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Insolvency and bankruptcy based on Islamic principles within China – a data-driven analysis and framework

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Abstract

Islamic bankruptcy law and finance have taken on a growing role in modern economies, with several governments aiming to align the economic system with Islamic principles and solve some of the shortcomings of existing financial regulations related to bankruptcies. Within the last 40 years, China has become a major economy with significant development of its legal system. With the increasing growth and engagement with the Muslim world, challenges have arisen with speculative business practices and rising defaults. Furthermore, the growing engagement with Muslim countries has fostered a growing focus on providing Shariah-compliant legal frameworks to encourage trade and ensure the protection of corporations. Insolvencies and bankruptcies are natural in an economy. However, Islam emphasizes the importance of there being no distinction between balance sheet insolvency and cashflow insolvency, as well as the importance of personal responsibility for the debts incurred. The article has presented a solid outline of the Islamic and Chinese bankruptcy laws and how Islamic principles can be integrated into the Chinese legal system. The arising system in the form of either a separate legal system or one integrating these principles into the existing bankruptcy regulations can significantly strengthen debtor responsibility and recovery rates and encourage fairer business practices.

Keywords: Bankruptcy law; Islamic Law; Chinese Bankruptcy law; data-driven analysis; bankruptcy framework

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1. Introduction

Insolvencies and bankruptcies are a natural part of any economy, ensuring that resources are best utilized and that businesses in distress or those not viable have an exit strategy.

Bankruptcy and insolvency in Islamic law are well covered. The Arabic word *Iflas* refers to bankruptcy and covers both balance sheet insolvency in addition to income and cashflow statement insolvency. In the case of a balance sheet insolvency, the entity's assets are less than its liabilities. Given the equality of the asset side and the liabilities and stockholder equity, this implies that the stockholder equity has to be negative (Jan, et al., 2019). The income statement or cashflow insolvency is when the entity does not have sufficient liquidity or monetizable assets to cover the debt that comes due. The associated Arabic word *muflis* refers to a bankrupt entity irrespective of whether it refers to a male or female person or an enterprise. The challenge is that once one becomes a *muflis*, then one either has to fully repay all the debts that are unforgiven or face death.

The main text relating to bankruptcy is the Quranic verse 2:280, which emphasizes that for any person in distress, there should be respite until the person recovers. Furthermore, it emphasizes that one should not boast about forgiving debt but rather see it as a sign of gratitude. This puts social responsibility and charity at the heart of Islamic law, but given that it is solely a recommendation, it has to be seen in the light of other Quranic verses that compel Muslims to repay debts. Not repaying makes this a sin and not just a legal obligation (Ismal, 2012).

This implies that both creditors and debtors are compelled to be honest, ensure fairness, and fulfil their contracts. The prophet emphasized that without a just cause, delaying the payment of a debt or an obligation is unjust. Debt is frowned upon for Muslims based on ethical and moral perceptions. Specifically, there have been comments by the prophet that emphasized that one's soul will be suspended with debt and freed only upon the repayment of all debt (Jan, Marimuthu, Shad, Zahid, & Jan, 2019).

2. Literature Review

Islamic bankruptcy law and Islamic financial law are closely related. These two are connected in terms of economic equality and social responsibility. This means that the scriptures mandating Muslims to do charity immediately follow the ones declaring that all types of riba are prohibited. A strong heavenly need to be benevolent and compassionate is intertwined with lending and repaying. Additionally, the fixed idea that money is only a medium of trade and a storage method with no inherent worth affects both ideas (Kilborn, 2011).

This implies the consistent insurance of fair treatment and the punishment of economic hardship caused the inability of a debtor to fulfil their obligations. Another key part is that Islamic law does not equate to the discharge of debts within Islamic rule. The main reason for this is that Muslims are supposed to fulfil their obligations and promises and should not rely on charity or the benevolence of others unless necessary. Furthermore, this aligns with the lack of interest in money or the increase in debt over time, so the debtor may have sufficient time to settle their debt. This implies that the amount of debt, in both real and economic terms, goes down over time, requiring an individual to pay back the debt at any time in one's life. This requires Muslims to fulfil their promises and obligations to God and man (Devi & Firmansyah, 2018).

This suggests that Islamic law's core normative principles—no discharge and societal responsibility—are crucial to its application. The primary distinctions are entity shielding, the time and risk worth of money, and intangible and non-possessive assets and rights.

When looking at the time value of money, this is commonly measured via the inflation rate, which indicates the opportunity cost of having control over and the use of the money within the specified period. On the other hand, the risk value is considerably more complex, consisting of the risk of not being paid back and not being paid for circumstances outside the scope for which it was provided. The latter risk is not considered in Islamic law, given that money may be quantified as either a commodity or be regarded as a universal unit of exchange.

A critical part of Shariah law is that no value is attached to the ability to utilize money. Riba states that being paid back the nominal amount is unethical and sinful. The main difference is that in Islamic finance, the time value of tangible assets is different from that related to inflation alone and consists of the asset's market value. For example, precious metals as commodities are permitted to increase in value. This supports the harmonization of repayment obligations and bankruptcy requirements (Ata, 2019).

Another key aspect is that in Islamic law, the charging of interest on money is rejected. However, entity shielding and forms of limited liability partnerships have never been incorporated into Shariah law and corporate forms never developed in Islamic law. Personal and economic activities must be conducted via direct proprietary ownership or one of the nominated forms of partnership.

Non-possession liens and security interests were not included in classical Islamic law. Property rights are restricted, and personal possessory liens are only recognized in common contexts. There is an exception, which concentrates on the ability to demand the seller recover items that a debtor was never given on credit for or that were not paid for (Jan, Marimuthu, bin Mohd, Isa, & Shad, 2019).

Notably, numerous Roman rules, which did not appear in English common law until the 15th century, were integrated into Shariah law. The usufruct of real estate and leaseholds (Ijara) was recognized by Shariah law, and shared ownership through a partnership was allowed.

Individuals who have more debt than assets or whose current expenses are more than their current incomes are referred to be muflis. This suggests that there is no difference between insolvency on the balance sheet and insolvency on the liquidity front. The temporal value of money and intangible assets are not considered in sharia law because it is assumed that tangible goods may be sold easily. This suggests that there is no need to differentiate between an asset and cash flow shortages since the debtor's assets may be utilized to pay off the obligations.

This suggests that when a debtor defaults after the creditor requests payment of the obligation, the debtor becomes a muflis. Islamic law grants both men and women the complete legal power to enter into contracts, possess property, generate money, and inherit, hence the rules are the same for both sexes. Businesses are subject to the same rules, and there is no difference between company and individual bankruptcy. Given that Islamic law did not create the idea of limited liability companies, the majority of economic interactions were in the form of partnerships and joint ventures (Awad & Michael, 2010; Hermawan, Sari, Biduri, Rahayu, & Rahayu, 2023).

This suggests that an organization's liabilities are the debts of each owner or partner in a partnership. One must distinguish between the various kinds of partnership structures to address this further. The most typical type is an inan partnership, a restricted investment vehicle with restrictions on the project's scope and lifespan. This suggests that the sum each partner contributes to the partnership is a component of the partnership's assets. The partnership does not own any of the other properties. The partners are each personally responsible to third parties but are not each other's guarantors. It follows that the third party must request payment directly from the partner with whom they have negotiated. After paying the claim, the partner is then permitted to ask the other partner for contributions (Graham, 2011).

No debt that exceeds the agreed-upon assets of the partnership may be assumed by the partners. The other partner is not responsible for anything beyond the initially agreed-upon contribution to the partnership fund if one of the partners incurs one of these debts without permission. If the partnership becomes liable for debt above its assets due to unforeseen circumstances (such as a partner's death), and none of the partners have voluntarily taken on the excess obligations or debt, then the other partners will be responsible for making up the shortfall by their interests in the partnership. Although it is possible to distribute earnings excessively, liabilities cannot be treated in the same way (Islam, Semeen, & Farah, 2013; Serra, Lemos, & Matins, 2021).

Another sort of partnership is a mufawada partnership, in which the parties to the agency contract operate as one another's and the guarantors' agents. The capital investment and profit-sharing responsibilities of each partner must be distributed equally. Any liabilities not met by the mufawada assets are jointly and severally accountable by all of them (Awad & Michael, 2010).

Similar to earlier, if an obligation requires one of the partners to contribute more than their personal investment in the mufawada assets, they can ask the other partners for repayment. The other partners are not responsible for unlawful behavior, theft, or any other duties that are solely personal or not related to the partnership. Marriage, divorce, and exclusively personal assurances for other parties can all result in these duties.

One of the most significant partnerships where one partner may only provide finance and other resources is the Mudaraba partnership. There are no constraints on the type of funding used; the mudarba was first intended to support caravans and marine trade. The Mudaraba structure is meant to restrict the investors' responsibility to their initial investment. In the traditional mudaraba, the mudarib (manager) accepts the rabb al-mal's (investor's) cash under the terms of the contract and distributes a portion of the earnings to them for the mudarib's services. The contract specifies the percentage of share (Kilborn, 2011).

The mudaraba differs from a limited partnership in that the investor maintains technical administration while maintaining legal ownership of their contributed funds. This develops a concept in Shariah law that differs in that the asset's owner is not a buyer, lessee, or agent. This suggests that the investor is solely responsible for any losses. However, personality liability is conceivable if the management goes beyond their scope of responsibility. Credit may be used up to the stipulated capital; any additional credit acquisitions require specific authorization. If not, they risk being held personally accountable.

All relationships must end at the partner's will, death, insanity, or destruction of the capital to be considered valid under Islamic law. A mufawada relationship is also dissolved if the partners sense an imbalance in their respective financial interests, such as when one spouse contributes more to the repayment of debts than the other. Additionally, receiving property as part of the partnership as a gift or inheritance might lead to an imbalance. Additionally, if one partner falls bankrupt, the other partners' assets cannot be managed or sold, which might endanger the partnership. As a result, the requirements for insolvency for a person are identical to those that apply to partnerships (Steele, et al., 2018).

According to Islamic law, bankruptcy procedures are started by the creditor who asks the judge to order encumbering or distaining the debtor. The creditor is responsible for providing documentation of the debt and its due date. If the court finds enough assets to cover the obligation, she or he will order that the payments be made without infringing on the debtor's rights. However, if the debtor must be restrained while the court examines the debtor's solvency, the debtor's assets will essentially be frozen until the court issues another order. Distraint orders are quick preliminary injections that prevent debtors from controlling, selling, or encumbering assets.

The creditors' rights are connected to the debtor's property, and the debtor is not allowed to sell or manage the property, two of the four legal repercussions that follow the distraint order. Additionally, the creditor is entitled to more money than the other creditors, and the debtor's assets are sold to pay off the obligations (Jan, Marimuthu, Shad, Zahid, & Jan, 2019).

The creditors' rights are attached to the property, which provides the legal authority for the distraint order. This implies that the person in distraining is regarded as like a minor, insane or incapacitated person. The court then appoints a person of trust (rajul thiqah) to deal with the assets and the business affairs of the bankrupt entity. This then will wind down the affairs of the debtor, gather and value all the assets and then liquidate the assets.

If the other debts of the debtor are not due, then the distraint order will not accelerate the due date of the debt. This is based on the argument that the debtor is entitled to additional time to satisfy the debt at the due date. If it is not due, then no inclusion in the bankruptcy proceedings is warranted.

The liquidation is happening in an auction-like setting to ensure that the highest price is realized. Similarly, the rajul thiqah is appointed to take responsibility for the fulfilment of open contracts and the operation of the business as long as the creditors agree.

When it comes to the rights of the creditors, the creditors and debtor have the option to settle the debt. This leads to the withdrawal of the request for the distraint of the debtor. This enables both the debtor and creditor to enter negotiations and settle the respective claim. Such a settlement resolves any disputes and leads to an end of the litigation. Generally, settlements are highly recommended in Islamic law given the strong focus on social harmony. The settlements can be divided into two separate ones. The first type is the settlement where the debtor denies the claim. This is a situation where the person claims from the debtor a debt but does not possess cognizable proof of the claim. Such a settlement is based on a compromise to avoid litigation, but the creditor has to ensure that the claim is valid and in good faith. There are discrepancies in terms of whether such claims are accepted (Jan, Marimuthu, bin Mohd, Isa, & Shad, 2019).

The second kind of settlement is one in which the debtor acknowledges that he owes the claim while the creditor asserts a right. The creditor then agrees to a compromise in which a smaller payment is made to instantly resolve the claim. Whether such a settlement is legal depends on the legal school, and if the creditor willingly gives up his claim to the debt, the settlement should be viewed as a gift.

The creditors can be classified into receivers, reclamation creditors and lessors. The receiver is the first in line to receive the fees, expenses, and other compensation for the management of the bankruptcy proceedings. This includes transportation expenditures, notices to the public, and any other associated expenditures related to the operation of the business. The fees can be forfeited by the receiver if desired.

Given that the debtor is in possession of their property, the reclamation creditors are ranked second in priority. The creditor has the option to keep the asset or divide it with other creditors. However, five conditions must be met to reclaim the property. The debtor must still be alive when the creditor asks for the restoration of the property, which is the first requirement. The creditor forfeits the right to demand the return of the property if the debtor dies before it is done. After the property has been liquidated, the creditors must band together and divide the proceeds according to their individual debts. The second element is that the property has to be in the same state as when the creditor sold it to the debtor.

This implies that the property shall be undestroyed or undamaged. The third element is that the property of the creditor is possessed or controlled by the debtor. If the debtor sold, gifted, or pledged it, then the creditor solely joins the other creditors in proportion to the debt. The fourth element is that in the case that the debtor paid an instalment or downpayment, then the creditor does not have the entitlement to take back that property. There is the option to pay back the money the creditor has received in return for the property or share proportionally the debt. The fifth element is that if the property value increases or transforms into one with added value, then the creditor either joins existing creditors or takes the property back to the original state (Ata, 2019).

Lessors come in third, with a lease known as Ijara being the main recognized intangible asset. Therefore, the lessor has the right to revoke the agreement and seize his property if the lessee-debtor declares bankruptcy, provided that the lease date has not yet begun. The lessor is also a creditor for the unpaid rent if the lease term has already ended. The lessor is not allowed to terminate a lease that has already started, and the lessee-debtor is the only owner of the property. Additionally, the usufruct is a component of the bankrupt debtor's assets, and the unpaid rent is one of the requests made by the creditor (Graham, 2011).

The next party is the secured creditor, who has precedence over the collateral. Creditors who have a secured interest come next. Other than the lessor's ownership right, many intangible assets and rights are not recognized under classical Islamic law. As a result of this understanding, the owner of real property is now allowed to draw up a contract that creates the residual ownership rights up until the debt is entirely repaid, cementing the distinction between ownership and possessory rights. The Murabaha is a term used to describe such a deal. The Rahn, a real possessory pledge, is the only vehicle left after Murabaha and Ijara. Considering this, a creditor who has pledged collateral is entitled to reimbursement from that collateral (Steele, et al., 2018).

The protection of family assistance and appropriate living expenditures from creditors is a crucial aspect of Islamic law. For the wife, kids, and parents, this includes both clothing and food, and there should be enough money to live on. Usually, the house is protected from creditors so that the family has a place to live.

The creditor can follow the debtor into their company to see if there are any assets that can be sold and prevent their travel, or they can ask for the muflis to be imprisoned until all debt is paid (Awad & Michael, 2010).

Imprisonment or enslaving debtors has a long history, but Islamic law distinguishes between those debtors experiencing a force majeure and those willingly default. Those that can demonstrate that they do not have the funds but are willing to pay their debts, will not be imprisoned. There may be a limited prison sentence to determine the credibility and veracity of the claims of the debtor. The duration of such imprisonment will depend on the judge (Devi & Firmansyah, 2018).

The second approach is to permit the creditor to follow the non-paying debtor to determine whether there is any property that may be liquidated. This also implies that the creditor can publicly announce that the debtor owes a debt and may not be a person of trust.

Finally, the debtor may be restricted from travelling outside the town or city to prevent the debtor from dissipating or hiding the assets. Travel may be permitted based on reasonable grounds, such as health, pilgrimage, family obligations and other associated circumstances. If the debtor cannot pay the debt in question and this can be validly confirmed, then the travel restrictions cease.

3. Methodology

China has a unified and comprehensive bankruptcy system that covers all types of enterprises., including foreign investment vehicles and state-owned enterprises. China does not have a personal bankruptcy law. The key concepts within bankruptcy law are voluntary and involuntary bankruptcy and an independent administration. Furthermore, the creditors are heavily involved in administrating the bankruptcy, restructuring, and settlement (Jiang, 2013).

Additionally, the principle of extraterritoriality applies to all properties outside China and potentially voidable transactions. A major component of the legislation relates to protecting workers' rights whose claims rank ahead of the unsecured creditors but behind any secured creditors.

The Chinese bankruptcy law consists of 136 articles that are separated into 12 chapters and apply to any type of insolvent enterprise, irrespective of whether it is state or privately owned and includes financial institutions as well as foreign investment enterprises. The law does not apply to individual natural persons. Hence, regulations concerning individual natural persons are separate from the Chinese bankruptcy law, but there is currently no personal bankruptcy law that individuals can refer to. Additionally, the legislation solely applies to PRC entities but also incorporates the debtor's overseas properties (Rapisardi & Zhao, 2010).

An insolvency test has to be conducted to determine whether bankruptcy is permitted. Qualifying for bankruptcy, restructuring or settlement requires that the enterprise cannot meet its debt obligations and that the assets do not cover the liabilities or can pay off debts.

To commence the proceedings for bankruptcy, an application in the People's Court where the enterprise is domiciled is needed. This can be initiated by either the creditor or the debtor. However, if the debtor is a financial institution, then regulatory authorities under the State Council have to file such an application.

The court assigns the case to a bankruptcy administrator as soon as the bankruptcy application is accepted. The administrator may be a recognized member of any legal, accounting or specialized bankruptcy firm or has the necessary relevant professional expertise and qualification. Both the selection and the remuneration are determined by the Supreme People's Court (Parry & Long, 2020).

These administrators are reporting to the People's Court and are supervised by the creditors. Specifically, the meeting of the creditors can replace the creditor if needed or request the removal of the administrator in case the duties are not performed accordingly. Specifically, if the administrator does not act lawfully and impartially, or if the administrator may not perform the duties competently, then there may be a removal (Mrockova, 2021).

The administrator has several powers and duties, such as taking control of the debtor's property, seals and accounting records, documents and any other material. Furthermore, the administrator investigates and reports the financial status of the debtor. Additionally, decisions are made related to management and daily expenditures.

The administrator also decides on the continuation or suspension of the debtor's business operations and the properties' management and disposal. The administrator also represents the debtor during litigation, arbitration and associated proceedings, and presides over the meeting with creditors and any other necessary functions.

If the administrator fails to act with due diligence and care, then the administrator may be subject to personal liability or face fines. This arises if the administrator caused the loss to a creditor, debtor or any additional third party.

An important part of the claim filing is that the creditors have only a limited period to commence proceedings against the debtor. This period commences with the date of the publication by the People's Court upon the acceptance of the bankruptcy petition and the period has to be between 30 days and three months (Tomasic & Zhang, 2012).

These claims include the debts arising at the bankruptcy application date and any unmatured debts. Additionally, any conditional debts, time-limited debt obligations, and any claims arising from pending litigation and arbitration. Finally, indemnity obligations and damages under a contract are included, in addition to the debt owned by joint creditors.

The creditors have the right to get information and participate in the process through creditors' meetings and committees for creditors. This entitles the creditor to both attend and vote in the meeting. This requires that the claim is determined and accepted. Any resolutions of the meeting are taken by a simple majority of the voting rights, and the majority has to be at least 50 % of the value of the debtor's unsecured debt. The meeting is also responsible for verifying the claims of the creditor and applying to the court for the replacement or removal of the administrator. Furthermore, the meeting also supervises the administrator and selects the committee members. Additionally, it decides on the suspension or continuation of the business operations and approves any restructuring or settlement agreements. Finally, both the management and distribution of the properties of the debtor are handled by the meeting (Arsenault, 2011).

4. Results

An important part of the bankruptcy process is that any creditor that has debts to the debtor may request that the claims are set off against their claims. However, if the creditor incurred the debt knowing that the debtor cannot cover their debt, then this is not permitted.

Any contracts before the bankruptcy application's acceptance and not fully performed can be terminated or continued based on the administrator's judgement. However, the administrator has to notify the counterparties of the decisions within two months after the acceptance or 30 days after receiving a reminder. If this is not performed, then the contract will be terminated. When the contract is continued, the counterparty has the entitlement to a guarantee by the administrator. Failure to provide will terminate the contract as well.

Following this establishment of contracts, the priority of debt cover is determined. This incorporates bankruptcy expenses and common interest debts that are incurred after the acceptance of the bankruptcy petition. Furthermore, employee claims, and social insurance premiums in addition to outstanding taxes are to be reimbursed. Finally, unsecured claims in bankruptcy are to be covered. If the bankruptcy does not satisfy the discharge requirements, then the allocation will be done on a pro-rata basis. This implies that secured creditors generally prioritise the value of the secured properties, and any shortfalls of these amounts are treated as unsecured claims.

Rescue options play a critical role in Chinese bankruptcy laws, and the Bankruptcy Law permits the debtor and creditors to apply for restructuring or reorganization of the business. The legislation permits a compromise or settlement of the debts even if the bankruptcy application was accepted already (Lin, 2018).

The debtor has to submit a draft restructuring plan to the court and meeting of the creditors within six months after the court permits the restructuring request. Within the restructuring period, the debtor may apply for approval from the court to manage the properties and business under the administrator's supervision.

The voting groups are classified by the type of creditor. The first group are those with secured claims of the specific properties. The second group incorporates employees with claims on salaries and medical/disability subsidies. Furthermore, creditors subject to outstanding taxes and common claims are separate voting groups.

4. Discussion

The growing diversification of the Chinese economy and active engagement with many Muslim countries has presented a considerable opportunity for China to pivot new forms of finance adhering to Islamic principles and integrate more readily the systems of these countries. Given the growing trading and economic relationship, Islamic bankruptcy principles may provide both a domestic and international opportunity for fairer financial transactions and responsible business practices. Recent large-scale bankruptcies such as the HNA group, the economic struggles of the Evergrande group and other real estate developers that went into bankruptcy, such as Risesun Real Estate Development Co., Ltd. with more than 37 billion USD in liabilities, represent significant challenges (Goldberger & Vague, 2021). In several of these instances, excessive leverage and the shielding of the assets of the owners are major cornerstones of these instances.

The number of bankruptcies in China has increased significantly within the last several years. As demonstrated in Figure 1, the number of bankruptcies has increased from around 3,000 per year to more than 10,000 within the last four years. This significant increase makes sound bankruptcy proceedings essential and ensures that creditors are protected and the businesses engage in sound business activities. While increasing bankruptcies are caused by a variety of factors, such as economic hardship and growth restrictions, bankruptcy-supporting regulations may cause corporations to prefer to declare and get rid of their debt, instead of the owners supporting the corporation and focusing on repaying the loans to creditors.

To integrate Islamic bankruptcy principles within Chinese law, there are generally two options. The first option is to integrate Islamic principles into general bankruptcy law with a particular focus on ensuring that the concept of limited liability is restricted to ensure greater responsibility of decision-makers. The second alternative is to create a separate bankruptcy law based on Islamic principles and apply this to specific Islamic entities.

Integrating Islamic bankruptcy principles into Chinese bankruptcy law may be in various forms. The first and foremost option for integration is the abolishment of interest paid on outstanding debts. Given that an enterprise or partnership is in distress, the charging of interest on the debt will make it harder for the corporation or managing individuals to recover and repay these amounts. Furthermore, they may be encouraged to actively seek to repay debtors and be prudent in their business activities. Conventionally, the increasing debt amounts arising from interest puts the defaulting entity under massive strain and will make the debtor more likely to try to default as compared to attempting to find an amicable solution and pay off the debt. Specifically, debts should generally not be forgiven unless the individuals want to make a good deed. If the debtor is in real hardship due to circumstances that are beyond his control, then debt forgiveness if the credit-bearing entity can afford it, should be encouraged. In return, the creditor may receive a preferential mention and positive support from the government. Furthermore, if a debt is forgiven, the debtor should be obliged to contribute to charity or support others as a condition for any debt relief by creditors. This is explicitly emphasized by Islamic principles of doing good and supporting society.

The second approach is to establish an Islamic bankruptcy law that adheres to Islamic principles and applies to Islamic-compliant corporations. The benefit of such an approach is that it would encourage the formation of a strong Islamic financial system, and also enable foreign enterprises to set up Islamic-compliant entities that adhere to their faith. Furthermore, it creates a dual system with separate legal forms that may be easier to be implemented and can be in conjunction with a strong Islamic financial regulatory system. This helps in strengthening the Islamic finance system within China and encourages its growth may align with the objectives of the government for greater common prosperity and sound financial management.

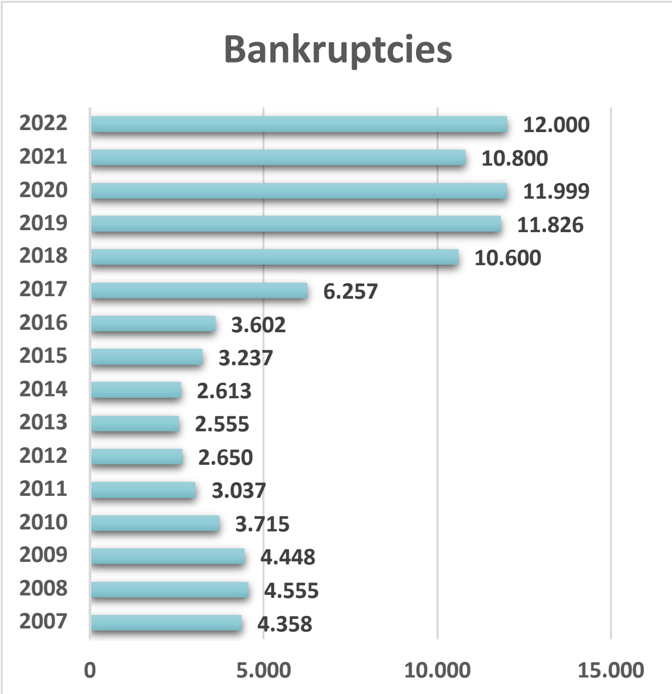

Figure 1: Chinese business bankruptcies from 2007 to 2022 (source: World Bank).

5. Conclusion

Islamic bankruptcy law and Islamic finance have taken on a growing role in modern economies with several governments aiming to align the economic system with Islamic principles in addition to solving some of the shortcomings with existing financial regulations related to bankruptcies. China has within the last 40 years become a major economy with significant development of its legal system. With the increasing growth and engagement with the Muslim world, challenges have arisen with speculative business practices and arising defaults. Furthermore, the growing engagement with Muslim countries has fostered a growing focus to provide Shariah-compliant legal frameworks to encourage trade and ensure the protection of corporations.

Insolvencies and bankruptcies are natural in an economy. However, Islam emphasizes the importance that there should be no distinction between balance sheet insolvency and cashflow insolvency, as well as the importance of personal responsibility for the debts incurred.

The article has presented a solid outline of the Islamic and Chinese bankruptcy laws and how Islamic principles can be integrated into the Chinese legal system. The arising system in the form of either a separate legal system or one integrating these principles into the existing bankruptcy regulations can significantly strengthen debtor responsibility and recovery rates, as well as encourage fairer business practices.

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