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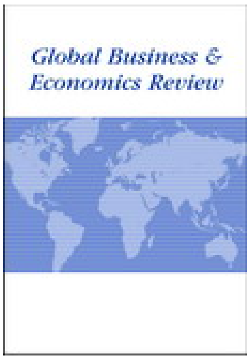

Global Business and Economics Review

ISSN online: 1745-1329 - ISSN print: 1097-4954
https://www.inderscience.com/gber

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DOI: 10.1504/GBER.2023.10050906

Article History:

Received:	22 March 2022
Accepted:	15 August 2022
Published online:	04 December 2023

Debt-based financing: a case study of Malaysian Islamic banks

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Abstract: The present study aims to address the concept of debt-based financing from the Sharīʿah perspective and to analyse the current practice of debt-based financing by the Islamic banks in Malaysia. A qualitative research approach is adopted using an in-depth study of the literature through classical and contemporary books to address the concept of debt-based financing. The practice of debt-based financing in Islamic banking is studied through the Islamic banks' official websites. The present study reveals that the current Islamic banking system offers debt-based financing to the customers where the customers are liable to pay the debt through monthly instalments. However, the concept of *dayn* and the rights and responsibilities of a debtor is not clear to many customers, and the failure of fulfilling the obligation by the customers hinders the smooth operation of the Islamic banks. Moreover, debt-based financing is drawing more attention and interest among most Islamic banks as compared to equity-based financing which is creating more debt.

Keywords: dayn; debt; debt-based contract; creditor; debtor; Islamic bank; Shariah.

Reference to this paper should be made as follows: Muneem, A., Razif, N.F.B.M., Ali, A.K.B. and Rosele, M.I. (2024) 'Debt-based financing: a case study of Malaysian Islamic banks', *Global Business and Economics Review*, Vol. 30, No. 1, pp.39–55.

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1 Introduction

One of the objectives prescribed in the *maqāṣid al-Sharīʿah* (objectives of Sharīʿah) is that wealth should be circulated among the people, and not be exclusive only to the rich. In this regard, a Quranic verse explicitly indicates the need for the circulation of wealth among the people:

> "Whatever (from the possessions of the townspeople) Allah has bestowed on His Messenger belongs to Allah, and to the Messenger, and to his kinsfolk, and to the orphans, and to the needy, and to the wayfarer so that it may not merely circulate between the rich among you. So, accept whatever the Messenger gives you, and refrain from whatever he forbids you. And fear Allah: verily Allah is Most Stern in retribution." (al-Qurʾān, 59:07)

Therefore, Islam allows borrowing and lending money among people depending on their needs and financial difficulties. Several Quranic verses (2:245; 5:12; 57:11; 64:17; 73:20) highly encourage the able to share their wealth and help the disabled, and that they shall be rewarded for such kindness and generosity.

Dayn (debt) is generally a liability of a person towards another, which may incur through many ways such as:

a a loan where a person borrows money and pays it later which is a liability of the borrower

b a sale contract where a customer is liable to pay the price

c a lease contract where the lessee pays the rent which is a liability toward his lessor

d paying compensation is a liability of a person to whom he harms or causes any damage

e zakat is also a *dayn* since it is a liability of a believer toward his Lord to pay it.

Sharīʿah provides some rules and guidelines to protect the rights of the creditors, while at the same time orders the debtors to settle the debt accordingly and timely. However, Islam also encourages the creditor to nicely request what is owing, and to provide ample time should the debtor face difficulties in settling the debt. To the debtors, Sharīʿah urges them to follow the footsteps of the Prophet (PBUH) in kindly and timely settling his debt to one of his companions (al-Nisābūrī, 2015). In this regard, the current Islamic banks offer Sharīʿah-compliant financing for the customers to purchase their essential items under several Sharīʿah concepts. To this end, Islamic banks allow the customers to settle the debt by instalments. However, many customers are not aware of their financing mechanism/structure and the Sharīʿah concept used in their financing; hence, they are also not aware of their obligations and responsibilities as a customer of the financing by Islamic banks (Ahmed and al-Aidaros, 2017; Yusoff et al., 2019). As a consequence, should the customers fail to fulfil their financing obligations towards the banks, the banks' operation as creditors would be disrupted and rendered inefficient, which is harmful and unfair to the banks (Elgari, 2003; Effendi, 2017). Moreover, under certain circumstances, the inability to timely honour the instalments would lead to the rescheduling/restructuring of the financing facilities for the customers, which in turn would extend the payment period and inevitably incur more difficulties to the customers in the long run. This practice is known as *qalb al-dayn* (debt restructuring) (Muneem et al., 2020, 2021).

Therefore, the present study aims to address the concept of *dayn* in Sharīʿah and its practices by the current Islamic banking system and to emphasise the rights and responsibilities of both creditors (Islamic banks) and debtors (customers). This will raise more awareness among the present and potential customers and will assist the banks to offer their financial services more smoothly and efficiently. Moreover, this research focuses on the practice of Islamic banks in Malaysia since there are many Islamic banks are operating in the country and the research only covers vehicle and home financing to have a good picture of the practice.

2 Literature review

2.1 The concept of debt (dayn) in Sharīʿah

The Arabic word *dayn* is used for several meanings such as debt, price, deferred payment, something which is delayed, and also something which is absent. The word *dayn* is an antonym of *'ain* (something which is present or in corporeal/tangible existence) (al-Fayyūmī, 1987; al-Rāzī, 1995; Ibn Manzūr, 1994; ISRA, 2010). Al-Qurʾān (2:282) mentions: "O you who believe! When you contract a debt (*dayn*) for a fixed period, write it down…".

The word *dayn* can either be comprehensive, or specific, in its meanings. The comprehensive meaning of *dayn* covers all kinds of liabilities, either the liability of a person towards Allah or towards other human beings. The liability and obligation of a person towards Allah or other human beings come in many ways, among them, debt, and trade. The comprehensive type of *dayn* is also defined by Ibn Nujaim (2001) as an obligation of rights on someone's liability. Similarly, *Majallah al-Aḥkām al-ʿAdliyyah* explains that debt is something which is obliged on a liability (Ḥaidar, 2003).

The definitions above include all types of liabilities on a person, and he is obliged to pay it either by performing the obligations like *ḥajj* (pilgrimage), *zakāh*, *ṣalāt* (prayer), and *ṣawm* (fasting), or by paying his assets such as the price of goods, rent of a house, or a loan. This type of comprehensive *dayn* is also mentioned in a *ḥadīth*. Ibn ʿAbbās narrated that a lady came to the Prophet (PBUH) and said, "My mother passed away and a month of fasting is due from her". The Prophet (PBUH) replied, "What would you do if there was due (*dayn*) from her? Would you not pay that?" She replied, "Yes (I would certainly pay on her behalf)". The Prophet (PBUH) then said, "Certainly, the debt (*dayn*) of Allah deserves a better payment (than the payment of anyone else)" (al-Nisābūrī, 2015). Similarly, another *ḥadīth* recounts that the Prophet (PBUH) replied to one of his companions when his companion asked about his father who passed away without performing *ḥajj*. The Prophet (PBUH) answered, "What would you do if there was due (*dayn*) from him? Would you not pay that?" He replied, "Yes, (I would certainly pay on his behalf)". The Prophet (PBUH) then said, "Certainly, the debt (*dayn*) of Allah deserves a better payment (than the payment of anyone else)" (al-Nasāʾī, 1999). It is important to note that both *ḥadīths* prove that the Prophet (PBUH) considered *ḥajj* and *ṣawm* as a debt (*dayn*) on a person as these have been on his liability/obligation to perform.

Regarding the specific meaning of *dayn*, the scholars define it in several ways. The specific meaning of *dayn* refers to explicitly the property (*māl*) related liabilities bound by any kind of contract, or usage, or loan, and so on (Ibn ʿĀbidīn, 2003; al-Qarah-dāghī, 2001; Raḥamānī, 2011). Ibn ʿĀbidīn (2003), from Ḥanafī school, defines *dayn* (debt) as something that is obliged in the liability of a person by a contract or consumption or by taking a loan. Ibn al-Humām (2003), another scholar from Ḥanafī school, describes *dayn* as the name of the property which is in the liability of a person, and that can be in exchange of any property that is damaged, or any loan that is taken, or any price of goods that have been sold, or any kind of contracts consisting of benefits like dowry (*mahr*) for a wife, or the rent of any corporeal object.

On the other hand, the scholars from Mālikī, Shāfiʿī, and Ḥambalī schools describe *dayn* in a different way. Ibn al-ʿArabī (2003) and Al-Qurṭūbī (2006) from Mālikī school defined *dayn* as every transaction, where one of the objects is in cash and another one is in liability at a later time. Ibn ʿAbd al-Salām (1991) from Shāfiʿī school described *dayn* as available in the liability without having its recognition. Ibn ʿAqīl from Ḥambalī school mentioned that *dayn* is something which is obliged in liabilities (al-Buhūtī, 2000).

The differences between the definition of Ḥanafī school and the majority schools (Mālikī, Shāfiʿī, Ḥambalī) are: according to the majority scholars, *dayn* can be in exchange for something like the price of goods, compensation of damages, rent, or, the debt can be not in exchange for something like *zakāh* (a person pays *zakāh* without involving in any kind of exchange with the recipient). On the other hand, according to the Ḥanafī school, the debt is a liability which is formulated in exchange for something; therefore, *zakāh* is not a debt as it is not in exchange for anything (Ibn al-Humām, 2003; al-Lāḥim, 2012).

Dayn is also defined by many contemporary scholars like al-Sanhūrī (1997) as an obligation (*iltizām*) of something to exchange with a certain amount of money or the same genre of any fungible items, and that is what makes it relevant to liability. Similarly, *al-Mawsūʿah al-Fiqhiyyah* (WASI, 1989) defined *dayn* as a liability on someone or a function of liability by assets which has been obliged for any of the reasons whether it was because of a contract like a sale contract, guarantee contract, *ṣulḥ* (conciliation), *khulʿah* (divorce by redemption), or subordinate of a contract such as expenses or something else like duress, *zakāh*, or compensation of losses. The word *dayn* is also used metaphorically as an asset that has been obliged in someone's liability. Moreover, AAOIFI (2015, p.117) defined *dayn* as: "any liability that is not in terms of a specified or defined item, whatever the cause of its establishment, i.e., whether its origin is in cash or a commodity, or in a particular described benefit such as the benefit of using particular things or services of persons. For instance, the consideration in deferred sales and loans are described as a debt".

The definition by al-Sanhūrī gives a general idea of the liability which comes through an exchange whereas the *al-Mawsūʿah al-Fiqhiyyah* indicates that the debt occurs with any kind of contract, whether it is a sale contract or other contracts like the expenditure of wife (*nafaqah*) or *zakāh* or the compensation for any losses. The definition by AAOIFI provides an example of the current practice of debt in Islamic banking where the payment is made by a customer in instalments for a financing facility through *tawarruq*, *murābaḥah*, *ijārah*, or any other concept.

A contractual agreement such as a sale contract, lease contract, any kind of compensation for damages (e.g., destroying someone's property/asset, or stealing something), marriage contract [e.g., dowry (*mahr*), *nafaqah* (expenses of wife), *khulʿah* (divorce by redemption)], and *zakāh* are some reasons of liability on a person which he or she has to perform by any means that suits to the matter. Hence, the word *dayn* is used in the present study as the liability and obligation of a person to fulfil as a contracting party of a financial agreement towards the creditor or financier based on the contract that has been agreed upon by both parties.

2.2 The permissibility of dayn (debt) in Sharīʿah

The four main sources of Sharīʿah namely al-Qurʿān, Sunnah, *ijmāʿ* (consensus of scholars), and *qiyās* (analogy) prove that taking debt or offering someone a debt is permissible. The holy al-Qurʾān elaborates the rules of *dayn*, deferred sale, and how to document the contracts in a verse where Allah says, "O you who believe! When you contract a debt for a fixed period, write it down" (al-Qurʾān, 2:282). The verse explicitly shows that dealing with debt is certainly permissible. Still, it encourages the believers to register/record the contracts that they have been involved in so that it may not lead to any kind of conflict amongst them. That is such a holistic command that was revealed to the Prophet (PBUH) a long time ago; whereas in this modern age, there are many systems used to record contracts far safer than any other time in human history. Another Quranic verse states that "…all these shares (of the deceased) are to be given after payment of the bequest he might have made or any debts outstanding against him…" (al-Qurʾān, 4:11). Regarding this verse, Ibn Kathīr (1999) mentions that there is a consensus among scholars that debt must be paid before will (*waṣiyyah*). Al-Ṭabarī (2000) adds that even if the debt covers the total assets of the dead person, the will (*waṣiyyah*) can be distributed within one-third of his assets. Based on their explanations, it is clearly understood that Allah gives priority to the payment of a debt before will (*waṣiyyah*) and inheritance distribution. It also means that debt is allowed in Islam, and the debtor should pay, or his inheritors should pay on behalf of the debtor if he dies before paying the debt.

In a *ḥadīth*, ʿĀʾishah (RA) narrated that: "The Prophet (PBUH) bought some foods from a Jew on deferred payment, and he pledged his armour/shield to him" (al-Bukhārī, 2015; al-Nisābūrī, 2015). This *ḥadīth* indicates that the Prophet (PBUH) bought some foods without paying in cash, which is called debt in the sale contract. It also means that it is allowed to purchase something in deferred payments. Otherwise, the Prophet (PBUH) would have not purchased foods on debt.

The *ijmāʿ* of the scholars confirms that offering someone a debt is considered as charity work, and such act is permissible in Sharīʿah. A person, either rich or poor, may under certain circumstances, be in need of financial assistance. That person then asks someone to lend him some money, goods, or something that he needs; this is normal among the people. The objective of the Sharīʿah for wealth to be circulated among the people is also achieved by lending money/giving debt (Turbān, 2001). Therefore, dealing with debt is allowed in Islam, with a condition that it should not engage with *ribā* (interest) or any other prohibitions.

2.3 The rights and responsibilities of creditors and debtors

Debt is a liability on the debtor, where he is bound to pay sooner or later, and it is the right of the creditor to receive it from the debtor as both parties have agreed upon it. Sharīʿah gives priority to the rights of both the creditors and debtors. The Prophet (PBUH) encouraged debtors to pay back the debt in a good manner in a *ḥadīth* which he said, "the best amongst you is he who pays his debts in the most handsome manner" (al-Bukhārī, 2015). In another *ḥadīth*, the Prophet (PBUH) paid Jābir (RA) more than he owed him for purchasing a camel from Jābir (RA) (al-Nisābūrī, 2015).

At the same time, Sharīʿah also sternly warns off debtors from being behind in payment. In this regard, Abū Hurairah (RA) narrated that the Prophet (PBUH) said, "procrastination (delay) in repaying debts by a wealthy person is an act of injustice" (al-Bukhārī, 2015). The *ḥadīth* describes it as an injustice and unfairness to the creditor where he transferred his asset or money for the benefit of the debtor. Another *ḥadīth* recounts that the Prophet (PBUH) did not even want to lead the funeral prayer for one of his companions who had debt until someone took the responsibility of payment on behalf of the deceased companion (al-Bukhārī, 2015; al-Nisābūrī, 2015). This shows the massive importance of repayment of debt and the rights of a creditor.

The debt is the right of the creditor, which is called *dayn al-ʿibād* (the debt towards human beings), and it will not be forgiven until and unless it is paid back, or the creditor willingly waives from his right on this debt partially or fully. Sharīʿah has full support for the creditor too. Sharīʿah allows the creditor to ask for his debt repayment from a debtor. In this regard, the Prophet (PBUH) said, "Whoever demands his rights, let him do so in a decent manner as much as he can" (al-Ḥākim al-Nisābūrī, 1997). The creditor is also encouraged to give some time for the debtor to pay him back, and not to be hampering him. Allah says in the al-Qurʾān "And if the debtor is in a hard time (has no money), then grant him time till it is easy for him to repay, but if you remit it by way of charity, that is better for you if you did but know" (al-Qurʾān, 2:280).

Sharīʿah allows believers to have debt when it is needed only, and by abiding Sharīʿah rules and conditions of debt. The debtor must pay back his debts, which is a form of kindness and support from the creditor because he allows the debtor to use his money, and this is how it becomes a trust (*amānah*) on the debtor which he must repay. Allah says in the al-Qurʾān "Verily! Allah commands that you should render back the trusts to whom they are due" (al-Qurʾān, 4:58). Sharīʿah provides the rights of asking for payment by the creditor from the debtor while considering the situation of the debtor and his capability of payment without having any Sharīʿah non-compliant benefits, i.e., *ribā*.

2.4 Debt-based contracts in Islamic banking

Based on the method of payment, Sharīʿah contracts can be divided into two:

a sale contracts that require immediate payment, for example, *bayʿ al-salam* (forward sale) and *bayʿ al-ṣarf* (currency exchange sale)

b sale contracts that allow the customer to purchase something immediately, but pay the price of the purchase at a later time, in full or in instalments, as agreed upon between the seller and the buyer, for example, *bayʿ al-murābaḥah* and *bayʿ al-tawarruq* (Ebrahim and Sheikh, 2016).

Also, there is a lease facility that is allowed in Sharīʿah, which is known as *ijārah*. In *ijārah*, the customer is allowed to use the subject matter and to pay the rent over the use of that subject matter within a certain period of time as agreed upon by the contracting parties. The rent that the customer pays to the owner of the subject matter is also considered as debt (AAOIFI, 2015).

Bayʿ al-murābaḥah (cost plus profit sale): The Arabic word *murābaḥah* is derived from the word *ribḥ* which means profit. *Bayʿ al-murābaḥah* "refers to a sale and purchase of an asset where the acquisition cost and the mark-up are disclosed to the purchaser" [BNM, (2013), p.9]. In the current practice of Islamic banks, a client asks a bank to purchase an asset from a third party which the customer will then buy it from the bank. The bank purchases the item and sells it to the customer at a price plus an agreed profit between them, and this practice is known as *al-murābaḥah lil ʾāmir bi al-shirā* (*murābaḥah* to the purchase orderer) (Ayub, 2007; SAC-BNM, 2009; Alkhan, 2020). The payment for the sale can be made either by cash or on a deferred basis (BNM, 2013). There are several products of Islamic banks where *murābaḥah* as used as the Sharīʿah concept for those products (Elgari, 2003; Hegazy, 2007; Suzuki and Uddin, 2016) such as vehicle financing (Omar, n.d.), personal financing (MIB, n.d.a), and cash line financing (KFHM, n.d.a).

Bank Islam Malaysia Berhad adopts *bayʿ al-murābaḥah* for its vehicle financing which is done through several steps as mentioned below:

> "(a) Bank appoints the customer as its purchasing agent to purchase the vehicle from the dealer. Customer irrevocably and unconditionally promises (Wa`d) and undertakes to purchase the vehicle from the Bank.
>
> (b) The customer purchases the vehicle from the dealer on behalf of the bank.
>
> (c) Bank sells the vehicle to the customer on Murabahah basis. Customer pays the selling price to the bank on deferred payment basis.
>
> (d) The customer pledges the vehicle to the Bank as security/collateral" (BIMB, n.d.a).

Bayʿ al-tawarruq (monetisation sale): *Tawarruq* can be translated as monetisation, and cash financing (ISRA, 2010). AAOIFI (2015, p.758) defines *tawarruq* as "monetization which refers to the process of purchasing a commodity for a deferred price determined through *musāwamah* (bargaining) or *murābaḥah* (cost plus profit sale) and selling it to a third party for a spot price to obtain cash". Regardless of the arguments of scholars on the permissibility of a certain type of *tawarruq*, it has been serving various financing products in most of the Islamic banks around the world. According to Mohamad and Ab Rahman (2014), *tawarruq* is also among the contracts used in most Islamic banks in Malaysia. Moreover, Islamic banks in Malaysia adopt *tawarruq* with combining with the *murābaḥah* contract in order to facilitate many financial products and the combination of such practice is known as commodity *murābaḥah* (CM). Normally the process of commodity *murābaḥah* follows the following steps:

1 The customer applies for financing from a bank to acquire a house.

2 Upon receiving the request from the customer, the bank buys a commodity (crude palm oil (CPO) in the case of Malaysia) and obtains the supply of that commodity.

3 The customer buys the commodity from the bank on a deferred payment using murābaḥah contract, where the debt is created.

4 Later the bank sells that commodity on behalf of the customer to a third party (broker) on a cash basis.

5 The third-party (broker) makes the payment immediately and obtains the ownership of CPO.

6 Then the cash amount from the broker is used to purchase the house that the customer applies to buy.

7 Finally, the customer pays the bank in instalment the price of the first sale of CPO using *murābaḥah* which is incurred in step 3 (Muneeza et al., 2020; BIMB, n.d.b; Fa-Yusuf and Ndiaye, 2017; Mohamad and Ab Rahman, 2014).

In the practice of Maybank Islamic Berhad, the commodity *murābaḥah* is used as follows:

> "(a) In accordance to our financing procedure we acquire/purchase a specific Shariah compliant commodity ('commodity') from a third party (commodity trader 1) upon your request equivalent to the facility amount.
>
> (b) We will then sell the said commodity to you at the bank's sale price which comprised of the facility amount plus profit margin ('bank's sale price') to be paid on deferred payment basis within the agreed tenure ('facility tenure').
>
> (c) You appoint us as your agent to perform the commodity sale transaction to a third party for cash. For commodity Murabahah trading purpose, we will at all times act as your agent to undertake the required commodity Murabahah transactions related to the facility.
>
> (d) We act as your agent to sell the commodity to a third party (commodity trader 2) at a price equivalent to the facility amount or limit.
>
> (e) Proceeds of sale of the commodity will be disbursed to you, developers, vendors or your stakeholders subject to the term and conditions of the facility." (MIB, n.d.b)

Al-ijārah (lease contract): *Al-ijārah* is a Sharīʿah concept for leasing contract and it means to rent or lease (Qalʿah-Jī et al., 1988). Technically, *ijārah* is a transfer of an asset for a specified period without transferring the ownership but with only the benefits of that asset and a lessee pays such an amount to a lessor as agreed (al-Shirbīnī, 1997; Al-Dusūqī, n.d.; al-Buhūtī, 1983). The owner of the property and the lessee will be mutually agreed on a specific rental payment for the subject matter of the lease. The amount of the rent may vary according to the agreement between the parties. In the present practice of Islamic banks, there are some products over which *ijārah* is used as an underlying contract. Besides, Islamic banks also allow owning the asset accordingly once the *ijārah* period is over which is called *ijārah muntahiyah bi al-tamlīk* or *al-ijārah thumma al-bayʿ* (AITAB), and this is used to purchase a car, a house, and so on (MIB, n.d.c; KFHM, n.d.b; Alkhan, 2020).

AmBank Islamic Berhad (AmBank Islamic) uses *al-ijarah thumma al- baiʿ* (AITAB) for vehicle financing. According to the practice of the bank, AITAB refers to:

> "two contracts, Ijarah (lease) and Bai` (sale) contracts that are undertaken separately and consequentially. Under the first contract, the customer (as hirer) leases the vehicle from the bank (as owner) at an agreed rental over a specified period. At the end of the lease period, the Hirer will purchase from the owner the vehicle at an agreed price which is equivalent to the last instalment" (AmBank Islamic, n.d.).

3 Methodology

An in-depth qualitative research approach is adopted to achieve the objectives of the present study. Since the study focuses on the concept of debt and its current practice, the literature of the present study is collected through several sources such as classical and contemporary books, journals, conference proceedings, online resources, and resolutions of Islamic financial institutions. Regarding the contemporary practices of debt-based financing in Islamic banks, the data are collected through their official websites, especially the Sharīʿah guidelines, manuals, policy papers, and product disclosure sheets (PDS). The collected data are sorted out based on relevance and importance to the objectives of this study. Based on that, the study highlights the current literature on the subject matter in several significant themes such as the concept of debt, the rights and responsibilities of the debtors and creditors, and the current practice of Islamic banks using a debt-based contract. After data collection and highlighting the current literature, the study uses the inductive approach in order to analyse the data and to obtain the objectives of this research. The inductive approach is applicable and reasonable for this study since it helps the researchers to obtain a general conclusion or significant result through various observations of particular cases that are happening. The approach is also called as 'bottom-up' method (Cropley, 2019). Additionally, the data are also analysed and presented through a descriptive method providing the concept of debt from the Sharīʿah perspective with special reference to the practice of debt-based contracts by Islamic banks.

4 Results and discussion

4.1 The growth of debt-based financing in Islamic banks

Islamic banks offer many types of products to meet the needs and demands of the customers. The nature of those products varies from one to another, and those products are based on Sharīʿah contracts. In the modern practice of Islamic banking, the customer asks for assistance from Islamic banks and shows his/her interest to acquire a certain product e.g., a vehicle or house, to a bank in order to purchase that product by the bank. Once the bank obtains that product, the bank sells it to the customer. Then the customer pays the price in instalments, which is considered debt on the liability of a customer. Therefore, the debt incurs from the sale contract which allows the customer to pay the price within a period of time (instalments). Tables 1 and 2 show that many Islamic banks in Malaysia are using *murābaḥah*, *ijārah*, *tawarruq*, and other supplementary contracts to serve customers for vehicle and home financing. It seems that the margin of financing for those products is also around 90 to 100% based on the products and banks' offers. In other words, a customer is entertaining almost full financing where he will be liable to pay in instalments up to 9 years for vehicle financing and 35 years for home financing.

Table 1 Debt-based Sharīʿah concepts for vehicle financing

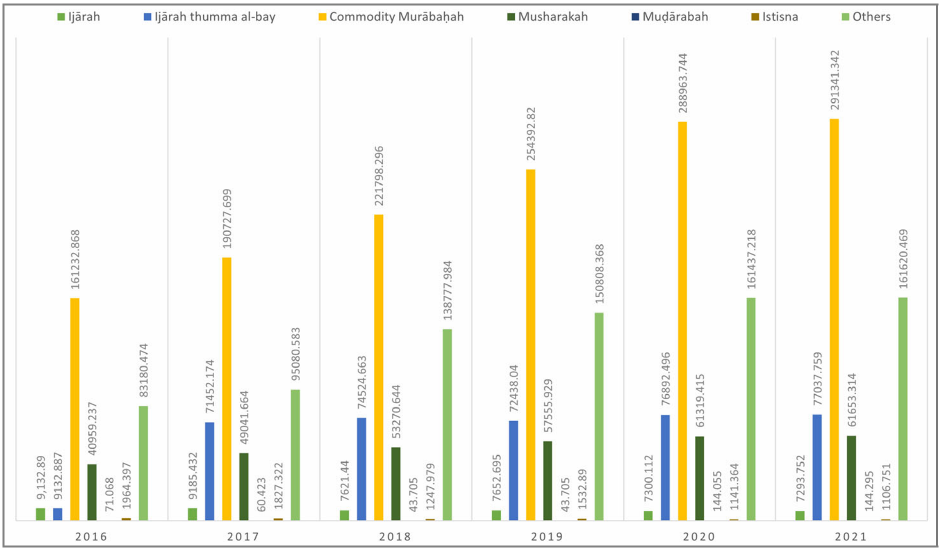
	Banks	*Sharīʿah concept*	*Tenure*	*Margin of financing*
1	AmBank Islamic Berhad	Al-Ijārah Thumma Al- Baiʿ (AITAB) + Wakālah (agency contract)	Up to 9 years	90%
2	Bank Islam Malaysia Berhad	Murābaḥah	Up to 9 years	90%/100% for fresh graduate
3	Bank Muamalat Malaysia Berhad	Murābaḥah, Waʿd Mulzim (binding promise), Wakālah, and Rahn (pledge)	Up to 108 months (9 years)	100%
4	CIMB Islamic Bank Berhad	Ijārah Thumma Al-Baiʿ (AITAB)	Up to 9 years	90%
5	Kuwait Finance House (Malaysia) Berhad	Ijārah Muntahiah Bi Tamlīk	2 to 9 years	90%
6	Maybank Islamic Berhad	Murābaḥah/Al Ijārah Thumma Al Baiʿ (AITAB)	Up to 9 years	90%

Table 2 Debt-based Sharīʿah concepts for home financing

	Banks	*Sharīʿah concept*	*Tenure*	*Margin of financing*
1	AmBank Islamic Berhad	Tawarruq, Murābaḥah, Wakālah and Waʿd	Up to 35 years or up to age 70 years (of the customer)	95% [inclusive of mortgage reducing term takaful ('MRTT')]
2	Bank Islam Malaysia Berhad	Tawarruq	35 years or age 70 (of the customer)	90%
3	Bank Muamalat Malaysia Berhad	Tawarruq including Murābaḥah, Wakālah and Waʿd Mulzim	20 years	90%
4	CIMB Islamic Bank Berhad	Commodity Murābaḥah	35 or 70 years of age (of the customer)	95% [inclusive group mortgage term takaful (GMTT)/legal/ valuation fees
5	Kuwait Finance House (Malaysia) Berhad	Ijārah Muntahiah Bi Tamlīk	35 years or 70 years of age (of the customer)	90% + 5% (MRTT/legal fees/stamp duty/valuation fee)
6	Maybank Islamic Berhad	Commodity Murābaḥah	35 years	Up to 95%

Figure 1 shows the current trend of financing contracts adopted by Malaysian Islamic banks.

Figure 1 Financing contract used by Malaysian Islamic banks (see online version for colours)



Source: BNM (2021)

Based on Figure 1, most of the Islamic banks give priority to commodity *murābaḥah*-based financing, followed by *ijārah thumma al-baiʿ*, *ijārah*, and finally equity-based financing. The *mushārakah* contract ranks fourth whereas *muḍārabah* and *istiṣnāʿ* have a very tiny portion for equity-based financing. Figure 1 also indicates that Islamic banks are adopting debt-based financing as compared to equity-based financing. A study by Muneeza et al. (2020) finds that nine Islamic banks out of 16 are using commodity *murābaḥah*, and five Islamic banks are using *mushārakah mutanāqiṣah* for their home financing facilities. According to Subky et al. (2017), the current trend of Malaysian Islamic banks for home financing is moving towards commodity *murābaḥah* and *ijārah muntahiyah bi al-tamlīk* (IMBT), while turning away from *mushārakah mutanāqiṣah* and BBA. The reason behind this is the flexibility of other contracts like commodity *murābaḥah* and IMBT to provide financing and the reluctance of Islamic banks towards equity-based financing.

3.2 The rationale behind favoring debt-based financing

Islamic banks tend to favour debt-based financing for several reasons. Firstly, to ease the consumers so that they can purchase the goods which are needed (Siddiqi, 1981). Secondly, there are many factories and companies that need a massive amount of money to buy machinery, equipment, and vehicles to continue their production and services. These companies also ask the banks to provide finance to maintain working capital and other necessary financial support. To cater to their needs, most of the banks provide several types of financing (BIMB, n.d.c; BMMB, n.d.; BPMB, n.d.). Thirdly, there are very few products for equity-based financing in the current practice of Islamic banks because there is a perception that equity-based financing is more difficult in operation as compared to debt-based financing; this perception is based on a conventional banking standpoint, where equity-based financing contains risk and complicated nature. The financial institute, as a partner in equity-based financing, must oversee projects which require managerial skills and expertise. It should also be noted that the client and the expected projects need to be assessed carefully (Akacem and Gilliam, 2002). Fourthly, in the case of *murābaḥah*, it does not raise as many Sharīʿah issues/concerns by practicing it for the Islamic banks which are easy and very compatible with the current financing system. Moreover, it has less risk and fewer complications as compared to the profit and loss sharing-based contracts (Alkhan, 2020). Fifthly, the tendency and preference of businessmen towards *murābaḥah* contract as it gives the freedom and full access to the asset/property to utilise without the requirement of sharing the profits or the management, and without having any interference by another party (Alkhan, 2020). Moreover, Amin et al. (2011) find that there are customers who fall for Islamic financing due to their attitude towards Islamic banking, social influence, and the pricing of Islamic banking products. Therefore, Islamic banks offer customers such facilities to purchase their wanted goods or facilities and ease their payment by allowing instalment facilities.

3.3 Consequences and duties in debt-based financing

The customers of those debt-based financing products need to fulfil the requirements of the payment according to the agreement. So, if they can maintain the obligation of instalments schedule accordingly, they will be free from that debt, and they may own the property at the end of the tenure based on the initial agreement. Figures 2 and 3 provide some information on the obligations upon the customer to fulfil his duty towards the financier.

Figure 2 The obligations upon the customer for vehicle financing

4. What are my obligations?

- Monthly Rental RM:
- The total amount payable, including the amount financed is RM:

Note:

- For variable financing, monthly rental and total amount payable may vary rate if BFR changes.
- A revision in BFR will result in an increase/decrease of monthly instalment or lengthening/shortening of the tenure of the facility (at option of Hirer).
- Any payment made which is more than the monthly instalment payable will be treated as an advance payment. Such payments do not in any way reduce the total interest payable and are not redrawable. The advanced payment will be used to pay the next instalment due or any fees and charges.

Source: CIMB Islamic (n.d.)

Generally, Islamic banks provide significant information about a product through the official website of the bank and the PDS. Based on those sources, a customer can find all the liabilities and duties that he/she should carry on upon the approval of the financing. The obligations are basically to pay some charges such as stamp duty, legal fees, processing fees, and others during the agreement. Most importantly, the monthly instalment should be paid on time as prescribed by the financier (the bank) and to take care of the vehicle or the house as agreed by both parties.

But if they fail to do so, the bank has to issue reminders to them. After two or three reminders, if they are still not able to pay the instalments, the bank will take necessary legal action as it is within their right to do so (Lee, 2016; Abdullah and Ramli, 2011). The financier also has the right to repossess the vehicle or home if the customer is unable to pay the outstanding. Moreover, Islamic banks also can impose compensation as a late payment charge on the customer until the outstanding payment is settled (Muneeza et al., 2019). On the other hand, if the customer comes to the bank when he is facing difficulty in fulfilling his obligation to the bank, the bank may suggest rescheduling or restructuring the existing financing facility to reduce the burden of the current facility. Thus, a customer may wish to reschedule his existing facility by changing his instalment rate and period while entertaining the same financing facility. In case the customer wants another financing so that he can avoid any financial constraints to continue his current facility, the customer may consult with the bank to apply for the restructuring of his existing financing facility through third-party financing (Muneem et al., 2020).

Figure 3 The obligations upon the customer for home financing (see online version for colours)

7. What are my obligations?

- Your Monthly Instalment is RM ____________.
- Total payment amount at the end of ______ years is RM ____________.
- Your Monthly Instalment and total payment amount will vary upon changes in the BR as illustrated below, however, the total payment amount will not exceed the Bank's Sale Price.

Rate	Today (BR = ______ %)	If BR goes up by 1%	If BR goes up by 2%
Monthly Instalment	RM	RM	RM
Total profit at the end of ____ years	RM	RM	RM
Total payment amount at the end of ____ years	RM	RM	RM

Note: Illustration on the effect of changes in BR can be referred to https://www.bankislam.com/personal-banking/other-information/base-rate-and-historical-benchmark/.

- Any changes in the BR, EPR and the Monthly Instalment (if any) which is applicable to your financing will be communicated to you prior to the effective date of the new rates and Monthly Instalment (if any).
- During a property construction period, you are required to service the monthly profit on the financing amount disbursed by the Bank to the Developer/ Contractor.
- Any excess payment amount between monthly payment and the actual profit charged shall be utilized to set-off any shortfall in monthly payment or to settle any other charges that may incur in the future.
- In the event that the property financed under this facility is not completed and has been categorised as abandoned by the Ministry of Housing and Local Authority, you are obliged to service the monthly payment to the Bank as per the payment term stipulated under the Letter of Offer for the following:

  (a) Financing amount disbursed to the Developer/ Contractor; and

  (b) Profit accrued until full settlement of the financing amount disbursed.
- Customer is obliged to pay the monthly payment until full settlement of the financing. Should the financing tenure extended beyond the retirement age, the customer is still obliged to pay the monthly payment. However, the customer may opt at any time to fully settle the financing upon reaching retirement age.

Source: BIMB (n.d.d)

5 Conclusions

Dayn (debt) allows people to borrow money and pay them back at a later time in one scenario, whereas in another scenario, which is more practised by the current Islamic banking system, a person buys a commodity, and he/she pays the price of that commodity in instalments for several years as agreed upon between the bank and the customer. The permissibility of borrowing money or buying commodities in instalments enables many people to fulfil their financial needs. Islam encourages people to help each other and be cooperative among them. Meanwhile, Islam also emphasises the repayment of the debt to the creditors by the debtors. The *ḥadīth* shows that it is such an injustice to the creditor to procrastinate the repayment of the debt, and it is also stated in the *ḥadīth* that a person may not enter paradise until his debt is paid.

In the current practice of the Islamic banking system, the debt occurs through a sale or lease contract such as buying a car or house or leasing them from the bank where the customer is liable to pay the price of such commodity in instalments. The most used concept for those sale contracts is *murābaḥah*, *tawarruq*, commodity *murābaḥah*, *ijārah,* and *ijārah muntahiyah bi al-tamlīk / al-ijārah thumma al-bayʿ* (AITAB). So, the payment of those contracts is considered as debt or liability of the customers to pay them accordingly. Therefore, the customers are obliged legally and religiously to pay the instalments and they should not procrastinate when they can pay the instalments. In case the customer is facing any struggle to fulfil his obligation, he may consult with the bank. Moreover, the bank has the right to have any legal action if the customer is not cooperative and dutiful with the payments. However, it is not encouraged for someone to burden himself with lots of debts while unable to pay back his debts by cash or property. The Islamic banking system may offer more equity-based products instead of debt-based products to stop more debt burden to the customers.

Generally, this study contributes to the body of knowledge and especially expands the literature on debt-based financing in Malaysian Islamic banks. Moreover, this study provides valuable information and guidance for the current and potential customers and, also for the general public to know the financing system provided by Islamic banks and the rights and duties as customers/debtors. The results of this study are significant for the bankers where this research can be a reference to introduce a new Sharīʿah compliant financing product and to issue guidelines and policies which protect the rights of banks as the financier and at the same time, allow the people to receive financial support to obtain what they need. The scholars will find it interesting as it provides the current status of debt-based financing in Malaysian Islamic banks and urges to have some alternative financing systems such as equity-based financing. Future research may find out other methods of payment and alternatives to help reduce the practice of debt-based contracts.

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