

# The Influence of Internal Governance on Halal Compliance of Malaysian Food Industry: Preliminary Study

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## **Abstract**

**Purpose:** The purpose of this paper is to examine the influence of internal governance factor towards the Halal compliance of Malaysian food industry.

**Design/methodology/approach:** Since this study involves with the data preliminary study, a self-administered questionnaire has been distributed among the participants of the Halal management workshop organized by Halal authority, in which the participants were among the persons who were involved directly with their Halal-certified company's Halal affairs.

**Findings:** Top management's commitment is significantly and positively associated with all dimensions underpinning the Halal compliance variable of the Halal-certified companies.

**Research limitations/implications:** This study involves with a several number of sample of respondents that have been carried out in the first-phase of data collection on the compliance of Halal at firm level and the current study is expected to be extended to a larger sample of respondents of Halal-certified companies which covers in major region/cities of Malaysia.

**Practical implications:** The study highlights the important aspects that the Halal-certified companies should embrace ethical business practices of Halal compliance that inculcating and reinforcing food integrity among food producers in order to keep abreast with their long-term's business sustainability.

**Originality/value:** The study contributes a fruitful insight on the role of internal governance to oversee the dimensions of halal compliance at firm level in the first place.

**Keywords:** Governance, Halal, Compliance, Stakeholder, Food industry.

## **Introduction**

Halal food industry becomes one of the leading industries that undergoes a remarkable growth due to the increasing demand on the halal food by international and local consumers. Given the upsurging number of Muslim populations around the globe and food-borne diseases, these factors are important impetus to the growing demand on halal food and awareness on the food quality. Halal food can be defined as '*a lawful and permissible food that meet the Islamic dietary guidelines to be consumed by consumers*' (Riaz and Chaudry, 2003). In order to ensure that food products are classified as Halal food, the food products entail for the compliance of a set of Halal guidelines and procedures as stipulated by the Halal authority body (i.e. JAKIM) which allows the food producers to secure for Halal certification. Halal certification is a symbol of confidence and trust that urges the purchase intention (Awan, Siddiquei and Haider, 2015) and willingness of consumers to purchase food products (Iranmanesh, Mirzaei, Hosseini and Zailani, 2019) and is granted as a result of compliance to the Halal-related standards and guidelines as determined by JAKIM and other

religious council at the state level which in tandem with the Trade Descriptions Act (TDA) 2011 (Khan, Khan and Haleem, 2019; Ahmad, Ungku Zainal Abidin, Othman and Abdul Rahman, 2018).

Literally, the production of food products involves with the interaction between the supply and demand parties that range from the upstream to the downstream of Halal supply chain activities. As far as the source of food ingredients are concerned, the emphasis on halal procedure is given on the way food materials/ingredients are supplied as well as the halal status of the supplier. In the production process, the food is prepared that is beyond the knowledge and sight of consumers. It is important to note that most of the food manufacturers are among the small-medium typed companies (SMEs) which are characterized by the limited in size and capital funds. Besides, the compliance of Halal guidelines is perceived as complex and requires firms to incur at higher costs of compliance which seem as major barriers for companies to sustain in securing Halal certification (Khan, et.al, 2019) Hence, there is a likelihood that these companies may shirk from their responsibility to comply with the Halal-related standards and guidelines in the food production, which ultimately may lead to the various food scandal issues such as fake halal logo and other food-borne illness that could jeopardise the well-being of consumers.

Unlike in the preceding corporate-related studies which viewed the roles of top management is rather act in the opportunistic behaviour on the basis of agency theory (Jensen and Meckling, 1976; Germain, Galy and Lee, 2014; Che Haat, Abdul Rahman and Mahenthiran, 2008; Bhatt, 2016), however in the context of SMEs the top management forms as part of board of directors and plays significant roles in overseeing the business operation and adherence to the set of standards and procedures for the benefits of its stakeholders (Fotopoulos, Psomas, and Vouzas, 2010; Nik Wan, Abu Bakar, Razak and San, 2014)). Consistent with the business pendulum, firms are no longer are viewed as profit-oriented artificial persons, but they are expected to perform social obligations that could give positive reciprocal effects between the firm and its stakeholders (Freeman, 1984). Being the management team that is responsible in steering the company's direction, it is expected that top management of food-producing companies is responsible to ascertain that securing of halal certification and consistent compliance of Halal food procedures are successfully fulfilled. Concerning this matter, thus this study attempts to investigate the level of Halal food compliance and to examine to which extent that the top management could influence the Halal compliance at firm level amongst the Halal-certified companies. The review of literature pertaining to the Halal compliance and top management's responsibility is further discussed in the next section.

## **Literature Review**

### ***Halal compliance and Responsibility of Top Management***

The word 'Halal' is literally originated from the Arabic language which provide a meaning of 'permissible', 'allowable' or 'acceptable', and it is widely used to refer on food and other aspects (Ab Rahman and Jamaludin, 2011). To obtain Halal status, it entails for a certain degree of compliance to affirm the extent of such Halal implementation. As far as food is concerned, Halal compliance is often related with the adherence to certain requirements or guidelines on food sources and its preparation as in accordance to Islamic laws, which implicitly bring the Halal-certified or -compliant companies closer to securing Halal certification. Halal certification is an important tool for the business sustainability as it symbolizes a significant source of consumers' trust and confidence due to the food products are proven free from any impurities and unlawful substances therein as it is being protected by the Trade Description Act (TDA) 2011. Prior studies have proven that business premises

with authentic halal logo and obtained Halal certification have successfully attract and retain their customers (Ahmad, Mohd Sidek, Mohd Adi, Jusoh and Kim Soon, 2013; Mohamed, Rezai, Shamsudin and Eddie, 2008) and provide positive business outcomes (Ab Talib, Ai Chin and Fischer, 2017; Salindal, 2018).

Given the significant benefits of Halal certification to the business, however some businesses are still averse towards securing Halal certification through practicing appropriate Halal compliance as food producers perceive that there are handful of barriers and limitations of such implementation (Ab Talib, Abd Hamid and Ai Chin, 2015). As being asserted by Khan, et.al. (2019), an effective halal compliance calls for external and internal supports including extensive government support, management and staff support and their commitment, adequate business resources and consistent implementation. Realising that Halal compliance and securing halal certification is a voluntary action of food producers, hence it is crucial to have an internal support especially from top management team to uphold the halal compliance endeavour and to ascertain consistent compliance to several stipulated requirements by national authority (i.e. JAKIM). As far as consumers' well-being is concerned, those manufacturers who fail to do so may implicate to the sustaining their Halal status and Halal certification may be revoked out of business, which ultimately could shake the consumers' confidence towards the business.

Although there are number of studies have been undertaken on the governance, however governance matters are given more focus on the large companies. Unlike the large-typed companies, there are few studies have been documented on the internal governance of small-medium type companies especially focusing on halal industry, as this industry is at growing stage and requires various supports from relevant and related parties. At firm level, the implementation of halal procedures is subject to the voluntary action of companies and such halal implementation may be undermine by the internal management due to lack of understanding and knowledge on halal affairs. For instance, Khan, et.al. (2019) have identified that weak support from internal management has caused the poor enforcement and compliance of Halal procedures and guidelines. Even though there are strong external governance roles at national level which is functioning to motivate and encourage the potential and existing halal-certified companies to continuously comply with the Halal standards and procedures, however the utmost important roles lie on the internal management to spur the halal implementation. Ahmad et.al. (2017) found in their qualitative study that top management is one of the critical factors that influencing the effective implementation of halal food management systems. Their study also found that top management commitment, customer focus, supplier management, halal training and policy and procedures constitute as essential elements in the halal implementation.

Most of the prior studies on halal governance are intensively confined on external governance by the government authorities (Mohd Noor and Noordin, 2016; Saad, Abd Rahman and Muhammad, 2016; Shafii, Zubir and Rahim, 2018; Noordin, Mod Noor and Samicho, 2014). Md Noor and Noordin (2016) deliberated on the current ecosystem of halal governance accentuates more on the external factors of market demands and competition rather than the internal factors of governance which involves the business strategy and corporate culture at firm level. Given the Halal industry experiences the unstandardized governance system at each state level, their study also suggested to enhance the efficiency of halal governance certification through the aspects of political, economic and institutional dimension of governance, improve a number of experts and personnel of halal certification and segregate roles into operational and governance functions.

It is realized that there are only few studies have been undertaken to examine and describe the roles of internal management in the halal implementations (Rahim, 2017; Khan, et.al., 2019;

Ahmad, et.al., 2017). Although the company's management is perceived as lack of knowledge and understanding of halal matters which lead to the non-compliance of violation of halal implementation, reliance on the external governance structure could not be a promising factor that food-producing companies could adhere to the Halal standards. The external governance is only functioning to bridge the gap on the lack of implementation of halal compliance at firm level. In fact, Rahim (2017) argued that the roles of internal governance are still at infancy stage and the function of internal halal governance including top management, board of directors, internal halal executive/ committee shall be strengthened and acknowledged in order to ensure the effective implementation of halal compliance at firm level. Rahim (2017) also advocated that internal halal governance system is crucial to minimize the likelihood of non-compliance and assist in the effectiveness of Halal operational system.

Given the above deliberation of limited prior studies and findings, thus it leads to the following hypotheses development:

H1: *There are significant association between the internal governance of top management and overall Halal compliance.*

H2(a): *There are significant association between the internal governance of top management and customer focus dimension of Halal compliance.*

H2(b): *There are significant association between the internal governance of top management and supplier management dimension of Halal compliance.*

H2(c): *There are significant association between the internal governance of top management and halal training dimension of Halal compliance.*

H2(d): *There are significant association between the internal governance of top management and employees' commitment dimension of Halal compliance.*

H2(e): *There are significant association between the internal governance of top management and policy and procedures dimension of Halal compliance.*

## **Research Methodology**

### ***Data Sampling and Data Collection Procedure***

This preliminary study is a quantitative in nature, in which it was carried out at the first stage of data collection involving Halal executives/managers who are responsible with their company's Halal affairs and/or operational managers who are well-versed with operating matters of Halal-certified companies. The sample of companies were Halal-certified companies which are situated in the vicinity of Klang-Valley (Kuala Lumpur and Selangor), as both locations are major cities and constitute the highest number of food-related companies. The data of companies was retrieved from JAKIM, with the list number of companies as of 31 December 2018 in Kuala Lumpur and Selangor was 22 and 82 companies, respectively. There were 50 respondents that have expressed their willingness to respond towards the questionnaire. After collecting the questionnaires from the respective respondent, it has been identified that there were 5 only unusable questionnaires due to some incomplete responses of the questionnaire. Overall, only 45 usable questionnaires that can be utilized in this preliminary study. Furthermore, reliability and normality tests have been tested prior to descriptive and inferential analyses are performed, and both preliminary tests were found satisfy for the subsequent analysis. Since the data of the study is found unevenly distributed at less than 5%, therefore the appropriate of subsequent analysis is the utilization of non-parametric statistic (i.e. Spearman bivariate correlation).

### *Measurement of variables*

In order to meet the objective of the study, the questionnaire was divided into two sections: demographic profiles of the respondent and company and the measurement of independent and dependent variables (i.e. internal governance and halal compliance). The questionnaire employs Four-point Likert scale as it eliminates the neutral level which offers opportunity the respondents to answer neither range of agree nor disagree statement (Dumas and Redish, 1999). As far as the Halal food is concerned, the reason behind the usage of Four-point Likert scale is to encourage the respondents to provide reliable and truth opinion on the real practice or implementation of Halal compliance among the Halal-certified companies. There are two variables constitute in the study; independent variable and dependent variable, which comprises of top management’s commitment (independent variable) and Halal compliance acts as the dependent variable, with several dimensions which underpinning the Halal compliance variable including customer focus, supplier management, halal training, employees’ commitment and policy and procedure of the company.

### **Findings**

**Table 1: Descriptive Analysis of Company’s Profile (n= 45)**

Item	Category	Number	Percentage
<b>No of employees</b>	< 20 employees	10	22.2
	20 – 75 employees	12	26.7
	76 – 100 employees	1	2.2
	101 – 150 employees	4	8.9
	151 – 200 employees	18	40.0
<b>Category of product</b>	Processed food	25	55.6
	Ready-to-eat food	5	11.1
	Confectionery	6	13.3
	Beverage	2	4.4
	Frozen Food	6	13.3
	Supplement-related product	1	2.2
<b>Ownership</b>	Muslim	14	31.1
	Non-Muslim	31	68.9
<b>Company age</b>	1 – 5 years	5	11.1
	6 – 10 years	16	35.6
	> 10 years	24	53.3

Table 1 above depicts the descriptive analysis of company’s profile, in which majority of the respondents were from medium-typed companies which are in the range of not more than 200 employees (40%), while the second highest was among the small size companies with a range of 20-75 employees (26.7%), and the remaining respondents were largely from a small-typed companies. Most of the respondents were from companies which mainly involved in producing processed foods (55.6%), bakery-based food (6%) and frozen food (6%). Majority of the food producers were largely owned by non-Muslim manufacturers. This is consistent with the prior studies which conjectured that business environment is considerably dominated by non-Muslims (or non-Malays) and there is no circumvention in producing food-related products among the different ethnics/religions as long as food production is in compliance with stipulated national authority’s Halal guidelines and requirements. In addition, majority of the companies have been established and are operating in more than a decade in the food industry.

Table 2: Descriptive Analysis of Respondents' Profile

Item	Category	Number	Percentage
<b>Gender</b>	Male	8	17.8
	Female	37	82.2
<b>Age</b>	< 30 years	11	24.4
	31 – 40 years	26	57.8
	41– 50 years	8	17.8
<b>No of years working in current company</b>	1 – 5 years	19	42.2
	6 – 10 years	12	26.7
	>10 years	14	31.1
<b>No of years working in food industry</b>	1 – 5 years	12	26.7
	6 – 10 years	13	28.9
	>10 years	20	44.4

Table 2 above depicts the descriptive analysis of the respondents' profile, as majority of the respondents were female (82.2%) with age between 31-40 years old (57.8%) who are in the midst of developing their working experience in this food industry. Most of them were well-experienced in the food industry as they have been working in the current working place between 1-5 years (42.2%) and have been in the food industry for more than 10 years (44.4%). This implies that have gained a substantial amount of job experience in the field of food industry at few numbers of food companies in the same industry.

Table 3: Response of Independent and Dependent Variables

Main Theme	Item	Strongly Disagree	Disagree	Agree	Strongly Agree	Mean
Top management's commitment	Item 1	1	2	19	23	3.42
	Item 2	-	3	22	20	3.38
	Item 3	-	1	29	15	3.31
	Item 4	-	3	28	14	3.24
	Item 5	-	2	29	14	3.27
Customer Focus (CF)	Item 1	-	-	13	32	3.71
	Item 2	1	1	12	31	3.62
	Item 3	1	-	20	24	3.49
	Item 4	-	-	17	28	3.62
	Item 5	-	-	14	31	3.69
	Item 6	-	-	11	34	3.76
Supplier Management (SM)	Item 1	-	1	16	28	3.6
	Item 2	-	2	23	20	3.4
	Item 3	-	1	23	21	3.44
	Item 4	-	1	24	20	3.42
	Item 5	-	-	24	21	3.47
	Item 6	-	-	18	27	3.60
Halal Training for employees (HT)	Item 1	-	2	27	16	3.31
	Item 2	-	2	33	10	3.31
	Item 3	-	2	32	11	3.18
	Item 4	-	3	29	13	3.29
	Item 5	-	4	29	12	3.20
Employees' commitment (EC)	Item 1	-	-	21	24	3.53
	Item 2	-	-	21	24	3.53
	Item 3	-	2	27	16	3.31
Policy and procedure (P&P)	Item 1	-	-	18	27	3.6
	Item 2	-	-	31	14	3.31
	Item 3	-	-	21	24	3.53
	Item 4	-	-	20	25	3.56
	Item 5	-	-	29	16	3.36

Based on the Table 3 above, majority of the respondents were agreed that their companies are highly emphasized on strengthening customer focus through ascertaining for cleanliness, comply with Halal management system, display Halal logo on products and label of food ingredients. They were also agreed that their companies are aware with the supplier status in order to ensure that their sources of food materials are derived from the Halal-certified suppliers. However, there were only small number of companies which were unable to confirm their supplier’s Halal status. The supplier’s Halal status in an utmost important where the food sources are derived from. In addition, majority of the respondents were agreed that their companies equipped their employees with better Halal knowledge and understanding through attending Halal training and/or workshops. However, there were only small number of companies which did not provide halal training for the employees due to unable to bear for higher training costs. Nonetheless, all the respondents were agreed that their companies complied with Halal standards and their motive and mission of Halal compliance were to exude that they cared for people’s well-beings. Majority of the companies have top management team that delivers their awareness on the Halal matters through the establishment of Halal committee, which aims to ensure that Halal guidelines are in compliance among the firm’s employees and showed their high commitment towards Halal compliance. However, there were still a small number of companies that did not have Halal committee at firm level due to high costs of implementation and perceived that manifestation of Halal commitment is an arduous task.

Inferential Statistic

Table 4: Spearman Correlation Analysis

Variable	Top Mgt’s Commit	CF	SM	EC	HT	P&P
<b>Top management’s commitment</b>	1.00	0.002** (0.587)	0.009** (0.499)	0.008** (0.505)	0.000** (0.680)	0.000** (0.662)
<b>CF</b>	0.002** (0.587)	1.00	0.009** (0.684)	0.003** (0.438)	0.000** (0.644)	0.003** (0.426)
<b>SM</b>	0.009** (0.499)	0.009** (0.684)	1.00	0.000** (0.517)	0.000** (0.757)	0.012* (0.373)
<b>EC</b>	0.008** (0.505)	0.003** (0.438)	0.000** (0.517)	1.00	0.000** (0.685)	0.000** (0.681)
<b>HT</b>	0.000** (0.680)	0.000** (0.644)	0.000** (0.757)	0.000** (0.685)	1.00	0.004** (0.539)
<b>P&amp;P</b>	0.000** (0.662)	0.003** (0.426)	0.012* (0.373)	0.000** (0.681)	0.004** (0.539)	1.00

Note:

\*\* Correlation is significant at the 0.01 level (2-tailed)

Table 4 above depicts the result of non-parametric correlation analysis between the internal governance factor (responsibility of top management) and overall Halal compliance and each dimension of Halal compliance. Since this study only involves an independent variable, hence there is no multicollinearity issue and satisfies the result. From the result, it can be concluded that the top management as an important governance factor have significant and positive association between the overall halal compliance of companies, as well as each respective dimension such as customer focus, supplier management, employee commitment, Halal training and policy and procedures. Therefore, the results showed that all hypotheses of

the study are supported with positive relationship at 5 percent significant level. In other words, these results attempt to imply that top management forms as essential governance factor that could influence the Halal compliance at firm level. This is consistent with the findings of the prior study (i.e. Ahmad, et.al.,2017), however it is contradicted to Khan, et.al. (2019) which failed to find significant relationship between top management and Halal compliance.

### **Discussion and Conclusion**

This preliminary study is undertaken in order to test the reliability and understanding the initial respondents by investigating the level of Halal compliance and to examine whether the top management of SMEs is able to exert influence towards the Halal compliance of the companies. Being the essential governance within the company, the function of top management is far away from acting as an agent in the widely used agency theory in the breadth of governance-related studies who behaves opportunistically towards the firm's board of directors and other stakeholders. From the view of stakeholders, top management is perceived as a crucial steering team to oversee all the food operational activities are under safety control and in compliance with Halal-related standards and guidelines. This is imperative to gain consumers' confidence and trust towards the food products since consuming Halal food is an obligatory act for Muslims. From the findings, it can be concluded that top management team as one of the governance factors plays significant roles in exerting influence towards the Halal compliance and Halal-related process from the upstream to downstream of Halal-supply chain activities. Nonetheless, the existing studies on governance and Halal compliance amongst SMEs are still under-researched and it is suggested that future researches shall be undertaken to scrutiny the functions of other internal governance factors that are essential in promoting the Halal compliance at firm level, either in empirical and qualitative studies .

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