Can Islamic Financial Literacy Minimize Bankruptcy Among the Muslims? An Exploratory Study in Malaysia

Md. Faruk Abdullah1, Muhammad Nazmul Hoque2, Md. Habibur Rahman1, and Jamaliah Said3

Abstract
Studies showed that Malaysians possess low financial literacy. Consequently, bankruptcy cases among young adults in Malaysia are rising. The government and its relevant institutions, that is, credit counseling and debt management agency, provide different training and awareness programs to minimize the bankruptcy rates. Muslims are among the majority that declared bankruptcy; hence, Islamic financial literacy (IFL) may have a considerable role to minimize bankruptcy cases by changing the attitudes and behaviors of debtors. Furthermore, studying IFL is pertinent to Malaysia because it is a Muslim-majority country with the leading Islamic banking market in the world. Therefore, this study aims to construct the theory of IFL from the sources of the Shariah and examines whether it is suitable to implement IFL in different financial awareness programs in Malaysia. The study concludes that IFL provides a comprehensive guideline for borrowers, lenders, financial institutions, and society to reduce bankruptcy. Furthermore, findings from the field study confirmed that IFL could be used in Malaysia to raise awareness among the related parties. This is a qualitative study that employed an inductive and deductive approach to review the sources of the Shariah to come out with Shariah rulings. Furthermore, this study conducted semi-structured interviews with the officials of related government bodies and agencies. It is expected that the outcome would have a direct implication on the policymakers and loaning institutions in Malaysia.

Keywords
Islamic financial literacy, Muslim, bankruptcy, loan, Malaysia

Introduction
Financial literacy has become essential in the modern world for achieving financial well-being (Biplob & Abdullah, 2019; Karakurum-Ozdemir et al., 2019; Lusardi, 2019; Philippas & Avdoulas, 2020). However, some studies revealed the worrying fact that today’s youth are significantly lacking in financial literacy. College and undergraduate students have poor financial knowledge even in the developed nations, which results in a high level of debts, bankruptcy, and weak retirement planning skill (Artavanis & Karra, 2020; Brown et al., 2015; De Bassa Scheresberg, 2013; Lusardi, 2019; Nga et al., 2010).

In the context of Malaysia, financial literacy is still between low to moderate levels. Many Malaysians have yet to possess a decent level of financial literacy (Idris et al., 2013; Janor et al., 2016; Yew et al., 2017). According to the Financial Education Network (2019), one in every three Malaysians believed that they possessed minimal financial knowledge. More than half of the Malaysians find it challenging to have emergency funds of MYR 1,000. Mokhtar et al. (2018) concluded that most Malaysians have limited knowledge of the risk and investment of wealth.
Consequently, Malaysia has an alarming number of bankruptcy cases. Until December 2017, the total number of bankruptcy cases in Malaysia was 300,958. From 2013 to December 2017, the courts administered 100,610 bankruptcy cases. In 2017 alone, 18,227 cases were registered for bankruptcy. Individuals aged between 35 and 44 years old have the highest number of bankruptcy cases, with 34,606 cases representing 34.4% of the total bankruptcy cases (Malaysian Department of Insolvency, 2018).

The Malaysian government considers bankruptcy a serious issue, especially among youths aged 25 and below. Bankruptcy causes serious trouble to the person’s personal life, and it is also a loss to the country. Bankruptcy involves closing the business, deactivating the bank account, restricting the withdrawal of money and opening a new account. Moreover, a bankrupt entity is not allowed to obtain a new loan. Apart from that, bankruptcy tarnishes the person’s image in society. Therefore, the Ministry of Finance in Malaysia is taking initiatives to resolve this problem by collaborating with the Malaysian Department of Insolvency and Credit Counseling and Debt-Management Agency. In this regard, creating financial awareness among Malaysian youths is a significant initiative (Carvalho & Hamdan, 2015; Hilmy et al., 2013; Malaysian Department of Insolvency, 2018). Moreover, if the problems persist, the ambition of Malaysia to become a high-income nation may be weakened. (AKPK, 2018; Mohd Aziz & Kassim, 2020).

Several studies discussed the conventional financial awareness among the youth (Brown et al., 2015; Garg & Singh, 2018; Idris et al., 2013; Kadoya & Khan, 2020; OECD, 2020). However, there is a lack of Islamic financial awareness. IFL is appropriate to Malaysia because it is a Muslim-majority country and one of the global leaders in Islamic banking and finance. Apart from that, Muslims hold the highest number of bankruptcy cases with a percentage of 54.21%, comprising 11,498 cases. Therefore, it would be more appropriate to implement IFL awareness among the Malay youths to minimize bankruptcy. Religion plays an important role in changing people’s behavior and attitude (Amin et al., 2014; Baele et al., 2014; Bekele et al., 2016; Bursztyn et al., 2019; Chunping et al., 2016; Salwa & Ilhammie, 2017). Amin et al. (2014) found that religion influences a customer’s choice of Islamic mortgage. Moreover, Baele et al. (2014) concluded that religion significantly influences the borrower in loan repayment. Bursztyn et al. (2019) concluded that religious ethics significantly influenced the loan repayments and defaults among the borrowers in Indonesia. Therefore, this study aims to construct the theory of IFL for bankruptcy avoidances. Then, it explores whether IFL can be used in Malaysia to reduce bankruptcy among Muslims.

While a number of studies have been conducted on IFL but most of them discussed IFL in a generic perspective (Antara et al., 2016; Dewi & Ferdian, 2021; Dinc et al., 2021; Sari et al., 2022). Most of the studies defined IFL as the knowledge of Islamic banking products and services and measured the level of IFL among the people. However, this study comprehensively develops the theory of IFL from the sources of Shariah. It shows the direct implications of IFL to the borrowers, creditors, Islamic financial institutions, and society to reduce the number of bankruptcy cases. To the best of our knowledge, no study was conducted on investigating the role of IFL in bankruptcy avoidances in the context of Malaysia using a similar approach.

It is expected that the study would develop a comprehensive framework of IFL focusing on debt management and bankruptcy avoidances. The study’s outcome would help Malaysian society and Muslim societies worldwide by improving their financial literacy. Furthermore, the government and related credit counseling and debt management organization might use the developed framework for their awareness programs. The policy recommendations might help the government and associated regulatory bodies take the necessary steps to improve people’s financial literacy and well-being.

The subsequent section of the article provides the literature review, which is followed by explaining the methodology. Afterward, the analysis of the findings is divided into two parts. The first part analyses the IFL framework based on library research, and the second part discusses the regulators’ perception of implementing IFL based on the interview data. Finally, the conclusion section summarizes the contribution of this article, provides policy recommendations and points out the limitations of the study.

**Literature Review**

Relevant works of literature are searched and reviewed based on the study objectives. The outcome of the literature review is presented in five sections: (1) financial literacy, (2) IFL, (3) bankruptcy in Malaysia, (4) the relation between bankruptcy and financial literacy, and (5) the relation between religious awareness and bankruptcy.

**Financial Literacy**

According to OECD (2020), financial literacy combines consciousness, education, skills, mindset and conduct, which are essential to make prudent financial decisions.
and finally attain financial well-being at the personal level. Similarly, Kadoya and Khan (2020) concluded that there is a relationship between financial knowledge, financial attitude and financial behavior. Similarly, Antara et al. (2016), states that financial literacy denotes a person’s knowledge, skill, attitude, and behavior to make a prudent financial decision which ultimately leads to financial well-being. A person’s behavior will be influenced by his or her level of financial literacy. According to Garg and Singh (2018), financial literacy is heavily influenced by the youths’ educational attainment. It is also influenced by different socio-economic and demographic factors, that is, age, gender, and marital status. Therefore, there is a link between financial knowledge and financial behavior. They revealed that the financial literacy among youths worldwide is poor, which is a matter of concern.

However, Firli (2017) defines financial literacy more broadly. He mentions that financial literacy is a framework, which combines personal savings and borrowings, calculating expenses, understanding economic, and financial concepts and issues, knowing the financial products and services and making investments. Agreeing with Firli (2017), Abdullah and Chong (2014), mention that financial literacy involves understanding financial products and concepts as an investor or consumer, making an informed decision considering the financial risks and opportunities, and performing other activities to develop financial well-being.

Islamic Financial Literacy

IFL is a new concept, and there have been several contemporary studies that defined IFL. Dinc et al. (2021) argue that IFL evolved based on Islamic law’s ethical and moral foundation. The primary difference between IFL and conventional financial literacy is that Islamic law prohibits interest in financial dealings. Dewi and Ferdian (2021) mention that Islamic law sets the boundary of financial dealings with more permissibilities than prohibitions. The three fundamental prohibitions of Islamic law are: (1) the prohibition of interest, (2) the prohibition of uncertainty and ambiguity in contracts, and (3) the prohibition of unfairness in contracts.

Having known the difference between IFL and conventional financial literacy, IFL can be defined as the knowledge, skills, awareness, and familiarity with financial concepts, products and services which have an impact on the individual’s attitude while taking an appropriate financial decision through following the rules and principles of Islamic law (Sari et al., 2022). Similarly, Rahim et al. (2016) simplified IFL as when individuals utilize their knowledge, skill, and attitude in managing their finances based on the principles and teachings of Islamic Shariah.

Although several studies have defined IFL, there is a lack of discussion on the components of IFL. Abdullah and Anderson (2015) defined IFL as the knowledge of Islamic financial products. Antara et al. (2016) measured IFL based on the Islamic finance concept. However, the aspects of debt management and purifications of wealth are overlooked in these definitions.

IFL does not only include the knowledge of interest-free Islamic financial products, but it is more comprehensive, including a person’s different aspects of financial actions such as saving for the future, incurring debt, and purification of wealth. To the best of our knowledge, only a handful of studies have discussed the comprehensive teachings of Islamic Shariah in managing one’s financial resources in the contemporary context. Therefore, this study intended to discuss IFL from a broader perspective.

Bankruptcy and Financial Literacy in Malaysia

In Malaysia, the bankruptcy law was amended in 2017. The law governing bankruptcy is termed “The Insolvency Act 1967.” According to the act, bankruptcy is a process where a person failed to pay his debt amounting to MYR 50,000 and above before declaring bankruptcy according to the court order (Bankruptcy Amendment Act, 2017). In this process, the debtor's properties fall under the management of the director-general of insolvency (DGI), who sells the debtor’s assets and distributes the proceeds of the sale among the creditors. Properties that are considered necessities for the debtor and his family include clothes and basic furniture with a value not exceeding MYR 5,000, which the DGI may not confiscate. Based on the amended law in 2017, a person can be automatically discharged from bankruptcy after completing the target contribution set by the DGI within 3 years, provided that there is no objection from the creditors (Malaysian Department of Insolvency, 2019).

Once a person is declared bankrupt, he cannot transfer his property to a third party. The existing bank account is deactivated, making the person unable to withdraw money. However, the person may open another account or reactivate the existing account after securing permission from the DGI by justifying a reason such as crediting the salary. The person with bankruptcy status is barred from traveling overseas except with written permission from the DGI or a court order that allows the person to travel overseas. Besides that, the person cannot be the director of a company based on the Companies Act. He is prohibited from conducting any business on his own or forming a partnership. The
person is also not allowed to join his spouse’s or relatives’ businesses (Malaysian Department of Insolvency, 2019).

According to the Malaysian Department of Insolvency (2018), Malaysia has an alarming number of bankruptcy cases. Until December 2017, the total number of bankruptcy cases in Malaysia was 300,958. From 2013 to December 2017, the court administered 100,610 bankruptcy cases. In 2017 alone, there were 18,227 cases registered for bankruptcy. On average, 1,519 cases per month and 50 cases per day are registered for bankruptcy.

Zainal and Ismail (2012) investigated the debt composition of 186 graduates and their attitudes toward repaying their education loans in Malaysia. The study revealed that graduates acquired not only education loans but also other loans such as housing loans, car loans, and credit card loans. In terms of repayment, the educational loan gets lesser priority among the loans to the borrowers. Education loan payment ranked at the fifth level after living expenses, payment for car loans, savings, and payment to parents. Therefore, Perbadanan Tabung Pendidikan Tinggi Nasional (PTPTN) obtained a low collection rate. However, this study did not elaborate on why the borrowers give less priority to the education loan payment.

Nga et al. (2010) examined the status of overall financial and product awareness among young adults in a Malaysian higher learning institution. They investigated whether demographic factors influence general financial awareness. Furthermore, they investigated whether taking a degree in business develops greater financial and product awareness among the youths in the modern time. They concluded that the educational level and specialization impacted the general and financial product awareness among young people. Furthermore, it was discovered that males have a higher level of financial awareness compared with females.

Mohd Aziz and Kassim (2020) mention that majority of the Malaysians have a low level of confidence in financial management, which includes Malaysians from diverse backgrounds. The majority of Malaysians believe that financial management is merely ensuring that their income meets their expenses. However, they overlook the savings and insurance aspects crucial to cover the costs in unexpected events in life.

According to the Financial Education Network (2019), one in every three Malaysians believes that they possess minimal financial knowledge. More than half of the Malaysians find it challenging to have emergency funds of MYR 1,000. Mokhtar et al. (2018) concluded that most Malaysians have limited knowledge on risk and investment of wealth.

### Bankruptcy and Financial Literacy Among the Youth

Garg and Singh (2018) examined the status of financial literacy among youth around the world. Based on their literature survey, they found alarming information that the financial literacy among the youth is low in the major parts of the globe. Moreover, they revealed that several demographic and socio-economic factors such as age, gender, income, marital status, and education level impact the financial literacy status of the youth. Finally, they concluded that financial knowledge, financial attitude, and financial behavior are interrelated.

Md.Shafik and Wan Ahmad (2020) investigated the status of financial literacy among Muslim undergraduate students in Malaysia through questionnaire surveys and interviews. They revealed that students who are exposed to financial knowledge and practices have better financial literacy status. Moreover, students’ social environment and interactions have a significant influence on improving their financial literacy. They suggested including Islamic financial knowledge in the tertiary education curriculum, which should be in accordance with the education environment, values, and cultures. However, they did not elaborate on the scope and dimension of Islamic financial knowledge that the students should attain.

After examining nearly 4,500 young people aged between 25 and 34, De Bassa Scheresberg (2013) concluded that most youths lack fundamental financial knowledge. Certain demographic groups have poor financial literacy, that is, women, minorities, lower-income and less-educated people. Nevertheless, it is not guaranteed that a high level of education will result in having financial literacy. The study pointed out that people with higher financial literacy have better financial outcomes, that is, they are more likely to plan for retirement and keep aside savings for emergencies.

### Religious Awareness and Bankruptcy

Bursztyn et al. (2019) examined whether religious ethics have an impact on loan repayment. They have revealed that reminding the borrowers of religious ethics related to loan repayment has significantly reduced the procrastination of loan repayment and loan default among the Muslim borrowers in Indonesia. However, their study experimented with only one ethical principle of debt repayment related to the Muslim borrowers in Indonesia. Therefore, it motivates the researchers to conduct a similar study in Malaysia with a broader perspective of religious ethics.

Salwa and Ilhammie (2017) found that faith has a considerable effect on impulsive purchasing. The authors carried out a methodological analysis in which they argued that Islamic financial rules were not in line with
the consumer’s impulsive purchasing actions. Besides, they claimed that highly religious people have a lower propensity to become impulsive buyers. In contrast, individuals who are not religious are less unaware of their spending.

Amin et al. (2014) suggested a theory of Islamic consumer behavior to explain the factors influencing the Islamic mortgage industry. They revealed that religious satisfaction plays an important role when applying for an Islamic mortgage. Using Maqasid al-Shari’ah, they attempted to develop an empirical Islamic framework to predict customers’ behaviors in an Islamic house financing market.

Baele et al. (2014) found that religion plays a vital role in determining the loan default. After comparing the default rates of conventional and Islamic individual loans in Pakistan, they concluded that Islamic loans have lower default rates than conventional loans. Thus, religion motivates individual borrowers to repay loans.

Bensaid et al. (2013) reviewed Islamic jurisprudence literature to examine several fundamental concepts of indebtedness in Islam. They found that debt is not desirable in Islam as Muslims are encouraged to work hard to earn their living through legitimate means. Debt is not only a burden for a Muslim, but it will affect him in the Hereafter if the debt is not settled. Allah SWT cannot forgive debt obligation as it is the human being’s right (haqq al-‘ibad). Therefore, the complete clearance of financial obligation to the public is necessary as it may affect a person’s religious deeds. Muslims are taught to avoid over-indebtedness; therefore, they should be prudent in their spending and financial planning. However, giving loans to others and showing compassion to debtors are righteous deeds.

Khan (2013) discussed the Islamic theory of consumer behavior, which relates to the Muslim’s financial planning. He argues that consumers should avoid consuming on their desires according to Islam and should only consider their needs. There is a clear difference between need and desire. Human as a social animal has the power to judge what is needed for their well-being. Desires that do not meet the criteria of needs should not be fulfilled. There should be a priority list of needs for resource allocation. The most important need should be on top of the list, while the least important should be at the bottom. The ranking of needs should be based on the most significant for the person’s well-being. In this regard, Khan referred to al-Shatibi’s classification of needs: daruriyyat, kamaliyat, and tahiṣiniyyat.

Research Gap

Even though several studies have attempted to discuss IFL but most of the studies lack two aspects. Firstly, most of their discussions are usually generic and related to the knowledge of Islamic banking products are services. However, Islamic Shariah provides a comprehensive guideline of IFL, especially concerning debt management. These guidelines are not only for the borrowers but also for the creditors and the society at large. Secondly, most of the studies are lacking in developing the theory of IFL from the primary sources of Shariah. This study fills this gap by referring to the primary sources of the Shariah in their original language, that is, the Quran, the Sunnah and the classical literature of the four schools of Islamic jurisprudence.

Moreover, though some studies have been conducted on the impact of IFL on loan repayment in various jurisdictions, there is a gap in examining the IFL’s impact on bankruptcy avoidances and how it can be implemented in Malaysia.

Research Methodology

According to the research objectives, this study adopted a qualitative approach. Qualitative research is a type of study that examines data gathered through language and behavior in natural settings. It is employed to get expressive information that cannot be achieved in quantitative data, that is, beliefs, values, feelings, and motivations that shape the behaviors. It is often used for generating ideas for improvements (Berkwits & Inui, 1998; Qualitative Research Consultants Association, 2017). In the context of this study, the following two research methods were employed:

Library research: the construction of the theory of IFL for several classical Islamic works of literature in the field of Islamic jurisprudence were reviewed first in their original language, which is in Arabic. The sources of the Shariah can be divided into two types: (1) primary sources and (2) secondary sources. The primary sources are the Quran, Sunnah, Ijma, and Qiyas (Al-Zuhayli, 1986, vol. 1, p. 417). This study adopted an inductive approach to review the texts of the Quran and Sunnah to find any Shariah rulings related to debt, wealth management, and bankruptcy. After obtaining the related texts, the commentaries of the Quran and Sunnah are read for a better understanding of the texts. Moreover, this study reviewed the opinions of the classical scholars of Islamic jurisprudence from the four school of thoughts, namely Hanafi, Maliki, Shafi’i, and Hanbali. In addition, the manuscripts from the scholars starting from the ninth century have been reviewed to derive the Shariah rulings for debt, bankruptcy, borrowing and lending practices, and wealth management. Finally, information gathered in Arabic texts were translated by the researchers.

Semi-structured interview: semi-structured interviews were conducted after the library research to gather
opinions of the experts on whether IFL can be used in Malaysia to reduce bankruptcy among Muslims. Therefore, the researcher had selected Agensi Kaunseling Dan Pengurusan Kredit (AKPK) officials and Malaysia Department of Insolvency (MDI). AKPK was established by Bank Negara Malaysia, the central bank of Malaysia, to help individuals manage their finances and become prudent in financial management. In addition, it provides financial education and counseling and debt management programs to the public (Agensi Kaunseling Dan Pengurusan Kredit, 2017). Besides, MDI is a government agency that handles bankruptcy cases and affairs related to bankruptcy (Malaysia Department of Insolvency, 2013a, 2013b). Therefore, several top-level executives of the institutions, as mentioned above, were chosen for the interview using the purposive sampling method. The interviewees were chosen based on their vast experience in credit counseling, conducting credit awareness programs, educating financial management, and handling credit issues. The names of the interviewees were encrypted to protect their privacy.

Data collected through library research and semi-structured interviews were analyzed thematically. Thematic analysis is a procedure in which the data gathered are read multiple times to find the common issues and main themes that summarize all the opinions. This type of method is the most common in qualitative research projects (Brikci & Green, 2007; Fereday & Muir-Cochrane, 2006).

Finding’s Analysis

The findings of this study were analyzed in two steps. First, the findings of the library research were analyzed to address the first research question. Second, the interview data were analyzed to answer the second research question.

Islamic Financial Literacy Framework

The data gathered from library research were divided into three main themes: (1) Shariah guidelines for the debtor, (2) Shariah guidelines for Islamic financial institutions, and (3) Shariah guidelines for the society.

Theme 1: Shariah guidelines for the debtor. The Shariah guidelines motivate the debtor to be sincere in paying back the loans. It suggests that the debtor should avoid financial distress where loans should not be taken for luxurious activities, and the debtor should control his or her spending behavior. Some Shariah texts put great concern on the repayment of debt while describing debt as the right of a human where Allah will not forgive the wrongdoing if the creditor does not forgive the debtor. The motivation to repay the debt is highlighted when the prophet (pbuh) refused to pray the funeral prayer for a deceased whose debt was not settled. Moreover, the Shariah prescribes the punishment for the debtor who does not repay the debt. The following sections elaborate on the Shariah principles.

Subtheme 1: Discouragement of debt for luxury. The Shariah discourages incurring debts for luxury, which is the excess to needs. The Quran and Sunnah condemn the wastage of wealth, which is consuming wealth more than one’s needs. Allah says: “O children of Adam! attend to your embellishments at every time of prayer and eat and drink and be not extravagant; surely He does not love the extravagant” (Surah al-’Araf: 31). Although this verse specifically mentions the wastage of food and drink, it provides a general rule for the consumption of wealth. Similarly, Jabir ibn Abdullah narrated that: Allah’s Messenger (pbuh) said, “There should be a bed for a man, a bedding for his wife, and the third one for the guest, and the fourth one is for the Satan” (Muslim, Book: Libas wa al-zinah, Chapter: Karahah ma zada “ala al-hajah min al-firash wa al-libas, hadith no: 2084, vol. 2, p. 1002). This narration condemn the action of having an excessive number of accommodations which is more than one’s need. In the commentary of the Hadith, Al-Nawawi (1994, vol. 14, p. 83) mentions that whatever exceeds the need is for pride, show, and amusement of the worldly life. Whoever has this characteristic is reprehensible, and every reprehensible action is related to the devil.

The prophet (pbuh) used to pray to get rid of debt because it may lead to sins like telling lies. In another narration, the prophet (pbuh) used to pray: O Allah! I seek refuge from you from worries, sadness, disability, laziness, stinginess, cowardness, burden of debt, and oppression of people (Al-Bukhari, Book: Jihad wa al-siyar, Chapter: Ghaza bi sabiyin li al-khidmah, hadith no: 2893, p. 714). Laziness, cowardice, and other characteristics mentioned in the hadith are not desirable. Similarly, debt is not desirable in Shariah. However, people may borrow for their need, provided that it is not for luxurious purposes.

Subtheme 2: Controlling the spending behavior. Unwise spending behavior is one of the reasons for personal bankruptcy. In a study on the causes of individual financial stress in Malaysia, Adnan et al. (2021) found the inaccurate consumption pattern has a more considerable impact on personal financial stress. It generates a mystical component of financial pressure, which is seldom examined. Many Malaysian youths declared bankruptcy due to over-spending (Agensi Kaunseling Dan Pengurusan Kredit, 2014; Diana-Rose & Zariyawati,
The Shariah has provided principles for Muslims on how to consume wealth. First, the Shariah sets an objective for spending, which is fulfilling the needs but not desires. Second, it provided the priorities to fulfill the needs. Finally, it prohibited wastage (Hossain, 2014). After setting the goals for needs, a rational man should follow the hierarchy of needs. He should satisfy the top level of needs first, followed by secondary needs. In this regard, the Maqasid al-Shariah’s level of needs might be referred to (Khan, 2013). According to Maqasid al-Shariah, the needs are divided into three levels, which are daruriyyat, hajiyat, and tahsiniyyat. Daruriyyat is the needs that are indispensable for humans; such are food, shelter, and medication. Humans must satisfy this category of needs, and they could not sustain without daruriyyat. The absence of daruriyyat threatens the existence of humans. Therefore, Muslim consumers should satisfy this need first (Al-Shatibi, 1997, vol. 2, p. 18).

The second category of needs is termed hajiyat. A man can survive without hajiyat, but his life will be full of hardship, such as the lack of transportation (Al-Shatibi, 1997, vol. 2, p. 20). Therefore, after fulfilling the first level of needs, he should satisfy the hajiyat. However, if he has spent all his money satisfying the hajiyat, he should wait before fulfilling this need.

The third level is called tahsiniyyat. Tahsiniyyat completes the needs of a man. Anything that contributes to a person’s well-being comes under this category, such as cleanliness (Al-Shatibi, 1997, vol. 2, p. 22). This need should be chosen after fulfilling the first and second categories. It is not wise to spend more for this category before the first and second categories (Khan, 2013).

Subtheme 3: Putting great concern on repayment. There are several narrations in the Sunnah which place great concern for the nonpayment of debt. Some scholars viewed that it is a major sin to delay the debt payment even though the debtor has sufficient wealth (Hasan et al., 2017). The prophet said: “It is injustice for a deserving person to delay the payment of debt” (Al-Bukhari, Book: al-Hawalah, Chapter: al-hawalah wa hal yarji’u fi al-hawalah, hadith no. 2287, p. 547). In another narration, Allah SWT will forgive all the sins of a martyr except debt. “The martyr is forgiven all of his sins...except for his debts” (Muslim, 2006, Book: al-Imarah, Chapter: Man qutila fi sabili Allah kufirat khatayahu, Hadith no 1886, p. 912). Even though a martyr has a high rank in the sight of Allah, his debt is not forgiven. It is important to mention that it is against the guidelines of Shariah to use bankruptcy as a means to exploit and usurp the rights of others. A person cannot be free from debt just because he is declared bankrupt (Zada et al., 2015). Therefore, a Muslim needs to pay all the debts and meet the rights of Muslims in this world.

The severity of debt can be seen when the prophet (pbuh) did not pray for a person who passed away with the debt of two dinars:

On the authority of Jabir (RA), a person passed away, and we have bathed him, clothed him, and put fragrance on him and brought it to the prophet (pbuh) so that he prays for him. We have asked him: “Will you pray on him?” He took a few steps and then said, “Has he any debts?” We replied, “He has a debt of two dinars.” Upon hearing that, the prophet went away. His companion Abu Qatadah then took charge of the debt. We thereafter went to the Prophet and Abu Qatadah told him, “I would pay the two dinars.” The prophet then said, “The creditor’s right is guaranteed and the deceased is free from debt?” He said, “Yes.” The prophet then prayed on him (Ahmad bin Hanbal, 1998, Book: Musnad Mukatthirina min al-sahabah, Chapter: Musnad Jabir bin Abdullah, Hadith no. 14590, p. 1017).

This prophetic narration depicts that even though the prophet used to love his companions, he did not perform prayers when their debts were not settled. This incident highlights the severity of this issue. When one of the prophet’s companions took charge of the debt, the prophet prayed for him. Although the previous prophetic narrations were warnings by mouth, this narration was the strong action of the prophet (pbuh) in setting an example for the Muslims on settling the debt before performing the funeral prayer.

Subtheme 4: Punishment for a solvent debtor. Along with the punishment in the Hereafter, there is the worldly punishment for a solvent debtor. When a person intentionally procrastinates to fulfill the debt while having the ability to pay it, the person is considered unjust and worthy of punishment in this world and the Hereafter. The prophet (pbuh) said: “Procrastination by the solvent debtor deserves a punishment and his dignity is compromised”(Abu Dawud, 1997, Book: al-Aqdiyah, Chapter: al-Habsu fi al-dayn wa ghayruhu, hadith no: 3628, vol. 4, p. 31). Hasan et al. (2017, p. 91) mentioned that based on the Hadith, Shariah scholars unanimously agreed that the solvent debtor could be imprisoned for denying the debt payment. The solvent debtor should be arrested and imprisoned until the debt is settled. Referring to the prophetic narration, Muslim jurists also remark that it is allowed in the Shariah to force the debtor to pay his debt using hash words.

Theme 2: Shariah guidelines for Islamic financial institutions. Using equity-based contracts by Islamic
financial institutions is another step to minimize bankruptcy. In equity-based financing, that is, musharakah and mudarabah, the financial institution and the client share the profit and loss (Mirakhor & Zaidi, 2007). If the client takes the financing to increase the working capital of his business and faces loss, the financial institution should share the loss with the client. In this case, the client should not be bankrupt. Unfortunately, most Islamic financial institutions rely heavily on debt-based financing to minimize their risks (Abdul-Rahman & Nor, 2016; Dar & Presley, 2001; Farooq, 2017). This approach ultimately leads to many bankruptcy cases. Even in some cases, when equity-based financing is used, Islamic financial institutions put many terms and conditions on the clients, which changes the equity feature of the contract to debt. For example, the customer is considered as defaulted and declared bankrupt when he does not want to proceed with the musharakah contract in the Musharakah Mutanaqisah home financing. However, musharkah is not a binding contract in the Shariah. Any partner in a musharakah contract is permitted to opt out of the alliance at any time (Abdullah, 2016).

Apart from this, Islamic financial institutions need to make their utmost effort while evaluating the client’s creditworthiness. Bankruptcy may happen due to poor examination of the client’s creditworthiness (Akkizidis & Khandelwal, 2008, p. 109). Therefore, it is the responsibility of the respective financial institution and its financing officer to establish the appropriate solvency status for the client. The prophet (pbuh) warned us in this regard that “Every one of you is a shepherd and is responsible for his flock” (Al-Bukhari, 2002, Book: al-jum’ah, Chapter: al-jum’ah fi al-qura wa al-mudun, hadith no. 893, p. 217). Similarly, Islamic financial institutions should be responsible while marketing an Islamic financial product. It is not acceptable for an Islamic financial institution to persuade a client to take financing beyond his financial reach. Instead, the golden rule should be followed, which is “treat others as you like to be treated.”

This principle can be comprehended through this prophetic narration: “None of you will have faith until he loves his brother what he loves for himself” (Al-Bukhari, 2002, Book: al-iman, Chapter: min al-iman an yuhibbu li akhihi ma yuhibbu li nafshihi, hadith no. 13, p. 13–14). Therefore, the financial institution should put itself in the client’s shoes while marketing a financial product to determine whether they can afford their product. In addition, with the advancement of technology, mudarabah-based equity crowdfunding can be operationalised to avoid debt for raising the necessary funds (Ishak & Rahman, 2021).

**Theme 3: Shariah guidelines for the society.** Islam prescribed zakah, a mandatory charity for the rich to donate 2.5% of their wealth to eight types of recipients (Bakar & Rahman, 2007; Dhar, 2013). The debtor is among the eight types of recipients. The following verse describes the recipients of zakah:

Zakah expenditures are only for the poor and for the needy and for those employed to collect [zakah] and for bringing hearts together [for Islam] and for freeing captives [or slaves] and for those in debt and for the cause of Allah and for the [stranded] traveller—an obligation [imposed] by Allah. And Allah is Knowing and Wise (Al-Quran, 9:60).

In the verse, Allah SWT declares that zakah can be given to a person in debt and does not have any means to fulfill his commitment. The Arabic term used in the verse is al-gharim which means, according to al-Qurtubi (2003, vol. 8, p. 183–184), the one who is overburdened with debt and undoubtedly is not able to pay it. Therefore, if a person has some wealth but is not enough to pay his debt, he is considered al-gharim. Besides, a person who does not have any wealth to pay back the debt is called faqir (poor) and gharim (indebted) at the same time. However, the Shariah stipulates that the debt taken should be for halal purposes, for instance, buying a house and paying medical bills (Shawish, 2015).

Besides zakah, voluntary charities such as sadaqah and waqf (Ibrahim, 2008, p. 5) can be given to the indebted person who cannot fulfill his debt. On the other hand, Bensaid et al. (2013) recommend that the Muslim society pays for the children who inherited debts from their parents and remove other types of financial difficulties from them. Therefore, the society’s role cannot be overlooked in this matter. The following hadith shows an example of the situation:

Imam Muslim recorded from Abu Sa’id al-Khudri (RA) that a person faced a loss in his fruit business and his debt is extended. The prophet (pbuh) told them, “Donate for him”. Then, the people started to donate for him. However, their donation did not fulfill all the obligations. The prophet (pbuh) told the creditors: “Take whatever you have got and you do not have more than that” (Muslim, Book: Musaqah wa al-muzara’ah, Chapter: Istihbab al-wad’ min al-dayn, Hadith no: 1556, vol. 8, p. 731–732).

The hadith explains that Muslims are encouraged to make voluntary donations to remove the debtor’s burden when a debtor is in genuine difficulty. In the present-day context, crowdfunding initiatives can be taken to collect donations to help those who are overburdened with debts due to genuine reasons. Alternatively, Islamic financial institutions may establish a cash waqf fund to help people who are overburdened with debt due to valid reasons. However, there should be criteria to prove that the person is in genuine difficulty so that others do not abuse the facility.
Another way of removing bankruptcy is for a Muslim to pay the debt of his Muslim brother. As discussed in the hadith narrated by Jabir, a person had passed away, and the prophet (pbuh) did not perform the funeral prayer for him. After that, Abu Qatadah took charge of the debt, and the prophet (pbuh) prayed for the deceased. The bankruptcy can be removed through donations from fellow Muslims.

Regulators’ Perception on Implementing Islamic Financial Literacy

To achieve the regulators’ perceptions on implementing IFL, we had interviewed four top executives in AKPK and MDI. Data obtained from the interviews are presented under two themes: (1) the importance of IFL, and (2) the application of IFL.

Theme 1: The importance of Islamic financial literacy. None of the respondents denied the importance of financial literacy in reducing Muslim bankruptcy. IV1 specifically mentioned that IFL should be included in their program modules. She believes that this kind of knowledge can positively encourage debtors to behave responsibly regarding their unnecessary spending. She states the following:

I think we should add Islamic financial literacy especially our prophet’s message on debt. We must add these kind of literacy in our modules especially for the attitude of our people on borrowing and getting debts for buying unnecessary things and developing Islamic concept on borrowing loan process. (IV1)

According to IV1, non-Muslims are interested to know about the features of the Islamic loan process. She highlighted that the Islamic framework would impact the people more positively and motivate them to reduce bankruptcy.

IV2 equally acknowledged the importance of IFL. However, IV2 added that literacy itself is not enough, and Muslim debtors have to change their attitude and financial behavior.

In our opinion, knowledge of Islamic financial literacy to minimise bankruptcy is important for Muslim to avoid from being declared bankrupt but that alone is not sufficient. It must go hand in hand with ones’ own attitude and discipline towards effective financial [management]. (IV2)

Furthermore, IV3 emphasized that generally, financial literacy, including IFL, became very important in higher education. Elaborating on the point, she mentioned that our financial literacy texts should include weighing the pros and cons of financial decisions based on whether they would be harmful or not.

Citing AKPK (2018), IV4 suggested that Malaysian adults should be equipped with sound financial knowledge to develop good financial habits. Based on her research, there was a positive relationship between financial knowledge and financial behavior. Malaysian adults who have superior financial knowledge scored higher in the financial behavior score, while those who scored poorly in financial knowledge had lower financial behavior score. Furthermore, there was a positive relationship between the levels of financial knowledge and financial well-being, further confirming the importance of acquiring financial knowledge. Thus, financial education is critical to enhancing financial well-being.

In line with the above findings, Biplob and Abdullah (2019) confirm that IFL is a crucial element to improve the financial behaviors of Muslims because it discourses unnecessary debts, disciplines the spending behavior and encourages savings and Shariah-compliant investments. Moreover, Bursztyn et al. (2019) concluded that some elements of IFL help reduce the procrastination of loan repayments and loan defaults.

Theme 2: The application of Islamic financial literacy. None of the respondents indicated that any kind of IFL framework is being practised in their organizations. However, they mentioned that some general awareness and counseling programs are being implemented. AKPK and MDI conduct awareness programs, whereas AKPK alone operates some counseling, management, and education programs.

AKPK has three main services: (1) financial counseling, (2) management program, and (3) financial education program. Under the financial counseling program, individuals are offered a one-to-one counseling service for financial matter. The management program offers counseling to manage the debt payment procedure. The financial education program is designed to help young adults aged 18 years old or above. This financial education program is offered at four stages: (1) when the students enroll in the university, (2) when they are in the final year in the university and are ready to enter the workplace, (3) when they start working, and (4) when they are about to retire (IV1). IV1 informed that these modules are not necessarily based on Islamic financial literature. For example, in the fourth module, they offer some guidelines for zakah payment, the concept of Islamic and conventional product, and ideas of insurance and takaful, but the module framework is not entirely developed based on Islamic financial literature.

Concerning the implementation of IFL in their awareness program, IV1 mentioned that it is suitable to include IFL in their existing teaching module. It is fine with the
non-Muslims to make a better financial decision. She states the following:

Yes, we can put one chapter in our current curriculum. It would be better for awareness of the people, even non-Muslim also may have interest with these principles, and they can separate what is right and wrong. Moreover, we can add the source of Zakat and others. We should focus on their spending behaviour. (IV1)

Similarly, IV4 indicated the importance of practising IFL. She suggested that financial literacy from different perspectives should be developed to improve the financial behavior of Malaysians. Referring to AKPK (2018) survey, she states the following:

An infrastructure to continuously enhance financial knowledge must be developed. Over the long run, serious efforts to improve the financial well-being among Malaysians is anticipated to have a positive impact on our society. A multifaceted approach to inculcate good financial behaviour and enhance financial knowledge must be taken in order to move more Malaysian adults into the elated level of financial well-being. (IV4)

Regarding the implementation of IFL awareness, IV2 suggested that it be implemented via mass media and social media. IV2 asserted that the IFL is important for both Muslims and non-Muslims, as well as bankrupts and solvents. So, the mass media and social media platforms should be utilized here. IV2 states the following:

Islamic financial literacy awareness can be implemented widely via media such as television, radio, newspaper, including social media as we are of the view that the knowledge of Islamic financial literacy is important for all, whether Muslims or non-Muslims, bankrupts or non-bankrupts. (IV2)

It can be concluded from the above findings that all of the informants support the idea of implementing IFL for bankruptcy avoidance and consequently improving the financial well-being of the people. Moreover, they suggest using mass media and social media to create awareness of IFL. In this regard, Sari et al. (2022) emphasized that media and technology are essential tools for improving IFL among school students. Moreover, Anwar (2021) affirms that media can improve the IFL of the people where the internet and android software are the two valuable tools for creating awareness among the young generation.

**Theme 3: Implications for Islamic financial institutions and zakah institutions.** IV1 mentioned that Islamic financial institutions and zakah institutions have a role in implementing IFL. It is observed that in some cases of default, Islamic financial institutions treat their clients worse than conventional banks. When a customer defaults, the Islamic banks sometimes impose the customer on paying back the principal and profit. For instance, if a customer’s principal is 40,000, the bank will ask the customer to pay the debt with a profit of 80 thousand. Thus, Islamic banks may create an extra burden on the clients and consequently contribute to clients’ bankruptcy.

Furthermore, IV1 pointed out that zakah institutions play a very important role in implementing IFL and, consequently, reducing the number of bankruptcies. Therefore, Zakah authorities should collaborate with Islamic financial institutions for this cause. However, it is a challenge to engage zakah with Islamic financial institutions as zakah authorities are independent authorities in each different state in Malaysia.

Based on the above findings, it can be resolved that the regulators in Malaysia also believe that Islamic financial institutions and zakat institutions have essential roles to avoid bankruptcy cases. Islamic financial institutions are suggested to take care of the welfare of their customers who are facing difficulties to repay their loans. Moreover, it is timely that zakat institutions should consider the people overwhelmed by debts as their beneficiaries. Mohammed Ali Bani Ata (2019) also emphasized on zakat fund and the consideration of the financial institutions to address the bankruptcy cases. Raza Rabbani et al. (2021) also put forward similar suggestions.

**Conclusion**

**Summary of the Findings and Contributions**

This study has developed a comprehensive theory of IFL based on the primary sources of the Shariah, which was missing in the existing literature. IFL provides a set of principles and guidelines for the debtor, creditor, Islamic financial institutions, and society to minimize bankruptcy cases. Concerning the debtor, the Shariah discourages a person to assume loans for luxuries as debt should be taken to fulfill needs. Delaying the payment of debt for a solvent debtor is termed a major sin. In order to avoid the burden of debt, Shariah provides a guideline to stop unwise spending. From the lender’s perspective, Shariah recommends the lenders either extend the deadline or forgo a portion or the entire debt when the debtor is in difficulty. With respect to Islamic financial institutions, they are suggested to provide equity-based financing to clients. For the Muslim society, along with voluntary charity, the Shariah prescribes zakah, a compulsory donation might be given to a person who cannot pay his debt.

The regulators in Malaysia also affirm that IFL can be helpful to minimize bankruptcy cases for Muslims and non-Muslims. IFL is crucial to improve the behaviors and attitudes of the borrowers as well as controlling
the spending behavior. Even though IFL is not practised in Malaysia’s current credit awareness programs, they believe it can be practised for bankruptcy avoidances and enhancing financial well-being. They have further suggested that the zakah management authority and Islamic financial institutions may play a significant role in implementing IFL for reducing bankruptcy cases.

**Theoretical and Managerial Implications**

This study recommends the central bank and related credit awareness agencies include Islamic debt principles in their credit awareness programs. Islamic financial institutions should practice genuine profit-sharing financing. Moreover, a collaboration between the central bank and zakah management authority is expected to distribute zakah among financially over-burdened people. Moreover, Islamic financial institutions may jointly establish a cash waqf fund to help the bankrupt.

**Limitation and Future Research**

This is a qualitative study to develop the theory of IFL and to explore the perception of the regulators on its importance and mechanism of implications in different credit awareness programs. Further study should be conducted on analyzing the impact of IFL on the borrowers’ behavior. Besides, research should be conducted on how Islamic financial institutions and zakah management authorities can collaborate to help the bankrupt.

**Author Note**

This research was conducted while Muhammad Nazmul Hoque was at Accounting Research Institute, UiTM Shah Alam, Malaysia. He is now at Faculty of Accountancy, Universiti Teknologi MARA Cawangan Selangor, Kampus Puncak Alam, 42300 Bandar Puncak Alam, Selangor, Malaysia and may be contacted at nazmul@uitm.edu.my.

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**ORCID iDs**

Md. Faruk Abdullah https://orcid.org/0000-0002-9111-1755
Muhammad Nazmul Hoque https://orcid.org/0000-0003-0432-5569

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