

ISLAMIC FUND & WEALTH MANAGEMENT

A way forward

This publication is very timely, as it not only broadly contributes to IiBF's university flagship initiative on Islamic social finance, but it also specifically provides updated information on fund and wealth management with regard to current policies and practices. Empirical findings, case studies discussions, seminal as well as recent related literature are gathered in this book to cater for everyone inside or outside the fund and wealth management industry. With *Shari'ah* as the governing principles, the fund and wealth management industry has remarkably flourished throughout the years. Parallel with the consistent and coherent growth, this book offers insights and in depth investigations covering different aspects that may influence the continuous prosperity of this industry and caters for all players in the field.

Areas such as unit trusts, asset management, *Takaful* as well as pension funds together with several innovative products and wealth distribution mechanisms are put forth and discussed like *Waqf*, an endowment fund that combines investment performance with social distribution opportunities for the benefit of the society or *ummah* as well as technological fund-raising mechanisms such as crowd funding, aim at mitigating problems pertaining to access to financing for those entrepreneurs in need of capital.

All the key components of Islamic fund and wealth management are discussed in this book, thus it is a must read for those involved in this area, especially those responsible for developing policies and practices, in order to carefully engineer more competitive and innovative products and mechanisms based on the findings and outcomes of these studies. Anyone who regards fund and wealth management as crucial knowledge for a more sustainable wealth-managed future should also read this book, including those who also seek productive retirement and pension funds, which follow *Shari'ah* principles.

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Chapter 20

Debt Management Program for Banking and Islamic Banking Facilities in Malaysia: From the *Sharī'ah* and Legal Perspective

Syarah Syahira Mohd Yusoff, Tuan Badrul Hisyam Tuan Soh and Rusni Hasan

Abstract

This chapter aims to provide a conceptual analysis of the Debt Management Program (DMP) which is under the purview of *Agensi Kaunseling dan Pengurusan Kredit* (AKPK). The research is based on a qualitative approach adopting the method of contextual analysis based on works of literature concerning DMP in Malaysia. Relevant effort induced by the AKPK will be highlighted in this study to provide an insight on how the DMP program in Malaysia is arranged. Furthermore, this chapter will also look at the *Sharī'ah* and legal issues in DMP to unravel the grey areas which require future focus of researchers. The chapter will provide information on debt from *Sharī'ah* perspective and the issues related to the practicality of the DMP. It will further recognize the need for constructing DMP for Islamic financing. However, the research is not an exhaustive study, as it only focuses on the practice of Islamic financial services in Malaysia. The findings of this study will provide a very useful source of information on the current state of debt management in Malaysia. In addition, it will further offer practical solutions to overcome any shortcoming with the current practice of DMP. This research will provide an avenue for the future research on DMP.

1.0 Introduction

Personal bad-debt is one of the highlighted major issue among the youths in Malaysia. Personal bad debt arises due to personal borrowing that includes personal loans, car loans, home loans and credit cards (Livingstone & Lunt, 1992; Lunt & Livingstone, 1991). As reported by the Malaysian Financial Planning Council that as at September 2015, there are 22,663 Malaysians under the age of 35 being adjudged as bankrupts due to poor management of debt (NST, 2016). According to

AKPK, 70% of the debt problem comes from overwhelming credit card debts (CompareHero, 2016). This situation creates an obligation on the part of the debtor to pay the amount owed to the creditor. The creditors in Malaysia are usually commercial banks which offer the retail products. The ever-increasing cost of living be it in the cities or sub-urban areas forces the consumer to take up either personal loans or any other types of loan. However, if the consumer fails to service or to pay back the loan and/or financing, they will end up with bad-debts. Ultimately, the creditor will take action against the consumer debtor to claim back the money. This will pose a problem not only to the consumer himself but unfortunately will also affect family institutions.

Personal bad-debt is seen as a result of lack of knowledge in financial literacy. Due to this, Bank Negara Malaysia (BNM) in the Financial Sector Blueprint 2011-2020 aims to provide the consumer with adequate financial knowledge to make a better decision for their financial lifestyles. *Agensi Kaunseling Dan Pengurusan Kredit* (AKPK) through the Debt Management Programme (DMP) is one of the BNM's initiative in protecting the consumers' welfare that is complemented by a comprehensive financial literacy programme set to enhance the financial capability of consumers.

The objective of this chapter is twofold. Firstly, the chapter aims to examine the practice of DMP and secondly, to highlight the *Shari'ah* perspective on debts and DMP. This chapter will be divided into five main sections focusing on the introductory part, the structure of DMP, literature review, *Shari'ah* perspective on DMP, and followed by a conclusion.

2.0 Debt Management Programme

The objective of AKPK is to help individuals take control of their financial situation and to gain peace of mind that comes from credit used with wisdom. Other than that, AKPK will also play an important role in educating and assisting consumers to ensure a higher rate of financial literacy amongst Malaysians. There are three main programmes under AKPK namely the Financial Education programme, Financial Counselling Programme and Debt Management Programme (DMP). For the purpose of this Chapter, the discussion will only cover the aspect of DMP by highlighting how DMP operates in Malaysia.

DMP is a personalised debt repayment plan for individual customers. DMP is supposed to be seen as a mechanism for the financial consumers in managing their debt that relates directly to their wealth and sustenance. The programme is conducted on a voluntary basis, meaning the consumer debtor will have to enrol and register with AKPK before the programme can begin. As at 30 November 2016, AKPK has successfully assisted 11,935 consumers to settle their debts amounting to RM488 million (Borneo Post, 2017). AKPK will assist customers with debts and re-arranged the payment method/table with all the financial institutions that are involved. The services provided by AKPK are free of charge. Under this programme, AKPK will help both the customers and the financial institutions to restructure the customer's debts. Under this programme, financial institutions that are required to work with AKPK comprise of all commercial banks including conventional and Islamic banks, all insurance companies, takaful operators, development financial institutions, credit card issuers, selected cooperatives, Malaysia Building Society Berhad and Perbadanan Tabung Pendidikan Tinggi Nasional (Bank Negara Malaysia, 2006).

All the customer's financial obligations with the financial institutions will be consolidated together and the AKPK will suggest an amount as minimum as RM50.00 per month subject to the agreement of both the customers and the financial institutions involved. Generally, the types of debt that are eligible under DMP are unsecured loans such as credit cards, personal loans and unsecured overdrafts. On the other hand, secured debt financing such as car and housing financing will be restructured on a case to case basis with additional requirements (AKPK, 2017). The maximum repayment period under DMP is 10 years inclusive of the proposed interest rate. Should the parties agree with the terms suggested by the AKPK, the debtor will then pay the monthly instalments through AKPK or directly to the financial institutions (AIBIM, 2017). For an individual to enrol into the programme, a person must fulfil certain conditions such as he/she must not be a bankrupt, not being in any stage of bankruptcy proceeding or any litigation proceeding, must have a sufficient net disposable income after meeting one's expenses and the total debt size must not exceed RM2 million. Consequently, it should be noted that once a consumer is enrolled into the programme, his/her name will appear in the Central Credit Reference Information System (CCRIS). It is a computerized database system that stores information reported to the Credit Bureau of the Bank Negara Malaysia about the borrowers in Malaysia. Hence, depriving his/her rights from any future financing or loan with any financial institutions.

The above highlights the practice of DMP in Malaysia. It is proven that DMP is indeed a successful programme as it assists debtors with their financial burden. The following section then will discuss existing literature on DMP to discover any gap and issues pertaining to the DMP.

3.0 Literature Review

This section unravels the academic literature concerning the DMP service. It is noted that very few Malaysian academicians have focused on this aspect other than literature produced by BNM and the AKPK themselves. DMP in Malaysia is a financial program under the AKPK who gets its mandate from BNM. The program will assist the consumers to settle the debts owed to the financial institutions or the banks. Unlike in Malaysia that only relies on AKPK, the United States has her own private and national DMP providers. According to Brown et al. (2012) there are more than 900 agencies that provide credit counselling services which include DMP.

Maswati et al. (2015) asserted that most people face with indebtedness issue due to lack of financial knowledge and the inability to manage the debt. Poor financial planning, failure in business, retrenchment from job, and health problems are also among the factors that lead to the consumers' failure in repaying the debt (Brown et al., 2012; Neill, Prawitz, Sorhaindo, Kim, & Garman, 2006; Xiao & Wu, 2008). DMP then seems to be a promising way out rather than being declared as a bankrupt (Bank Negara Malaysia, 2010; Brown et al., 2012; Dellande, Gilly, & Graham, 2016; Zakaria, 2014).

Brown, Link, and Staten (2012) describe Debt Management Plans as a voluntary repayment plan which is seen as an alternative to bankruptcy. On the other hand, debt management service is also considered as a tool in paying the debt to the creditor because the facilitator or the counsellor will help the debtor in negotiating the repayment structure (Dellande et al., 2016). Xiao and Wu (2008) further claimed that DMP will certainly benefit the consumers as well as the creditors. This is particularly true as the consumers may avoid the harassment from the debt collection agencies, legal action and at the same time enjoy a relatively low interest and a lesser amount of monthly commitment (Zakaria, 2017).

Even though the DMP seems to be a promising way out from the legal action, it was argued that such plans or programmes might not be successful without the consumer's positive attitude and commitment

towards the program (Ahmad & Omar, 2013; Brown et al., 2012; Dellande et al., 2016; Xiao & Wu, 2008). This view was supported by Zakaria (2017) who stated that the failing rate in AKPK for DMP program was mostly due to the consumers who are not disciplined and not serious in paying off their debts.

From the above literature, it is found that, all the debts will be put under one account by the counselling agency. This gives rise to the issue of mixed of funds should the financing also come from the Islamic financial institutions. The following section then will highlight whether there is any *Sharī'ah* issue with mixture of funds out of the DMPs.

4.0 Debt from Islamic Perspective

4.1 Debt in Islam

Debt, or commonly referred to as *Dāyn* in its technical terminology, refers to any liability that must be performed by a person whether it is related to property or non-property (Hassan and Haron, 2016). However, for this discussion, the term will be confined to the property-related liability only. Ibn Humam (died 1457), a renowned scholar from the Hanafi school of law defines *Dāyn* as the term used to denote any liability established upon a person to compensate for any property of others that he has destroyed, or loan that he has borrowed, or payment that arises from a sale contract or from a usufruct that he has derived benefit from (for instance, a payment of dowry in marriage contract or rental in leasing contract) (Hassan and Haron, 2016).

It is acknowledged that some might have a skeptical view on debt and regard the same as discouraged in Islam and therefore must be avoided as best as one could. To a certain extent, some might take a simplistic approach by equating a loan arrangement (or even a debt-based transaction) to *RibÉ* or at least a mean which would necessarily lead to *RibÉ*. This notion arises due to the lack of understanding on how *RibÉ* could (or could not) occur from loan. Also, a non-comprehensive understanding of Islamic legal texts could as well lead one to conclude that *Sharī'ah* is against the idea of loan and the indebtedness it carries. It is undeniable that some texts seem to imply such position at first glance. For instance, it is reported by al-Bukhari (died 870 CE) that Prophet Muhammad (P.B.U.H.) had taught a supplication seeking for protection from several things; anxiety and sorrow (*al-ḥam wa al-Hazn*), weakness and laziness (*al-Ajz wa al-Kasl*), cowardliness and stinginess (*al-Jubn*

wa al-Bukhl), and the burden of debt and being over powered by men (*Ghalabah ad-DEyn wa Qahr al-Rijal*) (Al-Bukhari, 2017: Ḥadīth No. 2720). It is also told by the Prophet Muhammad (P.B.U.H.) that there was a martyr, regardless of his high position in the eyes of Allēh for his sacrifices for Islam, shall be forgiven for all his sins except the failure to pay his loan (Muslim, 2017: Ḥadīth No. 1886). These prophetic sayings and the like may give the impression that debt is something bad which will lead the person in question to severe consequences should he fail to honour his commitment in settling the debt unless he managed to obtain a waiver from doing such, as the case may be.

However, a more extensive reading and analysis will suggest a different understanding. Not only there is no single verse in the Qur‘ān (the premier source of *Sharī‘ah*), could be understood as prohibiting or even condemning the involvement in a loan/debt arrangement as the giver or the taker or the witness. In fact, the longest verse in the Qur‘ān is the one which addresses the issue of debt and its management (Al- Qur‘ān, 2017, 2: 282). The verse prescribed in a detail manner how debt should be managed since the day it is created between the creditor and the debtor. This includes the way it should be recorded, validated and settled when it is due. In addition, it is no doubt the practice of loan giving/taking existed in the days of the Prophet (P.B.U.H.) and continues until the present day with no dispute among the scholars on its permissibility thus constituting a consensus agreement (*Ijmā‘*). Hence, it can be said that to portray the loan/debt as a totally ‘bad thing’ is inaccurate and rather an exaggerated statement. In this case, it can be said that the loan/debt is actually neutral in nature. Rather, the goodness or badness of debt lies – inter alia – within the conduct and practice in managing such obligation. In addition, since debt is undeniably among the necessities of daily life for certain group of people, it is illogical to undermine its practice under the pretext of *Sharī‘ah*. Should it be conducted and managed properly (in line with the requirements of *Sharī‘ah*), it will definitely serve the interest (*maṣlahah*) of human life, something that *Sharī‘ah* aspires to champion and uphold.

Looking from another perspective, *Sharī‘ah* does give emphasis on the issue of honouring the debt payment obligation. It is a clear instruction to the believer to stick to what has been agreed between parties through a concluded contract. In this respect, Allēh said: “O you who believed, fulfil your contract” (Al-Qur‘ān, 2017, 5:1). This verse certainly covers all sorts of legitimate contracts including the contract of loan. Prophet Muhammad (P.B.U.H.) also described the one who settled his debt in the

best manner possible as the best person among the believers (Al-Bukhari, 2017: Ḥadīth No. 2393). Such praise certainly can be construed as an encouragement for those who have debt to settle out his commitment as such action carries indubitable importance. In addition, there is a legal maxim in Islamic commercial law, which states that 'الأصل في العقود الجواز' والصحة' (The principal ruling regarding contracts is permissible and valid) (Ibn Taimiyah, n.d.). A permissible and valid contract certainly will cause the involved party to be entitled to certain rights and also to assume certain liabilities and responsibilities.

4.2 DMP from Islamic Perspective

Taking all the above-mentioned facts into account, it can be safely claimed that the obligation of honouring a financial obligation does not only relate to mundane world affairs but is also a part of the fulfilment of religious deeds for the sake of the hereafter. As such, the initiative like DMP, which is meant to facilitate and ease the fulfilment of this obligation must be duly commended since it carries the same level of importance as the obligation itself as mentioned by the maxim 'الوسائل لها حكم المقاصد' (means take the status of goals) (At-Tuufi, 1998). The maxim rules that should an obligation (*Wajibāt*) cannot be completed except through certain mean, such mean will be carrying the similar level of weightage as the obligation and regarded as obligatory as well (when in its original sense, it might not). For instance, originally, the ablution (*WĒdhu*) is only recommendatory. However, since the five times daily prayer will not be valid except if the doer, inter alia, maintains the ablution throughout the prayer, then the ablution, in this context, is considered obligatory as well. Similarly, as settling the debt is an obligation when it is due, any mean that can be invoked to facilitate such settlement can be considered as obligatory. Here lies the significance of DMP.

Notwithstanding the noble intention, the reality that the programme needs to face during its operation may attract some concerns especially from the *Shari'ah* perspective. The first issue to be highlighted here is regarding to the nature of debt that DMP would be dealing with particularly in the Malaysian context. Generally, a distressed customer that requires help from DMP may have debt arising from the following:

- 1) Conventional debt arising from the interest-bearing financing facility which is obtained from the conventional financial institution;

- 2) *Shari'ah* compliant debt arising from the financing facility which is obtained from the Islamic financial institution; or
- 3) A mixture of various facilities as per (1) and (2).

DMP would effectively analyze the customer's present cash flow, consolidate all the debts (as the case may be) and renegotiate a new payment structure with the financial institution (s). From the financial institution's angle, the negotiation of the debt could lead to either renegotiating the cash flow under the facilities which may result in lower but within the original or extended payment terms or refinancing the debt with new terms and/ tenure.

When it comes to debts from conventional loans/means, the process is quite straight forward as new payment terms could be agreed and the relevant interest could just be applied. However, the case would be different for debt from Islamic facility (where various structures like *Murabahah*, *Istisnā* and others can be its underlying contract) as it would require a series of different contract or underlying transaction in order to effect or create new obligations.

For instance, in a sale-based contract like *Murabahah*, normally it would have a fixed total obligation (ceiling) which is contracted upfront. Mechanisms such as *Ibrā'*, *Ta'widh* etc. are also built into a contract in order to address competitiveness as well as commercial consideration. Herein lies the complication. Due to the fixed obligation nature of the selling price as well as granting of *Ibrā'*, the remaining sales price may not be able to accommodate the revised terms under the DMP. This will certainly put the arrangement at the risk of *Shari'ah* non-compliance. It is also worth to mention here that in some cases, restructuring the payment of debt occurring from sales-based contract such as *Istisnā'* also may not be possible without refinancing the contract with other types of *Shari'ah* compliant contract due to the nature of its underlying asset.

The second concern is regarding the circumstance where conventional debt is also involved. It is noted that if a person enrolled himself to the DMP, all his debts from conventional banks and Islamic banks will be consolidated and treated as one. Here, the first question that arises is how would the DMP treat a conventional debt differently from conventional financial institutions? If the DMP renegotiates new payment terms without changing the underlying loan which is *Ribā* based, then the issue of *Ribā* would still be prevalent. On the other hand, if the DMP would undertake a refinancing exercise by adopting a *Shari'ah*

compliant contract such as *Tawarruq* (this is with the assumption that the conventional financial institution would be able to offer this option), then a possible *Sharī'ah* issue would be on the permissibility of using the proceed to ultimately pay both the principal and interest in which is an element of *Ribā* that is generally prohibited.

On top of that, the third concern is regarding to the act of creating new indebtedness (by entering a new contract) with the intention to settle out the existing indebtedness (that arises from the old contract), commonly known nowadays as '*Qalb ad-Dāyn*'. This refers to the execution of a new debt-based transaction in order to pay back an existing debt obligation by creating a new one (Hasan et al., 2016). In general, the process will involve the debtor, who has an existing debt obligation in his account, entering into a new contract with the same creditor which will create a new debt obligation, typically at an amount that is higher than that of the old obligation. As the result, the existing obligation will be absolved and the new debt with a higher amount will replace the existing one (Hasan et al., 2016). Since this arrangement will normally involve a new tenure (longer than the old tenure), its permissibility might be contested as a stratagem to *Ribā* through which the tenure will be extended with the consideration of adjusted total payment although it does not exceed the agreed ceiling price mentioned in the old contract.

Therefore, AKPK must carefully address the highlighted *Sharī'ah* issues to avoid any inconsistencies with the principle of *Sharī'ah*.

5.0 Debt Recovery from the Legal Perspective

From the above section, it is seen that the operationalization of DMP if not construed properly might entail a *Sharī'ah* non-compliance risk. From the legal perspective, debt if not serviced by the customer would entail a legal risk. The financier would most likely lodge a civil action against the customer to claim the unpaid amount. However, in banking practices this situation is considered as recovery process. Banks are likely to execute the recovery action because the customer owes them money and does not make repayments. The reason behind the recovery process is that the bank is actually a financial intermediary between the customers and the depositors. The money given to the customers is actually the depositors' money. Hence, the banks, need to recover the money back from the customers to repay the depositors upon demand. In Malaysia, the debt recovery process, be it a conventional loan or Islamic financing is governed under the Contract Act 1960. For failure

to comply with the contract that has been agreed upon, the creditor can enforce the judgment of the court by invoking bankruptcy proceeding under Bankruptcy (Amendment) Act 2017 if the debts owed exceed RM50,000.00.

Facing with these challenges in reclaiming the bad debt, the banks usually will follow the following practice in recovering the debts. According to one of the banking practitioner (Ijitma' Asas, 2017) in Malaysia, usually there are three stages involved in a recovery process before the bank proceeds with litigation process which are as follows:

- 1) Early care: at this stage, the creditor bank will call the debtor customer or send a letter to give a gentle reminder that the debt is outstanding;
- 2) Rehabilitation: during this stage, the bank will provide a solution by offering a new restructuring or rescheduling exercise to avoid any legal proceeding;
- 3) Recovery: this stage entails a legal proceeding. The bank will liquidate the customer's asset like foreclosing and auctioning (Order 83 of Rules of Court 2012) the asset or by having a Writ of Seizure and Sale (WSS) under Order 45 r1(1)(a) of Rules of Court 2012. If the amount from the foreclosure and WSS is insufficient, the bank (judgment creditor) will further initiate the bankruptcy proceeding against the judgment debtor.

It is then advisable for the customers who have financial problem to discuss their issue with the bank during the early care stage. During this stage, the bank will advise the customers to restructure the monthly payment rather than keeping quiet and face the litigation process later on.

6.0 Conclusion

In conclusion, DMP is a much-welcomed strategy for a Muslim who is indebted to pay back the amount owed as it is a religious obligation to pay back the debt in Islam. DMP is seen as an alternative to the customer-debtor who is struggling to pay their debt obligation to the banks. Nonetheless, it is discovered that DMP only offer financial advice and arrangement to unsecured financing i.e personal loans/financing and credit cards. Thus, for customers who are burdened with secured financing such as car loan/financing and home loan/financing, they are still subject to the normal debt structuring process provided by the bank. It is suggested that, BNM under the DMP programme should extend

the coverage to include the secured financing in their module. Further research should be done to unravel this possibility to assist the banking customers. It should be noted that, this study only provides a conceptual analysis on the *Shari'ah* aspect of DMP. Future empirical research should be conducted to provide a solution to the *Shari'ah* issues discussed above. Additionally, a case study research should also be conducted to verify the reason behind the failure of certain DMP programme.

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