

Short Communication

Managerial Accountability: A Review through Orphanages' Financial Record Practices

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ABSTRACT

The most significant role of non-for-profit (NFP) is to alleviate or to provide remedy to discrepancies in the delivery of social benefits by the private or the public sector. Thus, the accountability rendered by particular management group has become a crucial element to all stakeholders, particularly the donors (contributors). The purpose of this study was to examine the practices of accounting record of a few orphanages located in the district of Hulu Langat, Selangor. Through systematic and proper accounting records, the orphanage management could prove its accountability and satisfy the custodial role. This study employed survey to the orphanage management which had been selected through convenience sampling technique. From the analysis, it was concluded that the orphanage management has maintained their book-keeping which comprises of a simple list of income and expenses. However, the reporting standard requires for improvement so as to increase its usefulness and to allow accurate judgement on donation decision-making. In addition, an improved financial record will lead to a higher level of custodianship of the entrusted resources.

Keywords: Accountability, ethics, agency relationship, financial, non-profit organization

INTRODUCTION

Three main sectors in economic structure consist of the private, public and non-for-

profit (NFP) organizations. Each sector has their own role in satisfying the nation's development needs. In conjunction with developing countries, NFP has far more important role in terms of complementing or remedying the weaknesses of social good delivery of its private and public sectors.

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Orphanage is one of the NFP which renders unique services in terms of promoting the well-being and interest of the orphans.

Orphanage is not a new concept to the world. According to Jacobi (2009, p. 57), a large group of orphanages was founded in Europe during the sixteenth or early seventeenth century to provide education and assist the orphans in their transition into adulthood. Orphanages have been recognized as successful institutions in relation to orphans' upbringing since the early modern years. They have offered majority of the needy children with the opportunities to grow and to cope successfully with the norms and expectations of the world around them (Jacobi, 2009, p. 64). Meanwhile, the philanthropic-based effort has been receiving various aids and financial supports from the public now and then. Hence, the purpose of this study was to identify orphanages' practices of book-keeping and financial reporting as issues related to the accountability of the orphanages management.

PROBLEM STATEMENT

Accountability in financial management is indeed important for all types of organizations. Business entities are not the only type of organization which accumulates resources from its community (known as investors and lender groups). The non-profit oriented entities, such as the public and the non-for-profit (NFP) organizations, have also been similarly entrusted with valuable resources which are required for the disposition of management accountability

as well. NFP accountability, as well as its governance, has recently received attention from the public (Nag, 2010; Leong, 2010). This is because the resources are limited, and thus, an efficient use of resources is compulsory to achieve the organizations' goals. In addition, the donors have made their contributions with specific expectations and beliefs regarding the uses. As a result, it must be managed in the best interest of the expected targeted groups. Furthermore, there are circumstances in which the orphans have been exploited as the collecting agents for the sake of particular groups/individuals (Syed Ahmad Zulkarnain, 2010). This has raised concerns over the management accountability as the responsible custodian of the entrusted resources. As a result, this study was conducted to accomplish the following objectives:

1. To describe accountability of the orphanages' management through description of its financial record practices; and,
2. To explore the relevancy of accountability and governance issues within the scope of orphanage organizations.

LITERATURE REVIEW

Charitable giving is a form of well-institutionalized culture which plays a role in alleviating problems of capitalism (Hur, 2006, p. 661; Saunah *et al.*, 2009, p. 176). Furthermore, according to Saunah *et al.* (2010, p. 177), the not-for-profit (NFP) is one of the three main sectors in today's

economy which has grown its economic importance, as reflected in the European System of Accounts (ESA-1995). The other two are the private and public sectors. According to Wang and Graddy (2008), the level of giving in a particular society serves as an indicator of the civil society's strength. Competition for obtaining financial support is currently intense among the non-profit or charitable organizations (Hsu, Liang, & Tien 2005). The management has to adopt certain strategies in order to secure the long-term fund availability of their organizations. Thus, it is important to understand the factors that will affect the intention and behaviour for charitable donations and supports, as raised by Hsu *et al.* (2005). According to Hsu *et al.* (2005), reputations of charities and types of recipients are critical in determining donors' trust to continuously support charitable organizations.

Resource development efforts can benefit from the well-established relationships that an entity has with their key-constituent groups and influential individual members in their communities (Hall, 2002, p. 47). As a result, preserving and maintaining good relationships with key stakeholders is crucial for the survival of non-profit organizations. The relationship inevitably secures the short-term and long-term resource availability of the particular entities. Thus, trust is an important element to build a good relationship and to encourage giving activities among members of the society. Wang and Graddy (2008, p. 29) found that social trust is one of the factors that increases the amount of charitable

giving either for religious or secular cases. According to Wang and Graddy (2008), social capital has been increasingly applied as an analytical tool to explain variances in the performance of individuals and organizations. It refers to network, norms and social trust as the facilitating engines. Trust is developed through evaluation and perception towards the exercise of stewardship and accountability of the management. The donor requires the management to provide assurance that the contributed resources have been properly managed and able to achieve its purpose. In their study, Hsu *et al.* (2005) proposed that intentions to give donation could be increased if more relevant information was made available to potential donors. Although Hsu *et al.* (2005) found that information regarding financial management of the charity organization is of less concern when it comes to determining donors' supports, Saunah *et al.* (2010) reiterated that financial reporting has its importance in describing delivery of management accountability, as well as in enabling evaluation of management efficiency and effectiveness. Moreover, according to Saunah *et al.* (2010, p. 177), the means to understand the performance of charitable organizations in Malaysia is still limited due to unavailable or restricted sources of information, including the financial statements. Within the perspective of governance, Skousen (2005, p. 53) suggested that the fundamental aim of effective corporate governance is to produce fair and true financial report. Meanwhile, the role of true financial report

is crucial due to the asymmetric situation between organization's stakeholders and its management, which eventually threatens the interest of the absentee stakeholders (namely, the shareholders). As in the case of NFP organizations, the absentee stakeholders can be referred to the donor groups who have contributed their resources altruistically.

As far as the financial report is concern, the ability to produce such a report requires proper accounting records. The study by Saunah *et al.* (2010) revealed that there are variations in reporting practices among the Malaysian tax-exempt charitable organizations. This is due to the minimum regulatory requirement and the absence of reporting standards, which were established for the NFP financial reporting in Malaysia. As explained by Saunah *et al.* (2010, p. 181), according to Section 14(d) of the Societies Act 1966 (Act 335) and Regulations, the organizations registered under the Registrar of Societies (ROS) must submit Form 9 that consists of the Statement of Receipts and Payments of the previous financial year and a balance sheet of the respective year to the ROS within 60 days after its annual general meeting. However, the accounts are not necessarily be audited by the external auditors. Other statements which supplement the financial statement, such as the cash flow statement, statement of changes in general fund and notes to accounts (containing significant accounting policies and other explanatory notes) are also not required to be submitted by ROS. Moreover, Saunah *et al.* (2010) found that

only 18/37 or 49% of the NFPs submitted their Statement of Receipts and Payments, together with the Balance Sheet to ROS, as required by the Societies Act 1966 (Act 335) and Regulations. The contributions of this study lie on its' emphasis on the orphanage institutions, whereby Saunah *et al.* (2010) had focused on various tax-exempt charitable organizations in Selangor. Furthermore, this study involved the primary data which were obtained through surveys that had been carried out with selected orphanages' management. Thus, the use of primary data contributes to an understanding of orphanages operations and its financial aspect, as well as the practices of accounting record/reporting processes.

METHOD

This study falls in the category of exploratory study. As explained in Babbie (2004, p. 87), there are three common purposes in research; these are exploration, description and explanation. According to Babbie (2004, p. 87-89), exploratory study is suitable if the researcher wants to explore a new topic and become familiarize with the relatively unattended topic. In specific, there are three reasons for conducting an exploratory study, as stated below:

1. To satisfy researchers' curiosity and desire for better understanding;
2. To test the feasibility of undertaking more extensive study; and,
3. To develop the methods to be employed in subsequent study.

Thus, exploratory study is very much close to the inductive type of reasoning, rather than the deductive (Babbie, 2004, p. 52-53). As explained by Babbie, constructing a theory through inductive method requires researchers to observe the aspects of social life and to discover patterns that may point to relatively new ideas. This is significantly different from the deductive approach, in which all the key variables must be clearly identified and precisely measured using specific established measurements, and when testing of the specified relationship models is required. Nonetheless, exploratory studies possess some weaknesses, which include lacking of rigorous theory or precise expectations and rarely providing satisfactory answers to the research questions. Despite these weaknesses, exploratory studies are valuable in social scientific research, especially when the researchers attempt to yield new insights into topic for research (Babbie, 2004, p. 88-89).

This study involved orphanages in Hulu Langat Selangor. The selection of these orphanages was done through convenience sampling due to the difficulty in obtaining

co-operation from their management. Seven (7) orphanages finally agreed to participate in this study. Table 1 shows a summary of some of the involved orphanages' particulars.

There are two sections in the questionnaire. The first section comprises of the sources of income and the second section contains 14 questions on handling of accounting records. Short interviews were also conducted with a few orphanages in order to get detailed explanations on certain issues. The interviews were informally and simultaneously conducted to the administration of the questionnaires to obtain clarification for unclear matters, such as in the case of deficit, i.e. how did the management handle such a critical situation. The field work was done between August and September, 2010. The data were descriptively analyzed.

ANALYSIS

Table 2 shows a summary of the information about the selected orphanages.

As shown in Table 2, all the orphanages stated that their main source of income

TABLE 1
A summary of the details of the orphanage homes which participated in the current study

Orphanage homes	Year of establishment	Founder background
A	2007	Local NGO
B	2006	Individual
C	1966	NGO
D	2008	Individual
E	2005	Individual
F	-	Individual
G	1990	NGO (religion-base)

TABLE 2
A Summary of Orphanages' Sources of Income (Asset) and Expenses

No.	Orphanage	Sources of Income	Building/ premises	Average of Monthly Expenses (RM)
1.	A	Founder, society, NGO and sales of unused perishable donated items.	Contributed by NGO.	RM 8,536.24
2.	B	Tithe (<i>Zakat</i>), society, sponsorship, nursery, and café projects.	Rental and there are also orphans who are staying with their relatives, but their expenses are financed/ sponsored by orphanage B.	RM 28,986.00
3.	C	Society, corporate entities, and government.	Endowed land by state government.	No information
4.	D	Society	2 houses – one house is rented and the other house is an individual endowment (<i>waqaf</i>).	RM 11,078.00
5.	E	Society and corporate entities.	Rental	RM 8,485.00
6.	F	Society, NGO, founder's friends & relatives, and the local people	Individual private endowment (<i>waqaf</i>) of a house and a piece of land.	RM 10,335.00
7.	G	Government, society, special fund-raising project, and corporate entities.	Purchased self-own building.	No information

came from public donations. The donors comprised of individuals and corporate entities. Most of the corporate entities make their donations as parts of their CSR or as ways to reduce their business taxation. The types of donation received are usually in the form of cash, as well as in kind, such as groceries and clothes. The management also reported that the groceries items received are sometimes in bulk, which cannot be entirely used within their useful periods. As a result, the perishable items donated are sold to obtain additional funds for the orphanages and to avoid wastage. In addition to the cash and in kind, there are few orphanages which have received donation in terms of

building (premises) and lands for operating the homes, such as in cases A, C, D and F. This finding has further highlighted the importance of maintaining proper book-keeping and recording due to obligations owed towards various types of donors and contributors.

Meanwhile, a majority of the orphanages encounter income deficit in relation to their expenses. The incurred costs bore the orphanages vary in the range of RM8,536 to RM28,986 per month. The expenses items consist of utility, house-maintenance (including the rental), orphans' welfare (including the expenses for clothing and medication), transportation, schools and

groceries/food expenditures. Due to the deficit, some of the orphanage operators have to use their personal sources to overcome it, especially to cover certain fixed expenses, such as the rent and food/groceries. One orphanage has conducted business activities such as operating a nursery and a café business to generate additional income. However, the management reported that the income from these business activities is still insufficient to cover the overall operating expenses. Meanwhile, one orphanage has

received fixed aid from the government, specifically from the Ministry of Welfare.

EVALUATION OF ACCOUNTING RECORD PRACTICES

Table 3 shows the frequencies of the managerial responses to the 14 items in the questionnaire.

All the orphanage homes admitted to have prepared their annual financial reports and maintained their account records and book-keeping. From the observation,

TABLE 3
A Summary of the Management Responses on Financial Record Practices

No.	Items	N	Yes	No	Sometimes
1	Prepare the financial report annually.	7	7	-	-
2	Keep and maintain financial documents/ records systematically.	7	7	-	-
3	Have a specific unit/ an individual to handle organization's accounting record.	7	7	-	-
4.	Hire individual with book-keeping skills to manage organization financial records.	7	4	2	1
5	Every year, the organization submits its financial report to the registrar of association.	7	3	4	-
6	Every year the organization sends its financial report to the donors (contributors).	7	2	5	-
7	Every year, the organization sends its financial report to the main/ significant donors (contributors).	7	2	5	-
8	Accounting records are kept properly and available for verification at any point of time.	7	7	-	-
9	Financial report has been audited by external auditors.	7	3	4	-
10	The organization has established its internal audit committee.	7	4	3	-
11	Accounting records and operational procedures are monitored by the internal audit committee.	7	4	3	-
12	The organization has recorded the income according to its specific purpose/ use of the raised-fund (e.g. operation fund, orphanage development fund, education fund).	7	7	-	-
13	Obtain any tax exemption.	7	4	2	1
14	Receive fix government aids consistently.	6	1	5	-

however, it was found that the records have been maintained at the minimum level, without specifically complying with any accounting standards and procedures. Book keeping involves a simple list of the sources of income and expenses. There is a situation in which the disbursement is not recorded due to unavailability of relevant documents. Furthermore, most of the orphanages did not prepare balance sheets to show their financial positions for the reported year. As a result, the organizations' fixed assets and liabilities are not traceable throughout the record.

All the orphanages reported that they hired specific individuals to handle their accounting records. In particular, four of the orphanages hired workers with book-keeping skills to manage their records, while three others reported that they did not hire skilled workers to do the said task.

In terms of communication of the financial report, only three orphanages had sent their annual financial reports to the Registrar of Association. Meanwhile, only two orphanages sent their financial reports to their donors, and five others reported that they did not send any financial report to its donors or contributors.

Three orphanages claimed that their accounts were audited by external auditors. Four orphanages reported that they have their internal audit committee and two obtained financial statement verification from external auditors. Four of the orphanages claimed that the audit committee also monitored their accounting records and operations. All the orphanages claimed that

they established specific funds to record fund obligation for the specified purposes.

DISCUSSION

The most critical challenge faced by the orphanage management is to maintain the availability of fund. This requires continuous relationship between the donors and orphanage management founded on trust basis. The donors have contributed to the organization and such condition lead to the agent-principal relationship between the orphanage management and the donors. The agent (which refer to the orphanage management in this context) have the obligations to fulfil the expectations of its donors in terms of the entrusted resources. One of the methods that can be used to maintain orphanage-donors trust-based relationship is through the presentation and communication of the orphanage's financial report. The financial report allows the stakeholders to evaluate the orphanage's performance, form trust in the management accountability and finally increase the level of donation intention. The requirement for maintaining a systematic accounting record and producing a proper financial report is also in line with Section 29(a) and (b) of the Societies Act 1966, which state that:

“Every registered society shall supply free of charge to every member or subscriber or person having an interest in its funds on his application either:

- a. A copy of the last annual return of the society; or

- b. A balance sheet or other documents duly audited containing the same particulars as to the receipt and expenditure, funds and effects of the society as are contained in the annual return”.

As a result, through a systematic and proper accounting record, the orphanage management can prove its accountability. Although the orphanages have prepared their financial statements, these could have done in various presentations and the level of comparability is relatively low. Thus, these distort the ability to evaluate the efficiency and effectiveness of the entrusted management. Furthermore, it is relatively difficult for the stakeholders to gain standard information about the performance of the orphanage due to the variation in their financial reporting.

A systematic record also serves as a control mechanism to assure an efficient and effective use of an organization's resources. The efficient use of resources is essential to minimize the occurrence of deficits. Meanwhile, the absence of a systematic record will lead to inefficiency and hinder improvement to the organization's financial management. Based on the informal interview conducted, for example, there is one orphanage which allows any of its employees to access and make disbursement from its petty-cash and this is merely based on the sense of trust. The employees who have made the disbursement from the petty cash are supposed to give the expenses receipts based on self-trust. The

management stated that such a practice is being implemented due to reasons as follows:

1. Necessities to make immediate expenses whenever the person in-charge is not around; and,
2. The amount of the petty cash is relatively small.

However, such practice may potentially lead to inefficiency and abuse of fund by irresponsible individuals. Furthermore, the practice will also hinder the management from tracking any inefficiency or abuse and distort the presentation of a true and fair view of the financial position for the particular orphanage. Moreover, the unavailability of auditor verification has further increased the ambiguity of the information provided in such practice. The absent of auditor's verification on some of the orphanage accounts is also against the rule of Sections 26(1) and (2). The sections require the registered entity to submit its accounts for audit at least once a year and the auditor should have the access to all books and accounts as well to examine the accuracy of the reported annual return.

In conclusion, although the orphanage homes have been established on virtuous and philanthropic motive, it is still necessary to adopt systematic financial management and records in the operations. This is because the community would appreciate the philanthropists more and to give more collective support (financially and non-financially) in return, if the management could visibly manifest their utmost integrity

and accountability. One of the important means to deliver such accountability and integrity is through the practices of a systematic financial record and reporting.

IMPLICATIONS AND RECOMMENDATIONS

The existence of orphanages has complemented the government's role in providing social benefits for its citizens. The role has been in existence throughout the history of the world's modern society since the sixteenth century. Thus, the orphanages need to be transformed into credible and systematic organizations to enhance their community support capacity.

Therefore, some financial aids should be given to ease the financial burden of its operators. For instance, the government may allocate a special trust fund to cover at least half of the orphanages' basic operational expenses in the country. As far as the special fund is concerned, the government may impose strict requirements for each of the orphanages to produce and submit a standardized financial report as one of the terms for continuous fund allocation. In the long run, this will serve as a two-pronged strategy targeted at assisting the orphanages operations and promoting a higher standard of institutional accountability. In addition, the corporate sectors may also include orphanages as one of the subjects in their corporate social responsibility (CSR) programme.

In order to secure a continuous availability of funds, the operators could venture into business activities, as done

by one of the orphanage in this study. Although the effort could provide income independency for the orphanages, it would require additional fund to finance the activity. Furthermore, the project also requires some entrepreneurial and business management skills in order to ensure its profitability. In relation to the financial reporting, improvement can be done by hiring skilled individuals to do book-keeping. As the orphanages also owe the public their financial support, it is highly necessary for them to produce and communicate their financial positions to the interested stakeholders. As far as the financial management and accounting skills are concerned, higher educational institutions could provide some training programmes to employees of the orphanage homes. Such effort can be made part of the varsities' community services and as an implementation of experiential-based learning approach in their teaching mode. The experiential-based learning is a contemporary approach in the teaching of business management which includes real-life consultation opportunity (Ahmad Raffles *et al.*, 2010).

As far as the implications to the body of knowledge are concerned, the current study has satisfied the three reasons underlying the venture of an exploratory study. Based on this study, the issues of accountability and governance within the scope of orphanages have satisfactorily been proven as relevant and worth studying. However, the new topic requires more qualitative and inductive approach to comprehend aspects pertaining

to orphanage entity in detail. Based on the findings of this study, it is important for the researchers to develop a trust-based relationship with the management of the orphanages. One of the possible strategies is by becoming part of the organizations' contributors. However, the strategy requires incessant commitment, financial and time, as trust evolves through a passage of understanding and also sincerity between the parties involved.

LIMITATIONS AND SUGGESTIONS FOR FUTURE RESEARCH

This study relied on the convenience sampling technique due to the difficulty in obtaining co-operations from the management of orphanage homes. In particular, the orphanage management showed some degree of sceptic to disclose information to the outsiders. As a result, the number of orphanages involved in this study was relatively small. Though the number of the samples involved was relatively small (seven entities), this study has contributed towards exploratory of new area and creating awareness among the academicians regarding the gap in the social studies that is worth studying. Thus, future studies should involve more orphanages in order to increase the level of generalizability. As the number of respondents was relatively small, this study was constrained to performing the high-end statistical method which could provide more accurate insights into the issue. However, this limitation does not affect the contribution of this study as it is descriptive in nature and meant to promote

future exploration related to orphanages entities.

Meanwhile, the evaluation used in this study was based on management self-evaluation. Thus, it posed a threat of biasness in the evaluation of record maintenance practices. Two possible biases for the self-evaluation method comprised of the social desirability bias and management impression bias. As far as the bias is concerned, future studies should include evaluation from donors as well as directly evaluate the entities' financial statement. However, this effort can only be done if these orphanages were maintaining a proper donors' database, preparing their financial report and allowing researchers to access the relevant database.

In addition, future studies should also investigate the factors influencing donation decision-making among the donors. Such a study is particularly important to increase the level of donation as well as to secure income through adoption of accurate strategies and promotions which are able to capture the attention of prospective donors. This is due to the fact that fund-raising has evolved towards strategic and pro-active conditions, and thus requires a strategic and market-oriented fund-raiser. In addition, future studies could also explore on the factors driving the altruistic behaviour among orphanage founders/operators. This is an area which is interesting to be explored by social scientists (especially those in Psychology and Organizational Behaviour), with respect to the high commitment shown by the orphanage founders, such

as the willingness to put high efforts and sacrificing personal fund or resource in running the non-profitable entity.

CONCLUSION

This study attempted to understand the challenges encountered by philanthropic action. The study of philanthropic action could be done from various perspectives, such as the perspective of the operators, donors, and the governing body. In addition, this study also evaluated issues pertaining to the practices of accounting record in the orphanages. As indicated previously, fund-raising has evolved from a pessimistic state to a pro-active condition that requires the ability to visibly communicate the accountability of the management. One of the ways to communicate the management's accountability and performance to stakeholders is through a true and fair accounting record and reporting.

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