

Compensation and Penalty Imposed on Debt Settlement of Islamic Products

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Abstract

As the conventional system has been established ever since, the concept of penalty plays an important role in the conventional system at least to secure the financiers from being manipulated by the financees. However, the classical Muslim jurists prohibited such a type of penalty to be imposed on any Islamic debt-based transaction since it would involve an element of usury (*riba*). The purpose of this paper is to extend the examination on debt settlement compensation and penalty, and their compliancy with *shariah* law. The study was then conducted within the ambit of two sacred revelations and the rest of reasoning principles in *usulfiqh* as well as Islamic legal maxims. The findings show that the compensation (*ta'widh*) and penalty (*gharamah*) might be imposed by Islamic financial institutions on early settlement within lock-in period and on delayed payment. In addition, discretionary rebate (*ibra'*) might be given to the early settlement after the lock-in period. The limitation of this study is that it just focuses on compensation and penalty, and concentrates only on Islamic financial system.

Keywords: Compensation; Penalty; Delayed Payment; Early Settlement; Lock-in period; *ta'widh*; *gharamah*; *ibra'*

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