

## DEVELOPING A HAWALAH MODEL FOR ISLAMIC CAR FINANCING SETTLEMENT

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**Abstract:** As revealed by Malaysia's bankruptcy statistics between 2019 until May 2023, around 11.05% of bankruptcy in Malaysia is due to default of vehicle loan. This has led to the tightening up of vehicle loan underwriting and increased vehicle loan rejection rates. This paper attempts to solve this problem by proposing an Islamic contract transfer of debt; al-Hawalah as an alternative to reduce the number of defaulters in Islamic car financing. This study is an exploratory research using content analysis from the secondary data by observing on two aspects: car financing insolvency data and the Hawalah contract. In fiqh muamalat, *hawālah* refers to the transfer of financial liability from one debtor to another that would free the initial debtor from any debt (Kureshi and Hayat, 2014). This study is expected to come out with a Hawalah model for car financing settlement in Islamic bank.

**Keywords:** Transfer of debt, al-Hawalah, Car Financing

### 1. Introduction

Hawalah denotes "change" or "transfer" in Arabic (Wilson, 2002: 2). A debt transfer from the transferor to the payer is what the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) (2010) defines as al-Hawalah. Al Hawalah is the term used in fiqh muamalat to describe the transfer of debt from one debtor to another that would release the original debtor from all obligations (Kureshi and Hayat, 2014). The Hanafis define al Hawalah as a transfer of responsibility for a debt from the debtor to the party named as responsible for the obligation in the contract. (Al-Zuhayli, 2003). Additionally, the Mejelle's Article 673 specifies the Hawalah principle as a "transfer from one debtor account to the debtor account of another." (Kureshi and Hayat, 2014: 153).

In modern banking, instruments such a bill of exchange, promissory note, cheque or overdraft frequently use the Hawalah contract (Al Raisi et al., 2016; Kureshi and Hayat, 2014). It refers to transfer of debts from the transferor or the original debtor to the payer (Accounting and Auditing Organization for Islamic Financial Institutions, 2010).

In current, there is no application of hawalah in car financing settlement in Malaysian banks. The common use of Hawalah is for remittance of money. The issue of car financing raise concern when it becoming the third higher number of default in loan. Based on the Department of Insolvency Malaysia between 2019 until May 2023, 11.05%, or 3.810 cases, of bankruptcies recorded in the country were related to vehicle purchases. These statistics from a

report by the Insolvency Department, which also revealed the other reasons for bankruptcy.(Jabatan Inslovensi Malaysia, 2023).

Age-wise, individuals between 35 and 44 years old made up 38.44% of all recorded cases during the period, while those between 25 and 34 years old made up 18.52% of the total.

The researcher aims to develop a car financing security model to help car financing defaulter from being bankrupted through Hawalah contract model. This feature of product among others will transfer the liability of defaulter to the eligible payer after the agreement was concluded between all parties.

## 2. Literature Review

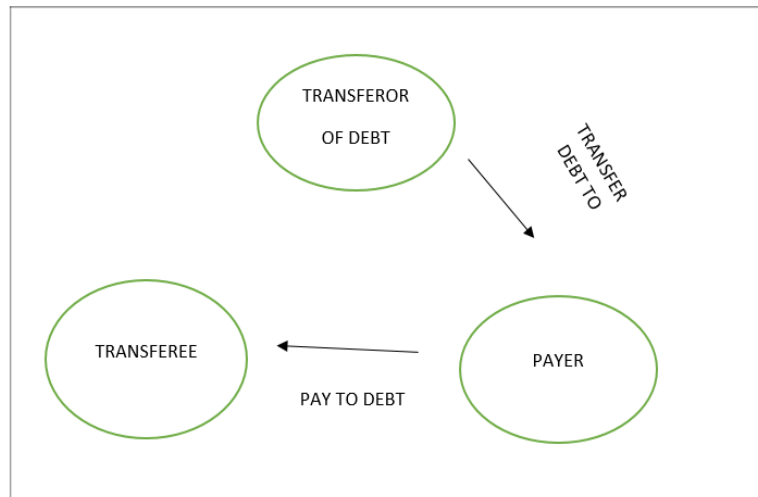
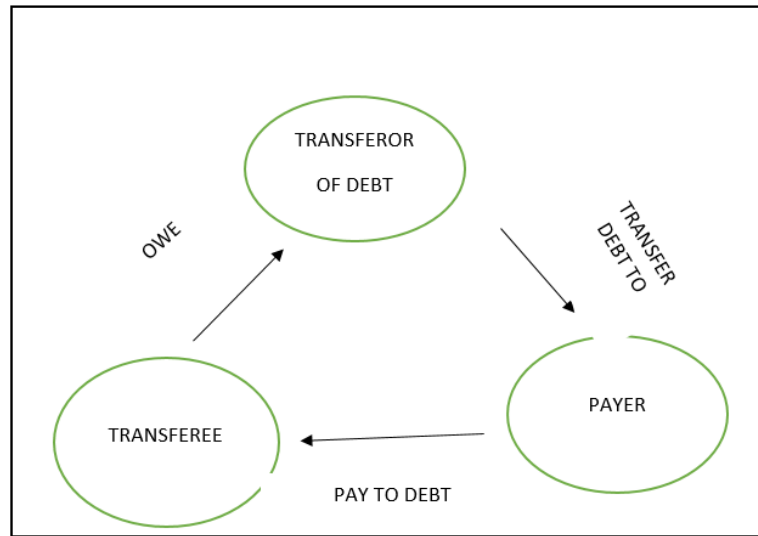
The translation from Arabic to English can often result in words with the same meaning being spelled differently. This is the case when it comes to ḥawālah (AlZuhayli 2003), which may be written as hawala (Maimbo, 2003), hawalah (Haqqi, 2011) and hiwalah (International Shari'ah Research Academy for Islamic Finance, 2012).

It's interesting to note that some academics refer to the Hawalah as an Informal Value-Transfer System (IVTS) (El Qorchi et al., 2003; Passas, 1999; van de Bunt, 2008). According to Viles (2008), anything of value can be transferred in Hawalah in addition to money. According to Maimbo (2003), al Hawalah "refers broadly to money transfer mechanisms that exist in the absence of or in parallel to, conventional banking channels" (page v). The phrase is merely used to describe different remittance systems in other research like Viles (2008) and Jost and Sandhu (2000).

The Transferor, Transferee, Payer, Debt, as well as the Offer and Acceptance, are the five pillars of 'Hawalah,' according to International Shar'ah Research Academy for Islamic Finance (ISRA) (2010). The individual who was the initial debtor is referred to as the transferor, while the creditor and the party who agrees to be paid through the transferor's debtor are referred to as the transferee.

Next, the Payer refers to the party accepting the liability that will be collected by the transferee, whereas the Debt refers to the subject of the transfer. The legitimacy of the ḥawālah contract is based from the Qur'an, the Sunnah, Ijma' and reasoning as established by AAOIFI in its basis for the Sharī'ah ruling. However, the conditions of ḥawālah differ among and between Sharī'ah schools, namely Ḥanbali, Mālikīs' and Shafi'i. More specifically, the juristic views differ with regards to the consent of parties, liabilities involved and on termination of the contract (AlZuhayli, 2003).

There are two types of ḥawālah: the restricted and the unrestricted model. Diagram 1 illustrates the restricted model, where the payer owes a sum of money to the transferor and the transferor owes a debt to the transferee. The transferor can elect to transfer the payer's debts to the transferee in order to settle the debt.



The concept of *awlah* is widely applied in both formal and informal financial systems in the modern financial period. The notion of '*awlah*' has been widely incorporated into modern banking services, including bill of exchange, promissory note, checks, remittance, and bank draught, as stated by Kureshi and Hayat (2014). Additionally, it is a procedure that can be applied to the book transfer settlement of overseas accounts.

Indonesia's Propindo Islamic Cooperative is a famous instance of a Hawalah-based lender. It can be used in the trading industry where Islamic Financial Institutions (IFI), particularly Islamic microfinance institutions, are involved. Cooperative is an autonomous Islamic cooperative that was founded by a number of small business owners in Jakarta, Indonesia to offer hawalah-based finance (Dewi and Kasri, 2011).

In light of the fact that SMEs often receive paid for the commodities they supply within 1-3 months, the cooperative aims to provide additional operating capital for their SME members. At the same time, the SME needs enough working cash to keep up production while awaiting the partner's payment. For SME, ensuring the sustainability of their firm comes with additional burdens. The Cooperative therefore offers Hawalah-based finance to address the issue. (Maryam Sofia Mohd Suhaimi, Maryam Syamilah Md Fauzi, Nadiana Noryatim,

Norashikin Mohd Noh, Nursyamimi Shuhaimin, Qurratulain Jaafar, Siti Maspuah Maulan, Zati Fatini Johan, Aishath Muneeza, 2016)

There is no literature on using Hawalah contract in car debt settlement. Commonly used for Hawalah contract is to transfer money from one country to other country. This exploratory research attempts to propose contract Hawalah for car financing settlement.

### **3. Methodology**

This paper has a specific focus on car financing, and thus other modern applications of ḥawālah in the international finance and trade are not examined. This is an exploratory study which based on secondary sources such as articles, journals and books were used particularly in the study of ḥawālah as a transfer of debt system. Exploratory research is often used when the issue is new or when the data collection process is challenging for some reason.

### **4. Discussion and Analysis**

Buying a car in Malaysia is a rather straightforward process, especially if you're looking at more affordable models like the Perodua Axia or Proton Saga. Thanks to low (or even no) down payments and lengthy loan periods, the majority of people can purchase an automobile. But maintaining that purchase is a totally different story.

Based on insolvency data from 2019 to April 2023, 11.11 % of the bankruptcy is derived from car loans. According to the Insolvency Department of Malaysia, one of the top four reasons for bankruptcy in Malaysia is a car loan. That typically occurs when a borrower recognises they are unable to make their vehicle loan payments and default on the loan. While it is simple to start the process of buying an automobile, the buyer must maintain discipline to make the ongoing monthly payments.

What transpires then if the customer discovers they are unable to make vehicle loan payments? The buyer runs the danger of having the bank that funded their loan seize their vehicle.

However, it doesn't always have to occur right away if you skip one payment. It is advisable for the buyer to get clarification from their bank because different banks have varying repossession terms. It can be after the second or even third missed payment.

Having said that, the banks go through a number of different steps when they act to seize your car.

#### **4.1 Car repossession rules in Malaysia based on the Code of Ethics for Repossession**

The following items have been clarified from Public Bank's Code of Ethics. Remember that the codes of ethics for various banks will vary.

When doing the repossession activity, permission holders must make sure their permits are both current and valid. Time allowed for repossessions is only permitted everyday from 9 a.m. to 9 p.m. Permit holders having a repossession order from the owner shall only enter a property with the occupant's knowledge and permission. Private property owners cannot permit trespassing without obtaining a court order. Permit holders who receive a repossession order

from the owner must act politely and presentably. They should make sure that they carry out their work with decency and professionalism. Using "strong-arm tactics" of any kind is absolutely forbidden when doing their jobs.

At the time of repossession, the permit holders should:

- Show the hirer his permit, national registration card, and a standard notice with the name, address, and phone number of the authorised officers he/she can contact right away to solve any issues.
  - Allow the hirer a reasonable amount of time to inspect the vehicle or commodities and remove his personal property.
  - Take pictures of the interior and outside of the car or the products and give them to the rightful owner.
  - Request the issuance of an inventory list outlining the location and state of the seized goods or vehicles.
1. If at all possible, the repossession of the vehicle or other commodities should be done in the presence of the hirer or another person who has permission to use them.
  2. As soon as it is practical, ideally within 24 hours of the repossession, a police report should be filed. In extreme cases, the report should be filed no later than 48 hours after the repossession.
  3. When carrying out their repossession activities, permit holders who have been given a repossession order by the owner must always operate in compliance with the laws, rules, terms and conditions, code of ethics, and guidelines established by the Controller.
  4. Permit holders should also follow any additional Codes of Ethics or Guidelines that the Controller may issue from time to time.

The customer cannot let getting their automobile repossessed deter them; it's a dreadful situation to be in. If anything, it's a terrific chance to learn what NOT to do to reduce the likelihood that this sad incident will recur in the future.

#### **4.2 How Can Customer Avoid Car from Repossession?**

Since customer's financial situation is the root of the issue, speaking with the bank is the next natural step. If possible, the customer can restructure the auto loan. If a person and his bank can come to an agreement, they might adjust his monthly payments and/or lengthen the loan to lessen his load. Banks are not required to review customer's finances, though. Therefore, if they are unwilling to assist, then the negotiation is done. The next best course of action is to sell the car before it reaches the stage of repossession if the bank declines to modify monthly payments and the customers are unable to pay the full amount owed. However, selling car is not something that can be done in a single day or even in a single night, therefore the customer has to ensure having enough time to get rid of it and pay off the bank loan.

If none of these options appear feasible, paying off debt on schedule is the best way to stay out of this position. It's important to keep in mind that if the owner has paid off more than

75% of their auto loan, banks cannot seize the vehicle. The customer needs a court order to do that. Customer is responsible for the legal fees and expenses necessary to repossess and retain your vehicle, which is another minor but significant point.

#### **4.3 Car repossession can affect person in more ways than one**

The customer won't just lose the automobile; having it repossessed will also impact his credit score and can make it more challenging to get loans or credit cards in the future. As absurd as it may sound, keeping these consequences in mind will help motivate to keep sending money in on time.

To make the required monthly payments on a hire buy loan for a car, one must be disciplined. It is crucial to do extensive planning and math up front to determine whether a person can actually afford an automobile.

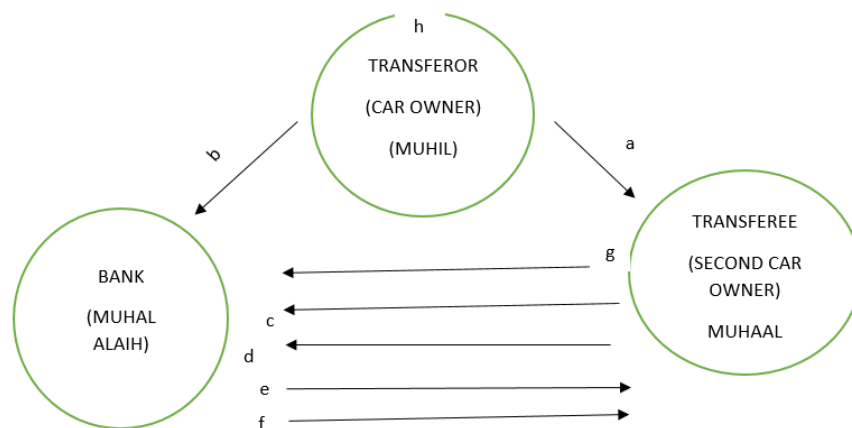
### **5. Recommendation and Conclusion**

This study attempt to propose a Hawalah as car financing debt settlement for those who has financial problem in paying car financing. Current practice in Malaysia for car financing default is through car repossession by the bank which may cause for probability of insolvency if the car owner cannot pay the remain balance. The worth thing is, the car is auctioned to other buyer and let the first owner with debt liability. But there is other thing worsen when the name of the defaulter is blacklisted in Bank Negara Malaysia system which may cause them barred from opportunity to get financing from any financial institution in the future. Hence, they have to face three worst things: the loss of car, the payment of the rest balance and the name being blacklisted. The researcher observes that this thing can be avoided through Hawalah contract.

#### **5.1 Hawalah Model for Car Financing Settlement.**

This contract involves three parties namely, the transferor, the transferee and the bank.

- a. Firstly, the transferor finds the transferee and agree among them to transfer the debt.
- b. Second, the transferor (Car first owner) introduce his transferee to the bank.
- c. The bank review the transferee financial record.
- d. After satisfy with the financial record of transferee, the bank approves the transferee to make settlement on the remain balance either by full settlement or by instalment.
- e. If the transferee chooses to pay the remain balance by cash, then the bank shall calculate all the financing amount remains and the transferee obliges to pay the amount.
- f. The ownership of the car will be transferred to the transferee (the second owner) after completion of the remain financing as agreed between the transferor, transferee and bank.
- g. If the transferee chooses to get financing from the first bank or other banks, then, the approval must be confirmed prior any transfer of the first debt.
- h. The first owner is secured from his liability on his car financing after the completion of the transaction between transferee and the bank.



## 5.2 Conclusion

As revealed by Malaysia's bankruptcy statistics between 2019 until May 2023, around 11.05% of bankruptcy in Malaysia is due to default of vehicle loan. The car owners have to face three worst thing: the loss of car, the payment of the rest balance and the name being blacklisted. The customer won't just lose the automobile; having it repossessed will also impact his credit score and can make it more challenging to get loans or credit cards in the future. The researcher observes that these things can be avoided through Hawalah contract.

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