules and regulations. One of the important steps in this process is the classification of a transaction item into which financial statement components such as assets and liabilities. The classification of items in these financial statements components has an impact on the interpretation of business wealth and ultimately on the determination of the amount of zakat on business. Various accounting practices also lead to different assessment of business wealth and finally impact zakat calculation (Ahmed et al., 2016). Furthermore, previous studies stated that there are several methods for determining the amount of zakat on business (Ahmad and Osman, 2010; Razaly et al., 2014, Irfan et al., 2021). In Malaysia, there are three methods to calculate zakat on business: (i) zakat accounting based on current assets; (ii) zakat accounting based on current assets and investment profits; and (iii) zakat accounting based on net working capital and business profits (Ahmad and Osman, 2010).

Generally assets are referred to resources owned and controlled by a business as a result of past transactions. It is also associated with the its future economic benefits or service potential when it flows into or out of the corporate entity. Controlled resources, benefits obtained, and risk exposure to the asset are all significant characteristics of an asset (Malaysian Institute of Accountants, 2020). Assets are divided into two categories on how they are presented in financial statements: non-current assets and current assets. Non-current assets refer to long-term investments that are difficult to convert into cash within a year or can not be realized in one accounting period, such as land and building. While current assets, such as business inventory, are expected to be realized or liquidated in the form of cash or can be sold within a year. However, for the financial sector, whether Islamic or conventional banking, the order of assets is listed based on liquidity and liquid assets are presented first.

There are few conditions under which a business is required to pay zakat. According to the Pusat Pungutan Zakat - MAIWP, one of the state zakat institution in Malaysia, the main conditions for zakat is imposed on business are (i) Muslim ownership, (ii) perfect ownership, (iii) completed the haul (a period of one full year), (iv) sufficient nisab (the minimum amount

of possession), (v) business intention, and (vi) halal business and services (source: <https://www.zakat.com.my/info-zakat/jenis-jenis-zakat/zakat-perniagaan/>). Two of these six conditions, sufficient haul and sufficient nisab, are directly related to assets. While the other four, which are Muslim ownership, complete ownership, intention, and type of business, allude to the owner of the asset (either an individual or an organisation). In relation to the conditions to be classified as an asset, are the criteria used by zakat institutions appropriate or do they need to be further refined for the purpose of calculating zakat?

Since assets are a symbol of wealth and are used in determining zakat, the interpretation of assets should be in line with zakat aspirations that is to help the poor and purifying riches. Zakat is a method of purification, both external and internal, that aims to educate human passions and emotions. The wealth that is owned is not absolute, but there are other people's rights (asnaf) associated with the wealth. Therefore, in determining the item of assets and the amount that needs to be distributed as zakat, the subjectivity factor (e.g., greed and emotions) of the person or individual cannot be denied. Moreover, there is room for financial statement preparers to exercise professional judgement in certain circumstances. The Qur'an also does not specifically explain the meaning of assets subject to zakat. There are various interpretations of the meaning of business asset or property among Islamic scholars (Bouheraoua et al., 2015). Hence, individuals who are entrusted with assets management should be careful and cautious when making accounting classification. Imprudent judgement can affect the presentation of financial statements, including issues such as assets involved in the determination of zakat on business.

In light of today's increasingly complex businesses, new interpretations of a business's assets and liabilities are required. These developments cause the interpretation of assets for zakat on business, as suggested by previous scholars, to be given attention and further clarification. Furthermore, the construction of conventional accounting standards probably is not align with the interpretation and maqasid (purpose) of zakat. There is possibility of non-uniformity in determining the amount of zakat paid and how assets are recorded. As a result, the business owner probably chooses and inappropriate asset valuation method and tends to make a zakat assessment that does not reflect the true state of his business wealth.

The focus of modern business extends beyond tangible assets. Assets can also consist of non-physical forms such as digital currency. The difference in the characteristics and nature of these new assets requires a re-evaluation of the zakat calculation so that all these assets are included in the zakat calculation process. This demonstrates that the determination of zakat on business is dynamic in nature – taking into account the evolution of business and accounting practices without ignoring the Shariah principles.

In addition, the calculation of zakat on business does not simply refer directly to items in business financial reporting. Some adjustments need to be made to ensure that the asset is truly compliant with the requirements of zakat on business assets. Adjustments involving business assets for the purpose of zakat should be clear so that there is no confusion for business owners in determining the amount of zakat to be charged. This becomes more complicated when looking at the variety of forms of business activities as there are differences in the classification of assets according to the business sector. For example, for ordinary businesses, land is a non-current that is used as a long-term investment. Based on Financial Reporting Standard 116 Property, Plant and Equipment states that "Property, plant and equipment are tangible items that:

- a. are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and
- b. are expected to be used during more than one period”.

However, for property development companies, this asset will not remain a non-current asset. This asset classification will change to current asset when some conditions or events occur. According to MASB 32 Property Development Activities that: “The change in the classification of land held for property development to current asset shall be at the point when development activities have commenced and where it can be demonstrated that the development activities can be completed within the normal operating cycle.”

Due to the technicalities of accounting interpretation and business complexity, the asset-related accounting framework for zakat needs to be further enhanced to meet the objectives of zakat. Wealth measured through assets should be seen to share prosperity so that wealth is not only concentrated in organisations or among certain groups. Sharing wealth through zakat activities, which is the flow of zakat funds from the rich to the needy, will eradicate extreme poverty and help towards universal justice. This indeed coincides with the concept of Maqasid al-Shariah, or the goals of Shariah, among others, emphasising the preservation of wealth where the flow of wealth occurs continuously for the well-being of society (Laldin and Furqani, 2013).

Among the previous studies that examine accounting methods for business zakat are Obaidullah (2016) and Ahmad and Othman (2010). Ahmad and Othman (2010) raised questions about the zakat assessment method introduced by the Department of Islamic Development Malaysia (JAKIM) regarding the treatment of financial and non-financial debts, finished goods inventory, and semi-finished (in-process) inventory. According to them, the items are given different treatment even though they both are current assets. As a result, the assessment value of zakat will be affected. They suggest that a uniform method be established (whether the items need to be discounted or not) so that the assessment results are consistent.

A comparative study between countries also shows that there are differences in the method of calculating zakat for companies in Saudi Arabia, Kuwait, and Malaysia (Siswantoro et al., 2022). A similar point was also raised by Uyob (2020), that there is a difference from an Islamic perspective on the principles of accounting and business. Meanwhile, Abdul Kadir, Syed Adwam Wafa, and Abdullah (2020) have suggested separate reporting disclosure be made for business zakat and introduced zakat per share (ZPS) to encourage zakat payment.

A study by Tajuddin (2017) also found that various assessment methods are used by companies in calculating zakat, namely the working capital method and the calculation based on profit or loss after tax. The writer is of the opinion that this is in line with the principles of Shariah and should be supported considering that each company has characteristics or is involved in different activities. This is also in line with the findings of a study by Tajuddin, Shamsuddin, and Mat Nor (2017) that the business zakat calculation practice in zakat institutions is not a rigid method. In another study, Mohd Ariffin and Osman (2022) suggested that banking institutions have a clear zakat calculation framework, which will affect the amount of zakat that must be paid. Their study found that disclosure related to zakat information was made in the Shariah Committee report and Notes to the Financial Statement. In the same vein, Mohd Noor et al. (2017) recommend that the owners of small businesses use methods that are tailored to the type and form of business they run.

Based on the discussion above, this study identified several issues related to zakat on business which is presented in the following section.

Methodology

This study carried out a library search and reviews of prior literature and guidelines about business zakat issues and practices. The references, which are publicly available, are compiled from various sources namely accounting standards, zakat calculation manuals, the website of state zakat institution, and the annual reports of businesses listed on Bursa Malaysia. The information obtained is used to identify issues, methods, and practices related to business zakat.

Issues Related to Zakat on Business.

In discussing issues related to zakat on business, especially in the accounting aspect, the Malaysian Accounting Standards Board (MASB) through Technical Release i-1, Accounting for Zakat on Business, has outlined several aspects that deserve attention. Those aspects are the assessment of zakat, which includes four main components: the zakat rate, the zakat base, how to determine the base of zakat, and finally, how to measure the assets and liabilities of zakat. Another issue that has been well explained in the document is related to the presentation and disclosure of zakat information in the notes of financial statements.

Nevertheless, Technical Release i-1, according to Abdul Kadir and Abdullah (2019), focuses more on how a company accounts for zakat (including disclosure in the financial statement notes) than the aspect of zakat calculation. With that, they suggest that there is still a gap between zakat reporting for the purpose of accounting reporting and the information required for the purpose of zakat calculation. At the same time, the researchers acknowledged the commendable initial efforts by standard accounting to disentangle to some extent issues related to business assets and zakat.

With regard to Technical Release i-1, it has highlighted several issues pertaining to zakat on business, which are: zakat on business entities, zakat calculation, zakat base determination, and zakat eligibility for assets and liabilities. However, these issues are beyond the jurisdiction of the MASB, which only focuses on the accounting aspect, and these issues are under the authority of the zakat institution. For that, it is recommended that zakat institutions in Malaysia to be more proactively through collaboration with accounting bodies to build comprehensive guidelines related to zakat on business.

Considering the importance of promoting good zakat governance practices, Jabatan Wakaf, Zakat dan Haji (JAWHAR) as the body responsible to coordinate waqf, zakat and hajj affairs in Malaysia, has published a Zakat Calculation Management Manual (Manual Pengurusan Pengiraan Zakat or the Manual) to be used as a reference. For the aspect of zakat on business calculation, one of the things emphasised in the manual is the obligatory condition of zakat on business. Among the things that companies need to pay attention to are:

- a. Mixing capital ownership between Muslim and non-Muslim owners and shareholders.
- b. Mixing between halal and haram business activities.
- c. Value of business asset (nisab) between Muslims and non-Muslims.
- d. The asset/property's ability to grow or generate wealth (al-Nama').
- e. The perfection of ownership is only open from the physical aspect (hiyazah) to managing its administration (tasarruf).
- f. Method of asset acquisition (through exchange rather than other methods such as inheritance or charity).

- g. The elements of business intention and practise must be present.

In discussing the calculation of zakat, some issues should be identified and resolved first. It is important for a business owner, especially a financial statement preparer, to understand this issue. According to the Manual, the issues that need serious attention are:

- a. Identification of current and non-current assets.
- b. Investment category, whether long-term or short-term
- c. Identification current and long-term liabilities.
- d. Determination shareholder funds or capital

Through the Manual, JAWHAR stated that there are 2 zakat calculation methods that can be used by a business as follows:

- a. Working Capital Method:
 $[(\text{Current Assets} - \text{Current Liabilities}) +/- \text{Adjustment}] \times \% \text{ ownership of Muslim Shares} \times 2.5\%$
- b. Capital Growth Method:
 $[(\text{Owner's Equity} + \text{Long-Term Liabilities} - \text{Fixed Assets} - \text{Non-Current Assets}) +/- \text{Adjustment}] \times \% \text{ ownership of Muslim Shares} \times 2.5\%$.

Based on a preliminary search on the website of the Zakat Institutions (ZIs) in Malaysia, it was found that these two methods are indeed the recommended ones to be used by businesses. In fact, there is a zakat calculation function (i.e., zakat calculator) provided for the purpose of zakat calculation, and zakat payers are also given clear guidance in calculating zakat. The following is an example of a business zakat calculation (Figure 1) and calculator (Figure 2) provided by the Kedah State Zakat Board.

ZAKAT PERNIAGAAN



DALIL MENGENAI ZAKAT PERNIAGAAN

Firman Allah S.W.T yang bermaksud:

“Orang-orang yang tidak dilalaikan oleh perniagaan atau jual beli daripada mengingati Allah dan mendirikan solat serta menunaikan Zakat”

(Surah An-Nur : Ayat 37)

Syarat-Syarat Zakat Perniagaan

- Islam
- Kepunyaan Mutlak
- Niat Menjalankan Perniagaan
- Cukup Haul
- Cukup Nisab
- Perniagaan Yang Halal

Kadar Bayaran Zakat Perniagaan

- Kadar bayaran zakat perniagaan ialah sebanyak 2.5% atau 1/40 daripada jumlah harta perniagaan

Kaedah Pengiraan Zakat Perniagaan (bagi syarikat yang mempunyai Penyata Kewangan)

- Sdn. Bhd. - GLC
- Berhad - Koperasi
- PPK

Kaedah (A)

Kaedah Modal Kerja (Syar'iyah)
 Aset Semasa – Liabiliti Semasa +/- Pelarasan = Harta perniagaan yang diwajibkan zakat

Kaedah (B) - Institusi Kewangan

Kaedah Modal Berkembang (Urfiyyah)
 Ekuiti pemilik + Liabiliti Jangka Panjang – Aset Tetap – Aset Bukan Semasa +/- Pelarasan = Harta perniagaan yang diwajibkan zakat

Kaedah Pengiraan Zakat Perniagaan untuk Milikan Perseorangan (bagi perniagaan yang tidak menyediakan penyata kewangan)

- Kedai Runcit - Pasaraya
- Syarikat Enterprise - PKS / IKS

(A) Aset yang diwajibkan zakat pada tarikh cukup haul	BINGGIT MALAYSIA (RM)
Tunai dan Setara Tunai (Akaun Simpanan, Akaun Semasa dan lain-lain)	15,000
Stok barang jualan (anggaran sahaja jika tiada rekod yang tepat)	10,000
Penghutang dagangan (anggaran yang diyakini kutipannya sahaja)	20,000
Jumlah	45,000
(B) Hutang perniagaan pada tarikh cukup haul (ditolak daripada nilai aset)	
Pembekal stok jualan (nilai hutang kepada semua pembekal)	10,000
Belanja operasi belum bayar (sewa kedai, bil utiliti, gaji pekerja dan sebagainya)	9,900
Tolakan lain : Pendapatan Kaedah Bank Konvensional	100
Jumlah	25,000
(C) (x) % Milikan Muslim (Sekiranya berkaitan)	
(D) Nilai bersih aset diwajibkan zakat (A-B x C=D)	25,000
Jumlah zakat = Nilai D x 2.5% (Kadar Zakat)	625.00



IMBAS UNTUK
PENGIRAAN

Figure 1: Zakat on business – Kedah State Zakat Board

(source: <https://www.zakatkedah.com.my/zakat-perniagaan/>)

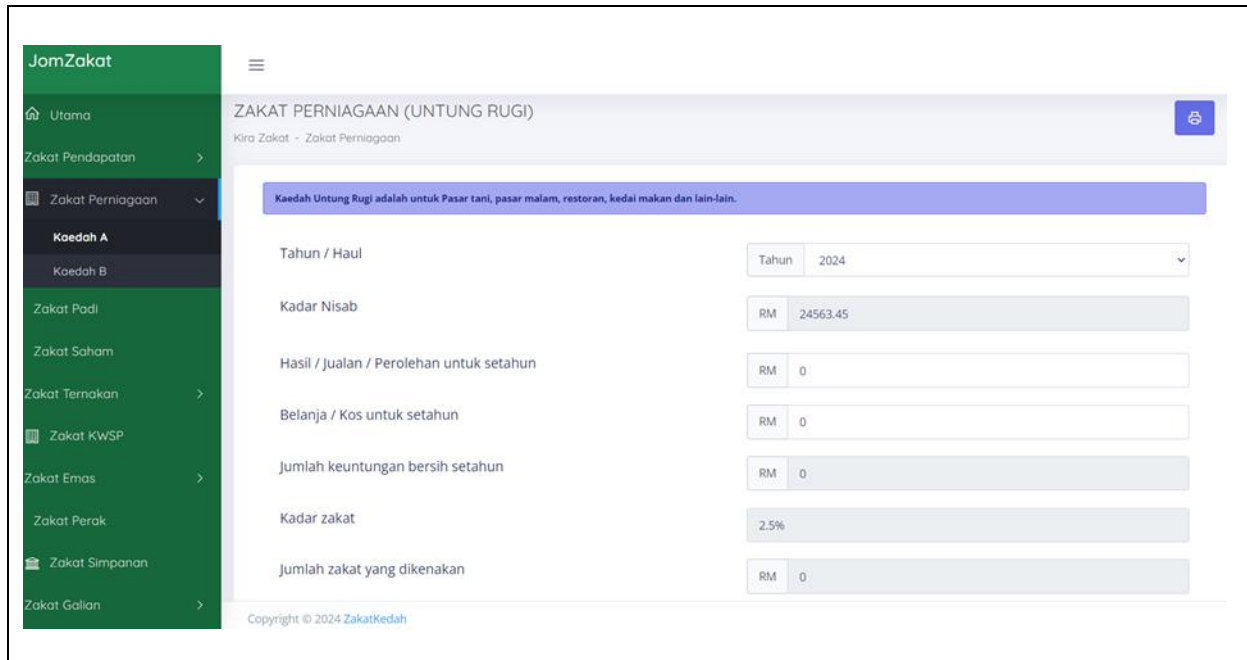


Figure 2: Calculator of zakat on business

(source:<https://jom.zakatkedah.com.my/kirazakat/tabkirazakat.php?op=1>
 Accessed on 23 January 2024).

Therefore, in the method of calculating zakat on businesses, the manual issued by JAWHAR provides great benefits to zakat management institutions. This manual promotes the uniformity of zakat calculation practices in Malaysia. Confusion about how to calculate can be minimized and entrepreneurs/companies are given a choice in determining the calculation method that suits their business.

Zakat on Business Reporting Practices in the Company's Annual Report

Presentation and disclosure in financial statements. One of the important features of quality financial statements is that they present and disclose financial information that is useful for users. The same is the case with the presentation and disclosure of information related to zakat on business. This information must be disclosed in financial statement so that the users, especially Muslim, get a clear picture of zakat expenditure. FRS 101, 'Consolidated Financial Statements, issued by MASB in paragraph 10 states that:

“A complete set of financial statements comprises:

- a. a statement of financial position as at the end of the period;
- b. a statement of comprehensive income for the period;
- c. a statement of changes in equity for the period;
- d. a statement of cash flows for the period;
- e. notes, comprising a summary of significant accounting policies and other explanatory information; and
- f. a statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.”

The practise of zakat disclosure in financial statements

In relation to the practice of presenting and disclosing information related to zakat, the following is an example of the disclosure of zakat-related information in the financial statement of Syarikat Takaful Malaysia Keluarga Berhad for the year ended 31 December 2021. The amount related to zakat is stated in:

- a. Statements of Profit or Loss And Other Comprehensive Income – stated as zakat
- b. Statements of Cash Flows – stated as zakat paid

Also, the following information is disclosed in the financial statement notes, which are part of the Summary of Significant Accounting Policies. The note explicitly states that:

Zakat

This represents an obligatory amount payable by the Group and the Company on behalf of its individual Muslim shareholders to comply with the principles of Shariah. Zakat is computed at 2.5775% of zakat base amount of the Company, which is computed using the “Adjusted Growth method”. The zakat computation is reviewed and approved by the Shariah Advisory Body. The Board has the discretion to pay additional amount above the obligatory zakat amount payable.

In general, this disclosure contains information about: (i) the company's responsibility for zakat, (ii) zakat rates, (iii) zakat calculation methods, and (iv) the Board of Directors' responsibility for the amount of zakat.

Other information disclosed in the notes to the accounts is the amount of zakat payable. The disclosure is presented in Figure 3 below:

NOTES TO THE FINANCIAL STATEMENTS

19. Other payables

	Note	Group		Company	
		2021 RM'000	2020 RM'000	2021 RM'000	2020 RM'000
Takaful Operator					
Deposit payable		263	263	263	263
Zakat payable		1,319	1,351	600	600
Dividend payable		100,275	99,652	100,275	99,652
Other payables and accruals		203,485	173,706	159,974	134,927
		<u>305,342</u>	<u>274,972</u>	<u>261,112</u>	<u>235,442</u>
Family Takaful					
Advanced takaful contribution		7,326	28,567	7,326	28,567
Deposit payable		3,695	4,436	1,699	1,659
Unclaimed monies		12,837	10,614	7,957	6,948
Due to Takaful Operator	11	43,375	40,376	43,313	40,340
Other payables and accruals		55,690	61,591	52,378	58,484
		<u>122,923</u>	<u>145,584</u>	<u>112,673</u>	<u>135,998</u>
General Takaful					
Advanced takaful contribution		24,194	25,314	-	-
Deposit payable		117	117	-	-
Profit payable to participants		890	738	-	-
Due to Takaful Operator	11	30,703	21,754	-	-
Due to Family Takaful	11	106	302	-	-
Other payables and accruals		32,074	32,465	-	-
		<u>88,084</u>	<u>80,690</u>	<u>-</u>	<u>-</u>

Figure 3: Notes To The Financial Statements - Other Payable

(source: Annual Report 2021 Syarikat Takaful Malaysia Keluarga Berhad)

For the segemental reporting, the amount of zakat expenditure is presented in Figure 4 below:

NOTES TO THE FINANCIAL STATEMENTS			
35. Operating segments			
<p>Segment information is presented in respect of the Group's geographical segments. This is based on the Group's management and internal reporting structure. Inter-segment pricing, if any, is determined based on negotiated terms. The Group does not present information by business segment as it is principally engaged as an operator of Family and General takaful / retakaful businesses. The financial position and performance of the Family and General Takaful businesses managed by the Group and the Company have been disclosed separately within these financial statements.</p> <p>Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise expenses, which are all incurred by Takaful Operator for the management of Takaful funds.</p> <p>Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.</p> <p>In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets are also based on the geographical location of assets.</p>			
Geographical segments			
	Malaysia RM'000	Indonesia RM'000	Consolidated RM'000
2021			
Total external revenue	3,054,416	124,594	3,179,010
Inter-segment revenue	-	-	-
Total segment revenue	3,054,416	124,594	3,179,010
Segment result / Profit before zakat and taxation	435,248	3,452	438,700
Zakat			(1,316)
Tax expense			(25,184)
Profit for the year			412,200

Figure 4: Notes to The Financial Statement – Operating Segments

(source: Annual Report 2021 Syarikat Takaful Malaysia Keluarga Berhad)

Based on the above figures, information related to zakat is stated as zakat payable and zakat expenditure. The amount of zakat payable for both years is also given for the purpose of facilitating comparison. Meanwhile, zakat expenses for business operation areas have been consolidated. The implementation of payment and disclosure of zakat information by businesses is a commendable act, and this information is disclosed in financial statements that can be accessed by the public.

Zakat disclosure recommendation

There is some room for any companies to improve their zakat information disclosure practices in financial statements. Apart from the information as discussed before, other information that could be presented for the purpose of zakat on business are determination of zakatable assets and liabilities, investment classification, and further details of zakat recipients. The preparation of information related to zakat in the financial statement can be made by referring to the Technical Release i-1 issued by MASB. It is important to note that comprehensive zakat information disclosure can influence the business decisions of users of financial statements.

Conclusion

Zakat is a religious obligation that must be fulfilled by every Muslim. From an economic perspective, the obligation to pay zakat can help ensure a balanced distribution of wealth and reduce the gap between the rich and the poor. The obligation to pay zakat is not only focused on Muslim individuals but also involves Muslim business entities that need to issue zakat on business based on their wealth. However, there are some issues involving zakat on business that need to be refined. This issue covers aspects of zakat on business payment eligibility, asset and liability classification, zakat calculation, and accounting practise requirements (for example disclosure in financial statements). The need for further disclosure of zakat information in financial statements is still not mandatory, and this causes users to not get a clear picture of the implementation of zakat on business activities. It is hoped that the above-mentioned issues can be resolved through close consultations and cooperation between private sector, zakat authorities, and accounting bodies.

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