

Penalty for Late Payment: The Study of Shariah Risk in Islamic Housing Products in Malaysia

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Abstract

The Islamic banking scheme has become an alternative to the conventional banking scheme since conventional banking is based on riba, that strongly prohibited by Shariah. Islamic banking scheme charges profit through Islamic-authorized sale and leasing transactions between banks and customers. However, through the sale and leasing transactions entered into, the customer is also required to purchase and rent in instalments as specified in the contract. If the client is late paying the specified instalment, how does the bank engage with it? Hence, the study to identify the management of Shariah risk by selected banks through the practice of Islamic housing financing contracts in dealing with the issue of customer default. This study was conducted qualitatively using two main methods: library research and the unstructured interview method. The library research method is applied to build the research theory by reviewing related literature and official websites. As for the interview, it is conducted to obtain primary data on the practice of late payment fines namely ta'wid (compensation) and gharamah (penalty) in selected banks. The researchers apply a purposive sampling

method in conducting the interview technique by interviewing experienced and knowledgeable respondents regarding the issue. As a result, this study found that out of the six banks surveyed, only two banks impose two both ta'wid and gharamah, while the other four banks prefer ta'wid fines. The study also found that the Shariah risk solution to the practice of charges imposed by banks is based on the stipulation set by Bank Negara Malaysia (BNM). This can be learned that only the government can fine offenders through the concept of ta'zir and BNM has delegated its power to the bank to carry out the charge to defaulting customers.

Keywords: *Gharamah; Ta'wid; Penalty; Compensation; Islamic Housing Financing*

Introduction

Two banking systems have been practised in Malaysia: the conventional and Islamic banking systems. Previously, Malaysia only practised the conventional banking system before independence when colonised by the British, who had introduced their banking system based on interest-loan. Since then, the conventional banking system has continuously dominated Malaysia financial

system (Ali and Hassan, 2020; Asni, 2021). However, in tandem with the establishment of Islamic banking abroad and the successful establishment of Lembaga Tabung Haji in 1963, there had been an insistence by the Muslim community in Malaysia to set up Islamic banking in Malaysia. The intention was realised when the Islamic Banking Act 1983 came into effect on 7 April 1983, which provided the first establishment of Bank Islam in Malaysia, namely Bank Islam Malaysia Berhad, to offer a Shariah-compliant Islamic banking scheme (Gullick 1987; Asni et al., 2021).

Since the launch of the Islamic banking scheme, it has provided an opportunity for conventional banks to participate. There are currently 16 banks offering Islamic banking schemes. Among the important products offered are Islamic housing financing products. There are now five Islamic housing financing products comprising *bay' bithaman 'ajil* (BBA), *tawarruq munazzam*, *musharakah mutanaqisah* (MM), *ijarah muntahiyah bi al-tamlik* dan *ijarah al-mawsufah fi al-dhimmah*. These products are approved by the Shariah Advisory Council (SAC) of BNM (Asni & Sulong 2018).

In fact, the Islamic banking scheme has become an alternative to the conventional banking scheme since conventional banking is based on *riba*, that strongly prohibited by Shariah. Generally, conventional banking engages with *riba* when it charges interest to customers through loan transactions. Similarly, it charges additional interest when customers are late paying their instalments from the stipulated period (Hatta & Samah, 2015; Asni, 2020).

In contrast, Islamic banking scheme charges profit through Islamic-authorized transactions of sale and leasing between banks and customers. However, through the

sale and leasing transactions, the customer must purchase and rent in instalments as specified in the contract (Haron 2005; Ahmad et al., 2021). If the client is late paying the specified instalment, how does the bank engage with it? According to Ishak's study (2019), the imposition of late penalties either in the form of *gharamah* and *ta'wid* by the bank may carry the implications of *riba*. However, based on *maslahah*, it is allowed for Islamic banks to consider these penalties in which they would considerably be affected due to the late repayment. In fact, like their conventional counterparts, Islamic banks utilise their depositors' funds as funding capital.

Meanwhile, the study conducted by Muneeza et al. (2019) found that the imposition of *ta'wid* and *gharamah* without identifying the debtor's situation could lead to Shariah issue. Thus, the researchers suggest that Islamic banks find other alternatives in solving the problem of practising the concept of *rahn* (collateral) and *kafalah* (guarantee) can be used alternatively to recover money which a customer owes to an Islamic bank.

Therefore, based on the Shariah risks found in the practice of late payment fines practised by the Islamic banks, this study will identify the management of Shariah risk by selected banks through the practice of Islamic housing financing contracts in dealing with the issue of customer default. Those products are selected because of their long-term financing that can be riskier for Islamic banks, including late payment fines.

Islamic Late Payment Fines in Malaysia: Literature Review

The Concept of Gharamah and Ta'wid in Islamic Law

Gharamah is a penalty, while *ta'wid* is a compensation. *Gharamah* is imposed on borrowers who are late paying debts from the specified period. While *ta'wid* is the compensation

payable by the debtor due to the late payment from the specified period as, the delay may lead to a loss of creditor (Ishak 2019b). The difference between both concepts can be summarised as the following: -

	<i>Gharamah</i>	<i>Ta'wid</i>
Rate of penalty	It could be more than 1%	Must be 1% per annum
Managing the penalty	Must be channelled to charity	Can be recognised as income

According to Sharia law regarding the imposition of *gharamah*, the Islamic scholars have agreed that the conditions and imposition of *gharamah* are *riba*. According to the early Islamic scholars (*al-mutaqaddimin*) such as Ibn 'Abd al-Barr, the scholars agreed that the *riba* banned by the Quran is when the creditor imposes additional fines to the debtor in return for paying later than the set time (Al-Barr 2000). Similarly, according to al-Jassas (1992), *riba al-jahiliyyah* refers to the addition of fines due to the delay in repaying debts from the period. Hence, 'illah (cause) of *riba* which Shariah prohibits, is the addition because of late payment of the debt from the specified time. It is a form of exploitation and discrimination between rich lenders and poor borrowers when the former exploits the latter's inability to pay (Ishak & Asni, 2020).

The ban is based on the hadith narrated by Ibn 'Ubaid that the Prophet (PBUH) saying that "every profit-generating loan (to a creditor) is a transaction of *riba* (al-Baihaqi 2003)." According to al-Hattab (1984) from the Malikiyyah scholars, if required of the debtor at the beginning of the contract that is when failing to settle the debts at the specified time, the debtor has to give something to the creditor, so it is *riba* whether it is a gift benefit or others.

According to al-Mundhir, the Islamic scholars agreed that when the creditor

requires the debtor to add in a gift for late payment, the additional or the gift is forbidden *riba*. Ibn Qudamah (1405H) said that the Islamic scholars agreed to ban *riba al-jahiliyyah*. According to al-Barr (1980), each condition of the addition of debt or grant in the form of benefit to the creditor in return for debt repayment, then it is *riba* even though the benefit is to feed the animal of the creditor. Based on the opinions of the different scholars or mazhabs, the scholars of *al-mutaqaddimin* agreed that the terms of addition by whatever name was placed because late payment of the time was the implication of *riba*.

The ban on the obligation of the increase in debt due to the late payment of the period is supported by contemporary scholars such as Mustafa al-Zarqa', al-Sadiq al-Darir (Majalah Abhath al-Iqtisad al-Islami 1405H), Sha'ban (1977), al-Misri (1405H) and al-'Attar (1975). While amongst the institutions is Majma' Fiqhi Islami (1990), they said, when the debtor is late paying the debt over the time, it shall not be liable for any increase whether on condition that it will be made in the early, mid-term or without in the contract as it is banned *riba*. Similarly, the term of the fine is banned by most Shariah advisory institutions such as Kuwait Finance House (2010), Bank Islam Jordan (1994), Dallah al-Barakah (2012), Bank Islam Qatar (2015).

Regarding the Shariah law of imposing *gharamah* by the bank against late-paying customers in instalments, the results collection of *gharamah* are not taken by the bank but channelled to charities (Ishak, 2019c). According to al-Qurrah (2019), most sect scholars comprising the Hanafiyyah, Shafi'iyyah, Malikiyyah and most current Islamic scholars ban the imposition of *gharamah* even though it was channelled to charities. This is because, when the terms of the imposition of *gharamah* fines are *riba*, the condition is null and *fasid*, although the result is either channelled to charities or not.

Regarding *ta'wid* by the bank against the customer due to the loss that the bank has to bear because the client's late payment from the appointed time has been disputed among the current scholars. Some current scholars such as Mustafa al-Zarqa', Muhammad al-Sadiq al-Darir (Majallah Abhath al-Iqtisad al-Islami 1405H), Egyptian Islamic Bank (2011), Dallah al-Baraka (2012) and Shariah Advisory Council of BNM (2010) allow the bank to take compensation loss. Among the arguments posed by those who allowed the compensation is derived from the hadith of the Prophet (PBUH) which means, "the wealthy (deliberately) delayed (to repay his debts) is injustice (al-Bukhari 1422H)." This Hadith suggests that those capable of deliberately delaying paying debts are cruel because of cruelty to creditors. Hence, the wrongdoers can be punished, i.e. being fined.

It is also based on the hadith of the Prophet (PBUH) which means "there is no danger and cannot harm others (Ibn Majah 1990)." According to al-Zarqa' (2009), there should be a *ta'wid* charge to the debtor if late payment of instalments, as it may harm the creditor. This hadith also created a method that means to eliminate harm. Therefore, it is obligatory to eliminate harm to the creditor by using a *ta'wid*. According to al-Duraini

(1988), *ta'wid* (compensation) is imposed if the creditor suffers losses due to the delay in instalment payments by the debtor.

Different Status of Debtors According to Shariah Law

In debt, Shariah distinguishes two groups of debtors, namely *mu'sir* (difficult) and *musir* (capable) (Ahmad et al., 2018). Shariah gives flexibility to the debtor who is in a desperate situation to give him time until he is in a state of ability. According to al-Sarakhsi (2000), al-Baji (1332H), al-Nawawi (1392H) and Ibn Qudamah (1405H) that the Islamic scholars agree that the creditor is obliged to give time to the debtors who are desperate until they can get out of the desperate situation. The agreement is based on the words of Allah SWT, which means, "If the debtor is in difficulty, grant him time till it is easy for him to repay (al-Baqarah: 280)." According to al-Qadi Ibn al-'Arabi, giving allowance to debtors who are in difficulty is justice, but the capable debtors who are late paying the debt are tyranny. To give time to difficult debtors is also supported by Majma' Fiqh Al-Islami (2012).

According to Islamic law, the determination on *musir* and *mu'sir* debtors is significant in Islamic study as there are differences in legal implications for both. From the point of language, *mu'sir* is to be difficult (*a'sar*), become narrow (*adaq*) and need something (*aftaqir*). The words *al-'usrah* and *al-i'sar* also mean *qillah dhat al-yad* which means financial hardship (Ibn Manzur 1990). The Hanafi, Shafi'i and Hanbali schools define *mu'sir* with people who have no money and property (Ibn 'Abidin 1386H; Al-Dimyati 1997; al-Mardawi 1956). While according to the Maliki School, *mu'sir* is a person who has no capital for sale (al-Dusuqi 2010). According to Majma' Al-Fiqh Al-Islami (2012), *i'sar* is a level of a person's financial

condition to makes him unable to bear the obligations obliged to him and settle his debts. The definitions given by the *fuqaha*, it is understandable that *mu'sir* refers to those who suffer from the narrowing of the money to settle the debt because the available funds are limited to meet the basic needs of life. Basic needs are like clothing, food, shelter, necessities of the home with enough rates for themselves and their families. To prove that one is in the state of *mu'sir*, Islamic scholars give four methods of proofing i.e., by the *iqrar* of creditor, that the debtor is *mu'sir*, witness testimony, oath and *qarinah* (indication) (Ibn' Abidin 1386H).

The indicator for determining the debtor is in a difficult situation is when he cannot fulfil the five claims in *maqasid al-daruriyyat*, beginning with religion, life, intellect, lineage, and wealth. *Daruriyyah* is the thing Allah requires to be preserved because according to the Shariah view, these five things are necessary for life, and if one of them is missing, life cannot be continued. The way to preserve these five things, the sect of al-Shafi'i states that the requirements are food, drink, clothing, shelter, maintenance (living costs) and education (al-Sharbini 2010). While for the capable debtor, the indicator is the concept of preservation of five things in *maqasid al-Daruriyyat* through the same sort, but the preservation is in the state of *maqasid al-hajiyyat* (Asni, 2019).

Ta'wid and Gharamah Guidelines by BNM

The imposition of *ta'wid* and *gharamah* by the bank to the customer for not settling the monthly instalment payment within the specified period. The *ta'wid* fine rate is 1% of the monthly instalment payment if the customer is late paying instalments after 14 days from the payment time set out monthly (Norazlina et al., 2019). The banks in Malaysia practice *ta'wid* as the SAC of BNM

permits it. The SAC of BNM, at its 95th meeting on 28 January 2010, has ruled that *ta'wid* may be imposed for the delay in the payment of financial obligations arising from the contract exchange (such as sale and hire purchase) and *qard* (debt). The received *ta'wid* revenue can be accounted for as income by the seller, financier or creditor based on compensation for the actual loss incurred by the bank. While charges from *gharamah* are not allowed to be taken as income but should be channelled to charities designated by the Shariah Committee (SC) in the respective banks as mandated by BNM (2013).

However, as a step to protect the customers, Islamic banks should consider the ability of customers to repay their financing. Maximum rates for *ta'wid* and *gharamah* charges are determined by BNM (2010b). Subsequently, the SAC of BNM, at its 101st meeting on 20 May 2010, also decided the mechanism of late payment charges for Islamic banking institutions (BNM 2010b). The imposition of late payment charges by Islamic banking institutions, which include *gharamah* and *ta'wid* is allowed with the following conditions:

- a. *Ta'wid* can only be charged for late payment from the specified period.
- b. *Ta'wid* can only be imposed after the payment period agreed by both contracting parties.
- c. Islamic banks can take *ta'wid* charges as income because they are charged as compensation for actual losses incurred by Islamic banking.
- d. *Gharamah* cannot be counted as income; instead, it must be channelled to charity.

According to Yaakub et al. (2014), the amount of compensation for *ta'wid* is less than the total amount of the late payment

penalty. Hence, the surplus of *ta'wid* results, the bank will channel it to charities in the name of *gharamah*. In the latest late payment penalty guidelines for Islamic financial institutions issued by Bank Negara Malaysia which came into force on 1 January 2012. Among those touched on the guidelines are that Islamic banks can impose two late payment charges comprising a combination of *ta'wid* and *gharamah* (Bank Negara Malaysia 2013).

For example, when a customer gets housing financing from Islamic banking for RM400,000. The monthly instalment payable by the customer is RM2000 before the fourth day of each month. Meanwhile, the profit rate of financing is 10%. Late payments are at 9.50%, as determined by the bank upon approval by BNM (Saleem and Mansor, 2020). The *ta'wid* charge imposed by the bank is 1% as determined by the state bank. While the charge for *gharamah* is the balance of the total late payment after being deducted

with *ta'wid* charge. Examples of such arrangements are (Bank Negara Malaysia 2013):

1. Calculation of combined late payment charges (*ta'wid* & *gharamah*):
 $RM2,000 \times 9.50\% \times 30/365 = RM16.61$
2. Calculation of fine *ta'wid*:
 $RM2,000 \times 1.00\% \times 30/365 = RM1.64$
3. Calculating the amount of *gharamah* payable is:
 $RM16.61 - RM1.64 = RM14.97$

As in the calculation, the total combined fine imposed by Islamic banks on customers if there is an arrear for a month is RM16.61. Then the bank will share the *ta'wid* charge of RM1.64 for the actual loss cost, and the remaining RM14.97 will be channelled to charity.

Table 1: Characteristics of the *Ta'wid* and *Gharamah* fines (Bank Negara Malaysia 2013)

Mechanism	<i>Ta'wid</i>	<i>Gharamah</i>
Concept	Creditors bear loss due to late payment	Penalty to avoid late payment
Rate of charge	- Based on real losses - Rate fixed at 1% - Based on the outstanding principal balance	- BNM sets rates - Not compounding - Based on the outstanding principal balance
Use of results	- Payment to the bank	- Delivery to charity
Liability	- Customer's capacity is not more than 1% of the outstanding principal balance	- Customer's ability set by BNM

Risk Potential and Risk of Shariah Non-Compliance

Shariah non-compliance risk arises from the Islamic banks that fail to comply with Shariah principles and decisions. This is

defined by the IFI Shariah committee or authorised body, which may lead to the loss by affecting Islamic banks' reputation, either in financial or non-financial form. The Shariah Governance Framework (SGF) of BNM defines Shariah non-compliance risk as

the risk of failure in fulfilling its obligation to adhere to Shariah principles or possible incidences of Shariah non-compliance (BNM, 2011). According to the Islamic Financial Services Board (IFSB, 2005), the risk of Shariah non-compliance is the risk arising from the failure of Islamic banks to comply with Shariah rules and principles, which are established by the Shariah Board of the IFI or related bodies in determining Shariah affairs.

Failure to comply with Shariah requirements may arise as a consequence in every aspect of Islamic banking operation. This failure could be due to the lack of governance, business processes, support systems, or awareness among Islamic banking staff (Rosly, Naim & Lahsasna, 2017). The risk of Shariah non-compliance can also occur in financing, deposits, investments, treasury, gold trading or product structure and legal documentation, which therefore, it needs to be adequately developed by following Shariah principles and legislation, as well as getting the endorsement of the Shariah committee (Ashraf & Lahsasna, 2017).

Also, as part of the requirement to avoid the risk of Shariah non-compliance, Islamic banks need to be alert for any potential factors that could lead to this particular risk (Ali and Hassan, 2019). This aligns with the *usul al-fiqh* method known as *sadd al-dhari'ah* (blocking the means). Technically, *sadd al-dhari'ah* means blocking permissible acts that may lead to evil. Therefore, Islamic banking must ensure security in every activity to avoid any risk potentials of Shariah non-compliance (Hassan, 2016).

Therefore, identifying the potential risks and risks of Shariah non-compliance with the practice of fines is important. This is because the practice of fines in Islamic banking is allegedly not Shariah-compliant because it is

similar to the concept of *riba al-jahiliyyah* as in the previous discussion. Therefore, based on these concerns, the researchers will study the Shariah risk management by the banks studied on the issue of fines imposed on the customers.

Methodology

Research Design

This study uses a cross-sectional narrative review conducted using qualitative data collection methods, specifically unstructured interviews. In this study, interview methods were used to understand the subject matter of the current research with those used in previous studies (Gunarathne and Senaratne, 2017).

Narrative research design is a design of inquiry from the field of humanities in which the researcher studies the experiences of individuals and asks them to provide stories about their experiences (Creswell, 2014). According to Creswell (2014), the researcher often retold the information in a narrative chronology. In the context of this study, stories from respondents about their experiences and knowledge were recorded and handwritten by the researchers to obtain holistic information on the strategies of Islamic banks studied in Shariah risk management related to the practice of fines imposed on customers defaults through housing financing contracts offered. In addition, the researchers also used unstructured interview techniques to obtain information from the respondents as it provided an opportunity for the respondents to present important new issues through open-ended questions (Wilson, 2014).

Selecting the Respondents, Data Management and Analysis

As this study explores the strategies of Islamic banks studied in Shariah risk management related to the practice of fines imposed on customer defaults, the researchers need to engage with appropriate interviewees through the purposive sampling method. The interviewees must have in-depth knowledge of the management of Islamic banking. In other words, it is a non-random selection, but the participants can provide in-depth and trusted information by their knowledge or experience (Etikan et al., 2016). In this regard, the researchers interviewed six officers from different Islamic banks offering all types of Islamic housing financing products in Malaysia. The interviews lasted for about 60 minutes.

The interviews were conducted to determine the respondents' knowledge of the study's objectives. The interviews were recorded through audio recording methods and manually written in notebooks as additional storage if the audio recording is damaged or destroyed. After transcription, the collected information would be analysed based on the thematic method. This method enables the researchers to segment, categorise, summarise and reconstruct the data into important concepts (Lisa M. Given, 2008).

In fact, this method is a practical approach for analysing different perspectives among interviewees, highlighting similarities and differences and generating unanticipated insights (Nowell et al., 2017). All methodologies applied through this study could support the researchers to obtain a holistic view of the strategies of Islamic banks studied in Shariah risk management related to the practice of fines imposed on customer defaults. Meanwhile, in terms of discussion, it will reveal the strategies of the Islamic banks studied to resolve Shariah risk in the practice of fines imposed. To safeguard the respondents' information, their names

were encrypted as requested by them. They are known as O1, O2, O3, O4, O5 and O6.

Validity and Reliability

To ensure the validity of the data, the interview is conducted with participants who are considered the most expert group in this topic. In this regard, the researchers must ensure that all interviewees have a Shariah background and are directly involved in managing Islamic banking at least 3 years. Thus, the selection of respondents consisting of Shariah officers is correct. In terms of the reliability of the data, all interviewees are questioned with the same set of questions. One-to-one interviews with standardized questions could improve the reliability of the study (Conway et al., 1995). All facts mentioned by interviewees to the researchers have been confirmed before leaving the session to avoid accidental errors. Before the interview, the questions were submitted a week earlier to prepare for the best answers.

The data also were subjected to triangulation. In research, triangulation helps address the limitations of a given methodology by complementing its weaknesses with the strength of other methods (Brewer and Hunter, 1989). Denzin (1984) identified four forms of triangulation, which are; data source triangulation (retrieve data from several different sources to form one body of data), investigator triangulation (using multiple observers instead of a single observer in the form of gathering and interpreting data), theoretical triangulation (using more than one theoretical position in interpreting data), and methodological triangulation (using more than one research method or data collection technique). This study used data source triangulation to ensure the accuracy, credibility and validity of the data. Therefore, to strengthen the data accuracy, credibility, and validity, the researchers asked the

respondents to show the official documents related to the fine practices practiced by the bank to be cross-referenced with the interview data. This is to mutually strengthen the data acquisition to achieve the objectives of the study.

Results

The following are the types of fines imposed by the banks studied:

Table 2: *Ta'wid* and *Gharamah* Practices by Selected Banks

Financing Products	Banks	Penalty Type
Tawarruq Munazzam	BIMB	<i>Ta'wid</i>
	Al-Rajhi	<i>Ta'wid</i>
	BSN	<i>Ta'wid & Gharamah</i>
BBA	Public Islamic Bank	<i>Ta'wid & Gharamah</i>
MM	Public Islamic Bank	<i>Ta'wid & Gharamah</i>
	RHBIB	<i>Ta'wid</i>
IMBT & IMFD	KFH	<i>Ta'wid</i>

Based on the table above, it is the result of an interview session conducted with the respondents who are Shariah secretariat officers representing their respective banks, namely Bank Islam Malaysia Berhad (BIMB), al-Rajhi, Bank Simpanan Nasional (BSN), Public Islamic Bank, RHBIB and Kuwait Finance House (KFH). Based on the extent of compliance by the banks surveyed on the stipulation of fines made by BNM, respondents comprising O1, O2, O3, O4, O5 and O6 agreed that the practice of fines which include *ta'wid* and *gharamah* is in line with guidelines issued by BNM. In more detail, O2 claimed:

“The ta'wid and gharamah fines practised by this bank for housing financing products are following the guidelines set by the central bank. This is because if the bank does not follow the guidelines set by BNM, the banking license can be revoked and the bank will have to pay a high fine. Ta'wid compensation will be taken by the bank, while the proceeds of the gharamah fine

will be channelled to a charity designated by the Shariah committee. ”

Based on the question on the risk of Shariah management on the practice of fines in the form of *ta'wid* and *gharamah*, respondents O3 and O4 stated,

“There is a Shariah risk on the practice of ta'wid and gharamah because it can bring riba implications, but it needs to be applied because it wants to prevent customers from not paying monthly instalments to the bank. This is because, the bank will suffer losses if it does not impose any fines. However, the imposition of fines in the form of ta'wid and gharamah does not violate the principles of Islamic law as it is set by the government, not set by the bank. The practice will violate the principles of Shariah law if the bank determines the fine on behalf of the defaulting customer without obtaining the consent of the central bank. ”

While some respondents consisting of O1, O2, O5 and O6 did not agree with the imposition of *gharamah*, but agreed with the fines of *ta'wid*. This is as stated by O6 that is,

“The imposition of fines in the form of ta'wid is an issue that is disputed by modern scholars, where some scholars allow it and some scholars do not allow it. However, the imposition of fines in the form of gharamah is agreed upon in its prohibition. Therefore, our bank does not impose fines in the form of gharamah.”

Based on the question of strategies to solve the problem of Shariah management risk on the practice of fines in the form of *ta'wid* and *gharamah*, O3 stated,

“The imposition of fines in the form of ta'wid and gharamah is determined by the government through Bank Negara Malaysia, the bank only acts as a representative who carries out fines on behalf of the government. Therefore, the practice of fines carried out by the bank is in line with Shariah law that the government can punish those who default to pay debts.”

In addition, the question of Shariah risk management for customers who default to pay home instalments, O3 stated,

“Shariah law differentiates the group of debtors where the indebted debtor is eligible to ask for a postponement but provided that the customer needs to contact the bank first to discuss how the appropriate mechanism to resolve difficulties such as job loss, disaster, permanent illness, death and so on. Meanwhile, for customers who can afford it, but fail to pay the monthly instalment to the bank, then the bank will impose a fine on them as allowed by Bank Negara Malaysia.”

Discussion

The study's findings show that the banks studied impose fines according to the fine guidelines set by BNM. The findings of this study are in line with the stipulation issued by BNM that the bank can impose fines of *ta'wid* and *gharamah* or one of the two fines. BNM established the practice of fines to prevent cases of default by customers in settling financial obligations as a result of contracts. According to Hussain et al. (2013) and Asni and Sulong (2018), based on the Central Bank Act 2009 (Act 701), the SAC of BNM is given the status as the sole authority in Shariah matters related to Islamic banking. Thus, Islamic banking practices in banks licensed by BNM are subject to SAC decisions, including issues related to fines.

The next study's findings showed that the majority of respondents disagreed on fines *ta'wid* and *gharamah*. Some respondents did not agree with *gharamah* and agreed with *ta'wid*. While some respondents agreed with *ta'wid* and *gharamah* as practised by their respective banks. For the respondents who agreed with the imposition of *ta'wid* fines is in line with some modern scholars such as Mustafa al-Zarqa', Muhammad al-Sadiq al-Darir (Abhath al-Iqtisad al-Islami Magazine, 1405H), Islamic Bank of Egypt (2011), Dallah al-Baraka (2012) and the MPS of BNM (2010) which requires banks to take the proceeds of compensation for such losses.

Among the propositions put forward by those who allow fines is derived from the hadith of the Prophet PBUH, which means, “the rich who (deliberately) procrastinate (to pay their debts) are unjust (al-Bukhari 1422H).” This hadith shows that those who deliberately delay paying their debts are unjust because they are unjust to the creditors. Thus, the oppressor can be punished as fined.

Apart from that, it is based on the hadith of the Prophet which means, “there can be no danger, and there can be no harm to others (Ibn Majah 1990).” According to al-Zarqa’(2009), it is necessary to impose a *ta’wid* charge on the debtor if he is late in paying the instalment because it can harm the creditor. From this hadith is also developed a method which means it is obligatory to remove harm. Therefore, it is obligatory to eliminate harm to creditors by using *ta’wid*. According to al-Duraini (1988), *ta’wid* compensation is imposed if the creditor suffers a loss due to late payment of instalments by the debtor.

The respondents who do not agree with the practice of *gharamah* are in line with the opinion of al-Qurrah (2019) that is about the law of imposition of *gharamah* by banks on customers who pay late instalments from time, the proceeds of *gharamah* are not taken by banks but channelled to charities. Based on this, the majority of the Islamic scholars of the sect consisting of the Hanafiyah, Shafi’iyah, Malikiyyah sects and also the majority of the current Islamic scholars banned the *gharamah* fine even though it was channelled to charitable bodies. This is because, when the condition of imposing of *gharamah* is *riba*, then the condition is void even if the result is either channelled to charitable bodies or not.

Some of the respondents who agreed with *ta’wid* and *gharamah* were reasoned that the imposition of both fines could carry the risk of Shariah non-compliance as it could lead to the implications of *riba*. However, it is allowed to be practised because the bank represents BNM to impose fines on defaulting customers (Ishak, 2019c). Such an opinion is in line with the scholars’ consensus that *riba*, which the Qur’an forbids is when a creditor imposes an additional fine on the

debtor in return for paying later than the stipulated time (Al-Barr 2000).

In addition, the reason was given by the respondents who said that the imposition of charge represents BNM is in line with the opinion of al-Qurrah (2019) that it is the responsibility of the government to punish people who commit injustice, especially involving offences to other individuals. Thus, the punishment of *ta’zir* in the form of fines imposed by the bank on customers who disobey is a stipulation set by the government through the BNM which delegates to the bank.

Therefore, the imposition of the fine is not subject to *riba* because the government has provisions to punish those who oppress others with *ta’zir* in the form of *ta’wid* or *gharamah*. Therefore, as long as the bank follows the fines set by BNM, it aligns with Shariah law. This shows that late payment fines are not related to the principal financing given by Islamic banks, instead they represent special fines authorised by the regulator for the sake of *maslahah*.

Based on the findings of the third study, all respondents agree that Shariah law distinguishes between the group of debtors who are *mu’sir* (difficult) and *musir* (able). Shariah gives leeway to the debtor, who is in a state of desperation, to give him time until he is in a state of affordability. Thus, to complete the Shariah risk management, the bank will allow customers who face difficult situations to pay their monthly instalments. However, the exception is on the condition that the customer must contact the bank in advance to discuss the appropriate mechanism. As long as the customer does not complain about their current situation, the bank will assume that the customer does not face any problem paying the monthly instalments.

The findings of the above study are in line with the opinion of the scholars consisting of al-Sarakhsi (2000), al-Baji (1332H), al-Nawawi (1392H) and Ibn Qudamah (1405H) that the scholars agree that creditors must give time to a debtor who is in such a state of desperation that he can get out of that desperate situation. The agreement is based on the chapter of al-Baqarah: 280. According to al-Qadi Ibn al-'Arabi, giving leniency to a debtor in the narrowness of life is justice, but for an able debtor who did not fulfil his obligation in paying a debt is unjust. Giving time to difficult debtors is also supported by Majma' Fiqh Al-Islami (2012).

However, it is recommended that the bank provide guidelines on situations that allow customers to defer financing. This is because unclear guidelines can confuse customers and Shariah objectives to provide flexibility to customers experiencing difficulties not being achieved. Therefore, al-Muni '(2011) proposed guidelines as an identifier for customers who are in a *mu'sir* situation as follows:

- a. Customers are already blacklisted either through CTOS, CCRIS or any authoritative source.
- b. The customer has been declared bankrupt by the court.
- c. The client is currently in the process of insolvency and has already been subject to legal action.
- d. After the event of default. This is because default only occurs after the customer fails to make a payment a few times.
- e. Client's acknowledgement and confirmation with evidence such as job loss, disaster, permanent illness or death.
- f. A customer whose property is frozen by the authorities or even

detained due to the prosecution process in court and proven that he does not own other property is considered a *mu'sir*.

Based on the above findings, although the issue of imposition of fines and differences between debtors can carry the risk of Shariah non-compliance by the banks studied, but found that the banks successfully manage Shariah risk as the objective of the establishment of Islamic banking is to follow Shariah principles in each its products and transactions. It is found that the success is due to the role of the SAC of BNM, Shariah Committee (SC) and Shariah officers in banks in ensuring that Shariah risk management can be addressed properly.

In addition, there is the need for innovation and development of Islamic banking financing products since it involves the management of penalties. The practice of late payment charges by Islamic banks in Malaysia should be explained properly to avoid confusion among customers. These efforts are regarded as the best move to avoid the problems faced by the customers. In conclusion, this approach does not deviate from the policy and principle of Islam and with regards to avoidance of the principal issues of *riba*, there is a need for consolidation of regulatory control by the Bank Negara Malaysia to instil transparency among Islamic banks in Malaysia.

The results of this study can bring good implications to the industries that offer Islamic financing in Shariah risk management, especially on the imposition of fines and differences among debtors. In addition, the results of this study also have significant implications for the public because it can increase public trust in Islamic banks in terms of Shariah risk management on the issues raised in this study.

Conclusion

The study's objective is to identify Shariah risk management by selected banks on the practice of fines imposed through Islamic housing financing contracts to resolve the issue of customer default. The results of the study found that there are elements of fines that include *ta'wid* and *gharamah* or one of both on five Islamic housing financing products that include *tawarruq munazzam, bay' bithaman ajil* (BBA), *musharakah mutanaqisah* (MM), *ijarah muntahiyyah bi al-tamlik* (IMBT) and *ijarah mawsufah fi al-dhimmah* (IMFD) practiced in Malaysia. Of the six banks surveyed, only two banks imposed two fines, namely *ta'wid* and *gharamah*, while the other four banks only imposed *ta'wid* fines. The study found that the Shariah risk solution to the practice of fines imposed by banks is following the stipulations of fines set by Bank Negara Malaysia (BNM). This is because, only the government can fine offenders through the concept of *ta'zir* and BNM has delegated its power to the bank to carry out the fine to defaulting customers.

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