

THE 268TH SHARIAH ADVISORY COUNCIL OF THE SECURITIES COMMISSION MALAYSIA MEETING (11 MAY 2023)

EXTENSION OF THE APPLICABILITY OF THE DEBT RATIO IN THE RESOLUTION ON SHARIAH SCREENING METHODOLOGY FOR UNLISTED MICRO, SMALL AND MEDIUM ENTERPRISES (MSMEs)

INTRODUCTION

The Shariah Advisory Council (SAC) of the Securities Commission Malaysia (SC) had, in several meetings, deliberated on the SAC resolution on the “Shariah Screening Methodology for the Unlisted Micro, Small and Medium Enterprises (MSMEs)” which was resolved at the 244th SAC meeting held on 20 May 2021.

It was resolved that the applicability of the financial ratio benchmark for total debt over total assets (Debt Ratio) in the Shariah screening methodology for the unlisted MSMEs will be revised from less than 49 percent to less than 33 percent after two (2) years from the date of the issuance of the Shariah Screening Assessment Toolkit for unlisted MSMEs (collectively “Toolkit”) which was on 5 August 2021.

Pursuant to the above, the issue in deliberation was whether the benchmark for the Debt Ratio should be revised to less than 33 percent on 6 August 2023 or to extend the period on the applicability of the Debt Ratio of less than 49 percent.



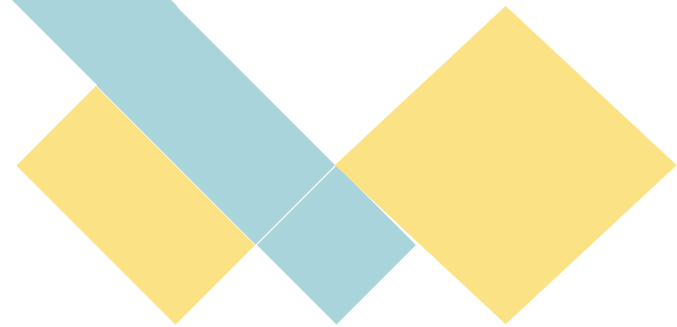
RESOLUTION

The SAC had, at its 268th meeting held on 11 May 2023, resolved that the benchmark of less than 49 percent for the Debt Ratio will be extended for another three (3) years from 6 August 2023.

SHARIAH JUSTIFICATION

The permissibility of the above SAC resolution on the less than 49 percent benchmark for the Debt Ratio in determining the Shariah status of the MSMEs together with the extension of the applicability of the Debt Ratio is based on *maslahah* (public interest) and *hajah* (need) which is supported by the following justifications:

- (1) Some of the Shariah scholars opined that *maslahah* and *hajah* can be used as the basis and consideration in determining an Islamic ruling and it is an exception from the general ruling.
- (2) The benchmark for the Debt Ratio of less than 49 percent that is determined for MSMEs can be supported by the Shariah scholars' views on *qadr al-hajah* (level of the need) whereby certain rate can be determined in the context of mixture of *halal* (permissible) and *haram* (prohibited) in someone's wealth based on the estimation of the need or *hajah* depending on the situations during a period of time and to avoid the abuse of the concept of *hajah* itself.



(3) To facilitate the growth of MSMEs industry from two perspectives as follows:

(i) From companies' perspective, it is to facilitate the growth of more Shariah-compliant MSMEs in the future due to the nature and background of the MSMEs which includes:

(a) MSMEs have limited knowledge about ICM or Islamic finance particularly on the technical knowledge in relation to funding since their focus are to run business;

(b) Most MSMEs are in form of sole proprietorship; and

(c) The rationale for the implementation of such Debt Ratio for two (2) years and to be extended for another three (3) years from August 2023 is to educate, create and increase awareness to the MSMEs in relation to ICM.

(ii) From investors' perspective, they do not have control over the management of the MSMEs including the method of fund raising either through Shariah-compliant or conventional mechanism. Hence, for MSMEs that comply with such benchmark and be classified as Shariah-compliant, it will provide opportunity for Islamic investors to invest in such MSMEs with limited knowledge and exposure in ICM or Islamic finance. Even though MSMEs involve in the element of *riba* through conventional funding, such element does not relate with the income to investors thus the income received by Islamic investors is considered as Shariah-compliant income.