

BOARD COMPOSITION AND DETERRENCE OF FRAUD IN NON-PROFIT ORGANISATIONS

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ABSTRACT

The growing numbers of Non-profit Organizations (NPOs) globally show the importance of NPOs in contributing to the society in terms of its social works. By championing the need of the people through their activities, NPOs enjoy public trust. As NPOs are generally subjected to less stringent requirements, they are more vulnerable to occurrences of fraud. Hence, this study aims to examine board composition as a mechanism to deter fraud in NPOs. This relationship was examined based on content analysis of annual reports of 205 societies registered with Registrar of Society (ROS) for the financial period 2010. Characteristics of board composition examined in this study are board professionalism and board with politically connected. Fraud deterrence are proxied by efficiency ratio, stability ratio and solvency ratio. This study finds that only board with professionalism has a positive significant relationship with fraud deterrence in NPOs. However, fraud deterrence indicators are only significant for insolvency ratios. In summary, this study highlights that an optimum mix of board members matters in reducing occurrence of fraud in NPOs.

INTRODUCTION

Non-profit organizations (NPOs) are generally defined as associations, charities, and other voluntary organizations formed to further cultural, religious or public service objectives (Bottiglieri, Kroleski, & Conway, 2011). Their goals are not focused on profit maximisation (Behn, DeVries & Lin, 2010) but solely for creating social values (Othman, Ali, Omar & Abdul Rahman, 2012). Their main source of revenues are from public donations as well as from other revenue generating activities such as obtaining grants from funders, contracting with government to provide services and charging for services rendered. By championing the need of the people through their activities, NPOs enjoy public trust. However, off late, there were several fraud cases in NPOs which have made headlines in media. As NPOs are generally subjected to less stringent reporting requirements, this has made it difficult to detect fraud in NPOs. Fraud is "theft by deception" (Kranacher, Richard & Wells, 2011) and it is a crime (Bank Negara Malaysia, 2010). Fraud in NPOs are not new (Crumbley, Heitger & Smith, 2009). Even NPOs with high religious values are not spared from committing fraud. For example, the vice-chairman of Kong Hee's City Harvest Church, used up the church fund of SGD18 million to finance his wife's singing career (Bloomberg Businessweek, 2012).

Managing donations and other primary decisions in NPOs are the responsibility of the board members. Studies have showed that board composition is able to deter fraud (Greenlee et al., Hodge & Piccolo, 2011). There are incidences where the fraud occurrence in NPOs are caused by the board members themselves. For example, the Malaysian Paralympic Council writes off RM3.8m in a company that runs by its president and his two sons (The Sun Daily, 2012). A study by Yu and Yu (2007) highlighted that board with political connections makes fraud more difficult to detect. As such, board composition matters in fraud deterrence.

This study aims to examine the relationship between board composition and fraud deterrence in NPOs. The board composition is to include the board size, board members with professional qualifications and board members with political connections. Fraud deterrence are proxied by efficiency ratio, stability ratio and solvency ratio. Previous studies had adopted these ratios analysis in their assessment in determining NPO's fraud vulnerability (Tuckman & Chang, 1991; Greenlee & Trussel, 2000; Hager, 2001; Trussel, 2002; Greenlee & Tuckman, 2007). The results of this study is to provide some useful insights as to the level of fraud in NPOs.

This paper will proceed by outlining the background of NPOs in Malaysia. It will then review the literature on the resource dependence theory, board composition, and fraud deterrence, from which hypotheses will be developed. Finally, this paper will proceed to the empirical stage of variable measurement, sampling, data analysis, discussion of results, limitations and suggestions for future research.

NPOs IN MALAYSIA

In Malaysia, NPOs comprised of organizations that are either charitable organizations or societies. NPOs with revenue of more than RM1 million can be registered as companies limited by guarantee and must be registered with the Companies Commission of Malaysia (CCM) and is held accountable by the Companies Act 1965. For NPOs with revenue less than RM1 million, they must be registered with the Registry of Societies Malaysia (ROS), within the Ministry of Home Affairs, and are held accountable by the societies Act of 1966.

NPOs registered under the Companies Act or Societies Act may apply for tax exemption under the Income Tax 1967. The Inland Revenue Board stipulates two conditions that registered institutions must comply with in order to qualify for tax exemption. These conditions are: (1) it must be established in Malaysia for charitable purposes only and (2) the organization must spend at least 50% (or such percentage as may be determined by the Director General) of its income including donation received in the previous year for the activities which were approved to achieve its objectives for the basis period for a year of assessment. In relation to disclosure and reporting requirements, there is no specific accounting standard for the NPOs. Nevertheless, NPOs are encouraged to comply with the International Financial Reporting Standards issued by International Accounting Standard Board and adopted by the Malaysian Accounting Standard Board or reporting standards applicable for private entities in the preparation and presentation of their financial statements. NPOs registered with ROS are required to submit Form 9 that consists of the statement of receipts and payments of the last financial year, together with a balance sheet showing the financial position of the last financial year to the ROS within sixty days after holding its annual general meeting. Other statements such as cash flow statement, statement of changes in general fund and notes, comprising a summary of significant accounting policies and other exploratory notes are not required by ROS. The overall disclosure and reporting requirements of NPOs in Malaysia reflect a minimum regulatory requirement environment.

LITERATURE REVIEW AND GENERATION OF HYPOTHESES

Resource Dependency Theory, Board Composition and Fraud Deterrence

NPOs are characterized by their dependence on public donations, government funding and fees. According to resource dependence theory (RDT), an organization operating in this environment will survive if they can manage the flow of resources and reduces the uncertainty in their environment (Pfeffer & Salancik, 1978). In addition, RDT contends that boards of directors enable the organisations to minimize dependence on resources or gain resources. Prior empirical studies provide evidence that board of directors is associated with successful resource dependence strategy (example Pfeffer, 1973; and Sanders and Carpenter, 1998). More recent studies suggest that type of directors on the board is associated with different benefits to the organisations. For example, board members from financial institutions are more likely to affect the financing obtained by organisations (Luoma and

Goodstein, 1999) and stakeholder directors are more likely to improve corporate social performance (Johnson and Greening, 1999). Board members that have been appointed provide capability in supplying competitive resources such as additional fund, collaboration with government or other organisations, or by improving the organisations outside image (Callen et al., 2010).

Greenlee et al. (2007) suggested that the board can be a whistle blower for any wrongdoings in the organisation thus able to improve accountability and deter fraud. Findings by Greenlee et al., Hodge & Piccolo (2011) documented significant findings between board effectiveness and financial vulnerability. They found that the organisation is less vulnerable as the board effectively executes their functions. The study by Greenlee et al. (2007) suggested that high quality of the board could improve accountability and lessen fraud. Thus, the finding strengthens the notion that the board has a significant influence in deterring fraud. Hence, these studies highlight that board composition matters in ensuring successful resource strategy. This study focuses on two types of board composition which are board professionalism and board with political connections.

Fraud occurrences in NPOs are regarded as performance assessment in some of NPOs literatures (Tuckman & Chang, 1991; Trussel, 2002; Greenlee et al., 2007; Asley & Faulk, 2010, Ryan & Irvine, 2012; Cordery et al., 2012). Hence, many studies suggests that financial ratios were used in measuring fraud occurrences. For example, Tuckman & Chang (1991) and Ryan & Irvin (2012) used three NPOs financial ratios which were efficiency ratios, stability ratios and solvency ratios to measure fraud occurrences in NPOs.

NPOs are dependent on public donations and government fundings as their main source of revenues. As such, efficiency ratio measures how well NPOs are able to manage their funds efficiently. Previous studies measured efficiency using administrative expenses, program expenses and cost of fundraising (Tuckman & Chang, 1991; Greenlee & Trussel, 2000; Ashley & Faulk, 2010; Ryan & Irvine, 2012). However, due to the unavailability of data, only administrative expenses is chosen in this study. Efficiency is measured using the administrative ratio:

$$\text{Administrative ratio} = \frac{\text{Administrative expenses}}{\text{Total expenses}}$$

Stability ratio are used to measure the ability of NPOs to sustain in the business for a long run. According to Tuckman & Chang (1991), NPOs are more stable when they diversify their income. NPOs which heavily rely on only one particular income might jeopardize the income and investment. Thus, revenue diversification is crucial and able to improve financial stability and deter fraud. The stability ratio is computed as follows:

$$RCI = \sum \left(\frac{\text{revenue}_i}{\text{total revenue}} \right)^2$$

Solvency ratios indicates how much assets of NPOs are funded by debt financing. Previous study found that the amount of debt has significant influence on the grant amount (ashley & Faulk, 2010). Therefore, this suggests that the higher the solvency ratio, the more fraud occurrence in NPOs. Therefore, solvency ratio is calculated as:

$$\text{Solvency ratio} = \frac{\text{Total Liabilities}}{\text{Total Assets}}$$

Board Professionalism and Fraud Deterrence

Board professionalism is believed to be part of the board composition that influenced board behavior (Miller-Millesen, 2003). In addition, Kramer (1985) stated that board with their professional status has greater access to control over organisational information. According to Carpenter & Westphal (2001), effective board with the mix of competencies and capabilities adds value to board governance function. Furthermore, boards with professional profile contribute to new ideas, more creative in problem solving, widen in knowledge and specific area (Westphal & Milton, 2000; Hwang & Powell, 2009) and improve innovative performance (Wincent et al., 2010).

Resource dependence theory suggests that a resource richness board and proficient in their respective field would provide better advice, information, and resource to the firms (Hillman & Dalziel, 2003; Pfeffer & Salancik, 1978). Therefore, it is predicted that board professionalism is associated to fraud deterrence.

This study adopted measurement of board professionalism from Bradshaw et. al, (1992) and Hwang & Powell (2009). The study initially analyzed professional background from list of office-bearers and looked for a member who has professional experience or professional education. The following hypotheses are developed:

H1a – There is a significant positive relationship between board professionalism and efficiency ratio.

H1b – There is a significant positive relationship between board professionalism and stability ratio.

H1c – There is a significant positive relationship between board professionalism and solvency ratio.

Politically Connected Board and Fraud Deterrence

In previous studies, it is found that politically connected board has the ability to influence the external environment and benefits the organisation through improving fundraising activities, networking with government or other related parties and organisation's outside images (Young et al., 2001; Bathula, 2008; Ford, Gresock & Peeper, 2011).

Moreover, Johnson & Mitton (2003) revealed that politically connected firms have greater stability when government imposed capital controls thus increasing the level of subsidies whereas such connection would have an adverse impact on the firm performance during financial economic

downturn. This indicates that there is a significant influence between politically connected board and fraud deterrence.

Previous study by Johnson & Mitton (2003) revealed that Malaysian firms with political connection relationship hardly survive when there is financial shock or crisis and the absence of capital control from government. Another study by Yu and Yu (2007) found that politically connected board are involved in corporate lobbying activities. This is because they are able to directly influence regulators and request for favourable regulation rules. Yu and Yu (2007) mentioned that lobbying is an important tool for fraudulent firms to conceal fraud. As such, politically connected board matters in fraud deterrence.

In this study, board members with political connection are defined if he or she at any time in the past held positions such as Senator, Member of Parliament or has been a Director of an organisation. Besides, any individual possesses a title such as Tun, Dato' Seri, Puan Seri, Datuk or Datin is also under this category. From this, the following hypotheses are developed:-

H2a: There is a significant positive relationship between politically connected board and efficiency ratio.

H2b: There is a significant positive relationship between politically connected board and stability ratio.

H2c: There is a significant positive relationship between politically connected board and solvency ratio.

METHODOLOGY

Sample and data Collection

The sample consists of 205 societies registered with the Registrar of Societies (ROS) for the financial year 2010. The sample consists of randomly selected NPOs situated in Selangor, Wilayah Persekutuan Kuala Lumpur and Terengganu. These NPOs are selected because they are amongst the largest and active NPOS in Malaysia. The research approach involves content analysis of societies' annual reports. Content analysis has been widely employed in prior studies to measure voluntary and mandatory disclosures in annual reports (example Hackston & Milne, 1996; O'Donovan, 2002; Clemens & Douglas et al., 2006)

Measurement of Fraud

Fraud in NPOs is measured by separating them into upper and bottom quintile with respect to the four indicators of fraud vulnerability (Tuckman & Chang, 1991). Table 1 highlights the four indicators of fraud vulnerability which are inadequate equity balance, revenue concentration, low administrative costs and low operating margin.

Table 1: Indicators of Potential Fraud Vulnerability

Indicator	Definition	Direction
Admin	Ratio of administrative expenses to total expenses	Lower ratio indicates potential fraud vulnerability
Revenue Concentration	Sum of square of: share of income from fees, share of income from contribution and share of income from other income	Higher concentration indicates potential fraud vulnerability
Debt	Ratio of total debts to total assets	Higher ratio indicates potential fraud vulnerability
Margin	Total income minus total expenditure, as a share of total income	Lower margin indicates potential fraud vulnerability

Quintile analysis in SPSS is employed to determine the bottom quintile of the four indicators as highlighted in Table 1. This is consistent with a study by Tuckman & Chang (1991) where they used quintile analysis in determining the extent of fraud vulnerability in NPOs. In this study, the quintile analysis is used on the sample to identify the fraud vulnerable NPOs.

Next, the fraud vulnerable NPOs are further classified into three levels; low risk, medium risk and high risk. This is to develop a financial profile of fraud vulnerable NPOs. The risk indicators can be an approach for regulatory authorities to determine which NPOs are low-risk, and which are high-risk. Thus, NPOs with higher risk should be closely monitored (APG Typologies Report, 2011). The classifications of risk are highlighted in Table 2.

Table 2: The Classifications of risk in NPOs

Fraud Indicators	Levels of Fraud Risk
One indicator in bottom quintile	Low
Two indicators in bottom quintile	Medium
Three and/or four indicators in bottom quintile	High

Table 2 highlighted that NPOs are labeled as low risk when they fall in the bottom quintile with respect to one indicator. If NPOs fall in the bottom quintile with respect to two indicators, there are labeled as medium risk. Lastly, the most vulnerable NPOs are identified when they fall in the bottom quintile with respect to all indicators.

Measurement of Variables

There are two independent variables in this study, board members with professional affiliations and board members with political connections. In addition to the identified independent variables, this study also includes organization size identified in prior research as a determinant of fraud deterrence

(e.g. Saeedi & Mahmoodi, 2011) as control variable. The definition and measurement of variables used in this study are listed in Table 3.

Table 3: Definition and Measurement of Variables

Variable Acroynm	Definition	Measurement
1) BOD_PROF	Board professional	Percentage of professional board to total number of board members
2) POL_CONN	Politically connected board	Percentage of politically connected board to total number of board members
1) SIZE	Organisational size	Total Assets

ANALYSIS AND RESULTS

Descriptive Statistics

As highlighted in **Table 1**, Tuckman & Chang (1991) mentioned that there are four indicators of fraud vulnerability in NPOs; which are (1) low administrative expenses, (2) less diversified revenues (3) high debt ratio negative and operating margin.

Quintile analysis is employed to determine the levels of quintile of four indicators. The results of the quintile analysis indicates that 145 NPOs (71 per cent) out of 205 NPOs are in the bottom quintile and therefore, they are judged as fraud vulnerable NPOs in this study. From the 145 NPOs identified to be fraud vulnerable, they were further categorised in accordance to the level of fraud as highlighted in **Table 4**.

Table 4: Categories of Fraud in NPOs

N=145 NPOs	Low risk	Medium Risk	High Risk
Fraud Vulnerable NPOs	92	46	7

Table 4 reported that from the 145 fraud vulnerable NPOs, 63 per cent of them are identified to be at "low risk". This means that 92 NPOs had one source of potential fraud vulnerability like low administrative expenses, one kind of revenue, negative operating margin or high debt ratio in 2010. In addition, table 4 shows the number of "low risk" NPOs is substantially greater than the number of "high risk" NPOs. On the other hand, 7 NPOs out of 145 NPOs are the most fraud vulnerable NPOs in this study. This indicates that they are less likely to avoid program cutback during financial shock.

Table 5: Descriptive Statistics for Independent and Control Variables

	N	Range	Minimum	Maximum	Mean	Std. Deviation
BOD_PRO (%)	205	1.00	0.00	1.00	0.12	0.21
POL_CONN (%)	205	1.00	0.00	1.00	0.11	0.22
SIZE (RM'000)	205	17,904.92	0.00	17,904.92	560.42	1,956.66

Table 5 reported that some NPOs have 100% board members with professional affiliations while others have 100% board members with political connections. It is also reported that some of the size in NPOs are very small with zero total assets to a fairly large size of a maximum total assets of RM17.905 million.

Table 6: Descriptive Statistics for Financial Ratios fraud in NPOs

	N	Range	Minimum	Maximum	Mean	Std. Deviation
EFFICIENCY (%)	205	1	0	1	0.66	0.36
STABILITY	205	0.70	0.3	1	0.79	0.20
SOLVENCY (%)	205	9.22	0	9.22	0.18	0.76

Table 6 reported that the efficiency ratio of NPOs vary from zero per cent to 100 per cent with a mean ratio of 66 per cent. This implies that NPOs use more than 66 per cent to pay for administrative expenses. The remaining balance is used to pay for program expenses and fundraising expenses. However, prior research suggested that NPOs should spend at least 60 per cent or more out of total organisation expenses on program activities (Harvey & McCrohan, 1988; AIP, 2010). The mean score of stability ratio was 0.79 and stability ratio ranged from a minimum of 0.30 to a maximum of 1. This finding suggested that on average, NPOs in Malaysia are highly dependent on few sources of revenue and thus they are more vulnerable to the financial instability (Ashley & Faulk, 2010). The result on solvency ratio shows that the mean ratio was 18 with minimum and maximum values of the ratio were zero per cent and 92 per cent respectively. Therefore, the mean value indicated that on average, 18% of the total assets of NPOs are funded by debts.

Multivariate Analysis

Multivariate Analysis is carried out to test the hypotheses in this study using normal scores data for both dependent and independent variables.

In this study, linear multiple regression is used as the basis of analysis for testing H1 to H3. The hypothesized relationships are modeled as follows:

Model 1

$$\text{EFFICIENCY} = \beta_0 + \beta_1 \text{BOD_PROF} + \beta_2 \text{POL_CONN} + \text{SIZE} + \varepsilon$$

Model 2

$$\text{STABILITY} = \beta_0 + \beta_1 \text{BOD_PROF} + \beta_2 \text{POL_CONN} + \text{SIZE} + \varepsilon$$

Model 3

$$\text{SOLVENCY} = \beta_0 + \beta_1 \text{BOD_PROF} + \beta_2 \text{POL_CONN} + \text{SIZE} + \varepsilon$$

In the above regression models, multicollinearity was tested using the variance inflation factor and tolerance levels, and found to be well within the satisfactory range. The results of regression analysis are presented in Table 7 and are now discussed in terms of tests of each of the hypotheses.

Dependent Variable	Efficiency			Stability			Solvency		
	R ²	0.055			0.035			0.256	
Adjusted R ²	0.041			0.021			0.245		
F	3.882			2.428			23.025		
Sig	0.010			0.067			0.000		
Model	Beta	T	Sig.	Beta	t	Sig.	Beta	t	Sig.
(constant)		-0.517	0.606		0.285	0.776		1.044	0.298
BOD_PROF	0.035	0.514	0.608	-0.58	-0.842	0.401	0.180	2.974	0.003***
POL_CONN	-0.240	-3.351	0.001***	-0.014	-0.195	0.845	-0.150	-2.368	0.019***
SIZE	0.040	0.552	0.580	-0.173	-2.395	0.018***	0.495	7.782	0.000***

Table 7: Multiple Regression Results For Factors Affecting Fraud in NPOs

Coefficient for each variable is shown with t values in parentheses. *Significant at 10 per cent level (1-tailed test); **Significant at 5 per cent level (1-tailed test); ***Significant at 1 per cent level (1-tailed test)

The results of the multiple regression analysis in Table 7 reported that the adjusted R² is 4.1 per cent, 2.1 per cent and 24.5 per cent respectively. Adjusted R² indicates the strength of the relationship between independent and dependent variables. These results reveals that solvency ratio obtained the highest Adjusted R² of 24.5 per cent. This could be explained by the diversity of board of directors. Although the other two variables have low adjusted R², the significant p value of all variables shown > 0.05 expect for stability ratio. The F values for efficiency, stability and solvency are 3.882, 2.428 and 23.025 respectively.

H1a predicts that board with professionalism is significantly positively related to efficiency ratio. The results showed that professional board and NPOs efficiency is positively correlated ($\beta=0.035$). Prior study also revealed corporate board member with higher educational level positively impact the firm's value (Kim & Lee, 2010) and improve directors' cognitive and decision making (Wincent et al., 2010). Nevertheless, the finding shows that there is no significant positive relationship between board professionalism and NPOs efficiency since the significant p-value is 0.608 which is higher than 10 per cent level. Following the similar finding by Rose (2007), this study rejects hypothesis H1a. One possible reason is that managing non-profit organisation does not require any board specific professional background. What they should have is the dignity and sincerity in doing their voluntary work.

With regards to board professionalism with stability ratio, the result showed that there is a negative relationship between professional and NPOs stability ($\beta = -0.58$). The p-value of 0.401 indicates that there is no significant existence of relationship between professional board and NPOs stability. In other words, professional board in NPOs does not add value to revenue diversification. However, Ingley & Walt (2001) suggested that qualified and professional board members are crucial as they can provide links to different external resources. The inconsistent result between actual and expected finding leads the study to reject the hypothesis H1b.

The analysis also showed that there is a positive relationship between professional board and NPOs solvency ($\beta = 0.180$). The regression result shows that the p-value is 0.003 is less than 1 per cent level. This indicates that the professional board has significant influence in NPOs solvency. However, this finding is not accepted by Jeanjean & Stolowy (2009) because they found that board with professional profile negatively associated with firm's leverage. Therefore, this study concludes to accept the hypothesis H1c.

On the other hand, H2 predicts that politically connected board is significantly positively related to efficiency ratio, stability ratio and solvency ratio. The multiple regressions demonstrated that there is a negative relationship between political board and efficiency ratio ($\beta = -0.240$). The result further reveals a negative significant relationship between politically connected board and NPOs efficiency (p-value = 0.001). This explains that politically connected board significantly reduced efficiency and fraud deterrence. None of the NPOs members with political stand would help in improving and granting a better performance. Contrary result was found by Goldman et al. (2009). They discovered that the stock market revealed positive abnormal stock return just after the announcement of the nomination of a politically connected individual to the board.

As with efficiency ratio, politically connected board also did not have any significant relationship with stability ratio (p-value = 0.845; $\beta = -0.014$). As such, this infers that board which has political connections are unable to assist in NPOs' stability and as such they are unable to deter fraud. This is consistent with a study done by Johnson and Mitton (2003), where they found that Malaysian firms with political connection relationship hardly survive in the event of any financial crisis because the firms have limited access for financial support.

As for the solvency ratio, the results revealed negative relationship between politically connected board and NPOs solvency ($\beta = -0.150$). This relationship is significant at 10 per cent level since its p-value is equal to 0.019 per cent. However, this study rejects H2c since politically connected board does not contribute to a better leverage in NPOs. Previous study revealed that firm leverage is positively related to politically connected board (Chen et al., 2004). Furthermore, the result is not consistent with Fraser et al. (2006), Agrawal & Knoeber (2001), and Faccio (2002) which suggested politically connected board has the ability to provide higher leverage to the organisation.

CONCLUSIONS AND LIMITATIONS

This study examines the relationship between board composition and fraud deterrence in NPOs. Studies done by Greenlee et al., Hodge & Piccolo (2011) showed that board composition is able to deter fraud. This study uses two characteristics of board composition namely board professionalism and politically connected board. Meanwhile, fraud deterrence is proxied by efficiency, stability and solvency positions of NPOs. Previous studies also highlighted that NPOs with high efficiency ratio, high stability ratio, and low solvency ratio proved to have well diversified revenues and therefore fraud deterrence (Tuckman & Chang, 1991).

From the result, from the total sample of 205 NPOs, 146 NPOs are found to be fraud vulnerable NPOs. 7 NPOs out of 145 fraud vulnerable NPOs are at "high risk" of fraud vulnerability. These NPOs are deemed to the lowest administrative costs, negative margin or deficit in the net operating income, the highest revenue concentration index and debt ratios as compared to the other two categories of financially vulnerable NPOs.

This study is to examine the relationship between board professionalism and fraud deterrence. The analysis revealed that board professionalism has a positive significant relationship with NPOs solvency. It means that board member with professional background reduced the insolvency risk and improved fraud deterrence and fraud deterrence indicators are only significant for insolvency ratios. The possible explanation is that board professionalism would have better financial decision making especially board with accounting and finance expertise. Several studies supported this findings where boards with professional profile contribute to new ideas, more creative in problem solving, widen in knowledge and specific area (Westphal & Milton, 2000; Hwang & Powell, 2009) and positively impacts innovative performance (Wincent et al., 2010). The efficiency and solvency of NPOs were not significantly influenced by the proportion of board professionalism in non-profit board.

On the other hand, politically connected board affects NPOs efficiency in inverse relationship. This means that the board with political connection significantly reduces efficiency and performance of NPOs. In fact, the appointment of individual with political connection are not able to deter fraud. This is consistent with prior studies by Chen et al. (2004) and Yu and Yu (2007) where they found politically connected CEOs were ineffective in enhancing firm efficiency and additionally, they make fraud difficult to be detected.

Furthermore, Johnson & Mitton (2003) found that firms with political connection faced financial difficulties during economic crisis due to their inefficiencies and the government did not bail out these favored firms. Indeed, these boards show low degrees of professionalism since fewer directors with relevant professional background or prior business experience were being appointed (Chen et al.).

Finally, there are some limitations in this study. Firstly, this study relies extensively on the annual reports provided by ROS. Future reasearch may consider the use of questionnaires sent to

board members or members of the NPOs in gauging the items considered as fraud deterrence. Secondly, the result of this findings only focuses on the three types of financial ratios to measure NPOs fraud vulnerability. Finally, this study focuses only on two types of board members. Future research may also consider the use of questionnaires or interviews with the broader types of board members in gauging their influence on fraud deterrence. Despite these limitations, this study provides useful insights in understanding the relationships between various board compositions and fraud deterrence in NPOs in a developing country environment.

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