

BRIDGING INSTITUTIONAL GAPS IN ZAKAT DISTRIBUTION FOR FINANCIAL RESILIENCE: ADDRESSING RISING INDEBTEDNESS IN ISLAMIC FINANCIAL INSTITUTIONS

^{1*} Siti Mazlita Yamaludin, ² Mohd Rahim Khamis, ³ Sharifah Faigah Syed Alwi, ⁴ Mohd Suffian Mohamed Esa, ⁵ Azman Ab. Rahman

¹ Faculty of Business and Management, Open University Malaysia

² Faculty of Business and Management, Universiti Teknologi MARA, Malaysia

³ Arshad Ayub Graduate Business School, Universiti Teknologi MARA, Malaysia

⁴ Institute of Islam Hadhari, Universiti Kebangsaan Malaysia, Malaysia

⁵ Faculty of Syariah and Law, Universiti Sains Islam Malaysia (USIM), Malaysia

*Correspondence:

Siti Mazlita Yamaludin, e-mail: mazlita@oum.edu.my

History:

Received : 6.4.2026

Revised : 18.5.2026

Accepted : 23.6.2026

Published: 30.9.2026

Cite as:

Yamaludin, S. M., Khamis, M. R., Syed Alwi, S. F., Mohamed Esa, M. S., & Abd. Rahman, A. (2026). Bridging institutional gaps in zakat distribution for financial resilience: Addressing rising indebtedness in Islamic financial institutions. *Journal of Fatwa Management and Research*, 31(3), 189–209. <https://doi.org/10.33102/jfatwa.vol.31no3.864>

Funding

The study was funded by Universiti Teknologi MARA under the Geran Insentif Penyelidikan (GIP) (600-RMC/GIP 5/3 (003/2023). The authors also extend their appreciation to all stakeholders and participants who contributed to this study.

Abstract

Indebtedness has become a growing socio-economic concern in Malaysia, exposing limitations in conventional income-based approaches to identifying financially vulnerable individuals. Within Islamic social finance, this raises an important question regarding how zakat for asnaf gharimin (genuine debtors) can respond to increasingly complex and situational forms of financial distress. This study examines how gharimin eligibility and zakat allocation are conceptualised and facilitated through institutional collaboration between zakat institutions and Islamic Financial Institutions (IFIs) in Malaysia. Using a grounded theory approach, qualitative data were collected through in-depth interviews with zakat officers, academicians, IFI practitioners, and debt agency representatives, complemented by document analysis. The findings reveal three interrelated dynamics: situational asnaf, whereby temporary financial shocks create context-dependent eligibility; institutional and governance mechanisms, where Shariah principles interact with contextual judgement in determining eligibility; and conflict-of-interest concerns within IFIs, requiring a balance between ethical governance and institutional financial roles. Integrating these findings, the study develops a Strategic Solutions Framework for Gharimin, offering a substantive theory that shifts zakat allocation from a fragmented, poverty-centred approach towards an adaptive and institutionally coordinated model. Its originality lies in integrating situational asnaf classification, Shariah-governed needs-based prioritisation, and data-driven institutional coordination within a zakat-specific framework. Theoretically, the study extends the conceptualisation of gharimin beyond static poverty classifications, while practically, it provides guidance for zakat institutions and IFIs to improve the identification, prioritisation, and support of financially distressed individuals through more responsive and ethically governed allocation mechanisms.

Keywords: *Indebtedness, Gharimin (Genuine Debtors), Zakat Distribution, Islamic Financial Institutions (IFIs), Grounded Theory.*



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INTRODUCTION

In recent years, rising indebtedness among individuals and financing recipients has emerged as a significant socio-economic concern, particularly following economic downturns and global crises such as the COVID-19 pandemic, with implications for financial vulnerability within the Islamic financial ecosystem. The disruptions have significantly impacted the financial resilience of individuals across all income segments, including the B40, M40, and, in certain crisis situations, T20 groups which resulting in increased financial distress and debt vulnerability (Sulaiman, 2020). As Shariah-compliant financial institutions, IFIs may contribute to institutional efforts aimed at supporting financially vulnerable debtors within the Islamic social finance framework.

Zakat, an obligatory charitable contribution in Islam, which provides financial assistance to eligible recipients, including gharimin who are unable to repay legitimate debts due to financial hardship. The Qur'an explicitly identifies eight categories of zakat recipients (asnaf) in Surah al-Tawbah verse 60, each representing distinct forms of financial vulnerability. Among these, gharimin (debtors) refers to individuals burdened with legitimate debts and unable to fulfil their repayment obligations. Unlike fuqara' (the poor) and masakin (the needy), which are directly associated with income insufficiency, gharimin represents a separate category rooted in debt-induced financial distress.

Although poverty and indebtedness are often interconnected, the category of gharimin may encompass forms of debt-related financial vulnerability that can affect individuals across different income levels, particularly in situations involving financial hardships, economic shocks, medical emergencies, or essential financial commitments. In such contexts, zakat allocation to gharimin serves not only as a form of financial relief but also as a strategic intervention to restore financial stability, preserve economic dignity, and facilitate reintegration into productive socio-economic life. However, despite the recognition of gharimin as a legitimate category of zakat recipients under Shariah, allocation for this group often remains comparatively limited within current zakat distribution practices, particularly when compared to more traditionally prioritised categories such as fuqara' and masakin (Ab Rahman et al., 2022; Ibrahim & Sahrim, 2019). In Malaysia, where the zakat management system is highly structured and decentralised across state religious authorities, the challenge is further compounded by bureaucratic fragmentation, limited data integration, and inadequate coordination between zakat bodies and IFIs. As a result, many deserving gharimin continue to face structural barriers in accessing zakat support, including inconsistent eligibility assessments across states, limited integration of debtor information, fragmented coordination between zakat institutions and IFIs, and continued reliance on traditional income-based poverty indicators that may overlook debt-induced financial distress. These challenges highlight the need for a more strategic, data-driven, and institutionally collaborative approach to zakat distribution.

LITERATURE REVIEW

Zakat and Gharimin in Islamic Finance

Within the Islamic financial system, zakat functions as a formalised mechanism for socio-economic redistribution, operating alongside other instruments of Islamic social finance. While its foundational principles are well established, scholarly discourse has increasingly shifted towards examining how specific asnaf categories are interpreted and operationalised in

contemporary contexts. In this regard, gharimin (genuine debtors) represents a category that warrants deeper analytical attention due to its evolving nature within modern financial systems. Historically, Islamic scholars have recognised gharimin as individuals burdened by lawful and necessary debts incurred for legitimate purposes such as essential living needs, basic livelihood survival, or permissible business activities, provided that the debtor demonstrates genuine financial incapacity and the debt does not arise from extravagance, negligence, or prohibited activities.

Classical jurists conceptualised this group within a moral and socio-economic framework, emphasising that debt must arise from permissible (halal) and necessary purposes. Scholars such as Al-Ghazali (1997) and Ibn Qudamah (1968), underscored that zakat assistance to gharimin serves not only to settle outstanding liabilities but also to restore personal dignity and prevent long-term socio-economic exclusion. Expanding this perspective, Yusuf al-Qaradawi (2009) framed zakat for gharimin as a form of social rehabilitation, aimed at enabling individuals to regain financial stability and re-engage in productive economic activity.

Importantly, the classical treatment of gharimin establishes it as a distinct category of financial vulnerability, separate from income-based poverty represented by poor (fuqara') and the needy (masakin). This distinction is critical, as indebtedness may arise across different income classifications and is often triggered by situational or structural factors rather than chronic income insufficiency. As such, the inclusion of gharimin within zakat distribution reflects a broader conception of socio-economic risk that extends beyond poverty alone.

In today's financial landscape, the relevance of gharimin has grown significantly. Contemporary gharimin may experience financial distress arising from diverse forms of debt, including education financing, housing obligations, healthcare expenses, micro-business financing, and selected consumer-related liabilities. These debt burdens have become increasingly significant in post-pandemic Muslim societies, where economic disruptions, inflationary pressures, and rising living costs have intensified financial vulnerability across different socio-economic groups. Consequently, the category of gharimin has become more prominent within contemporary zakat discourse. Nevertheless, these forms of debt are not assessed uniformly under zakat eligibility, as qualification depends on several Shariah-based considerations, including the legitimacy and necessity of the debt, the debtor's actual financial incapacity, the purpose of the financing, and the absence of prohibited or excessive expenditure.

Given this reality, recent scholars such as Haron et al. (2021) and Yamaludin et al. (2023), highlight that the rising burden of personal and business debt in Muslim-majority countries calls for a rethinking of zakat distribution frameworks. This study argues that a more strategic, data-informed, and systematic approach is necessary to improve zakat allocation for gharimin within increasingly complex contemporary financial environments. Within this broader ecosystem, IFIs may contribute in supportive capacities through mechanisms such as wakalah zakat arrangements, referral coordination, and financial data sharing. Haron et al. (2021) highlight that IFIs have the potential to support broader financial inclusion strategies through wakalah zakat mechanisms, where they function as zakat distribution agents under the supervision of state zakat institutions. Due to their access to customer financing records and repayment information, IFIs may assist zakat authorities in identifying individuals who potentially qualify as gharimin.

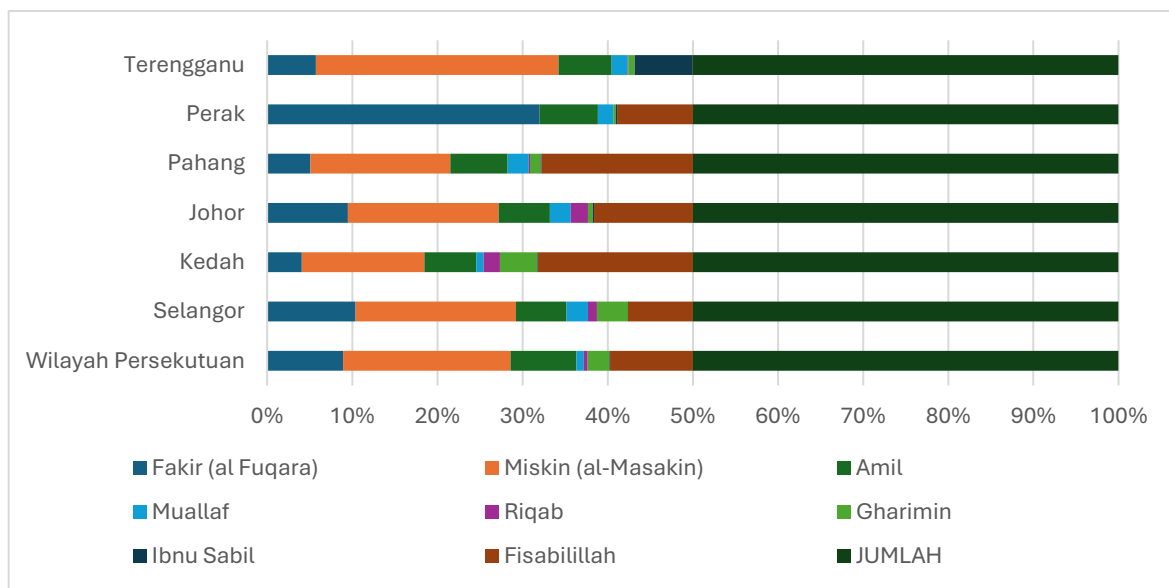
Nevertheless, the authority to determine zakat eligibility and approve distribution remains under the jurisdiction of State Islamic Religious Councils (MAIN) and official zakat institutions. Despite these institutional possibilities, current practices continue to reveal significant implementation gaps. In many jurisdictions, zakat allocation for gharimin remains relatively limited and is often overshadowed by more traditionally prioritised categories such as the poor (fuqara') and needy (masakin). This situation reflects broader challenges relating to institutional coordination, eligibility assessment, and the operationalisation of debt-related financial vulnerability within contemporary zakat governance systems.

This study responds to the urgent need for innovation in zakat management by examining the role of IFIs in optimizing support for gharimin. It aims to bridge traditional Islamic teachings with modern realities through a theory-based strategic framework. In doing so, it contributes to the broader discourse on Islamic social finance and the alignment of zakat governance with the evolving socio-economic landscape.

Zakat Distribution in Malaysia

In Malaysia, zakat collection and distribution are administered at the state level under the jurisdiction of respective State Islamic Religious Councils (SIRCs), creating a decentralized but institutionalized framework. While zakat is a compulsory financial obligation for eligible Muslims, its distribution is guided by clear Shariah principles, covering the eight asnaf categories, including gharimin. Nevertheless, in practice, allocation to gharimin often remains comparatively lower than allocations to traditionally prioritised categories such as the poor (fuqara') and the needy (masakin) (Azhar et al., 2023). Empirical data from JAWHAR (2023) further support this pattern across several Malaysian states. Figure 1 provides a comparative overview of zakat distribution to eight groups of asnaf in 2023 for selected Malaysian states, namely Wilayah Persekutuan, Selangor, Kedah, Johor, Pahang, Perak, and Terengganu. The data reveal substantial differences in allocation priorities and distribution patterns across jurisdictions, reflecting variations in socio-economic conditions, institutional capacities, and state-level zakat governance practices.

Figure 1: Comparative Overview of Zakat Distribution to Eight Groups of *Asnaf* in 2023

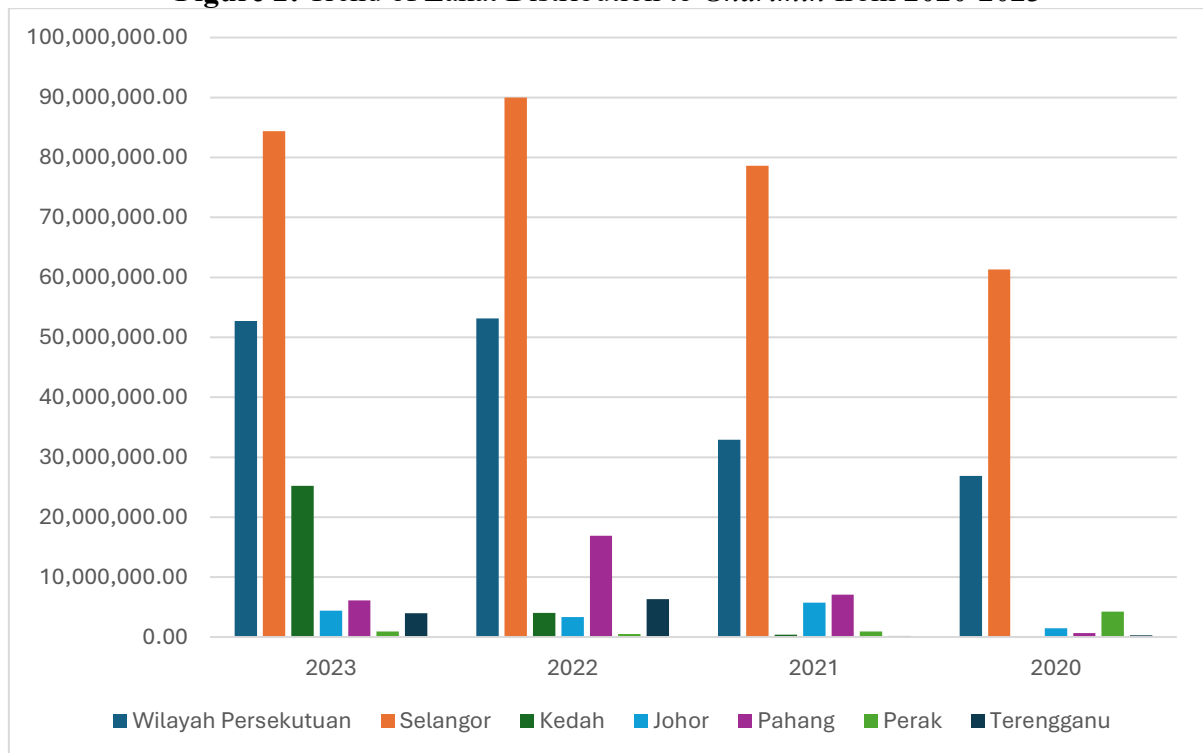


Source: Jabatan Wakaf Zakat dan Haji [JAWHAR], 2023

Overall, the categories of *fugara*’ and *masakin* consistently received the highest proportion of zakat allocation across most states, demonstrating the continued dominance of poverty-oriented distribution practices. Selangor recorded the highest total zakat distribution in 2023 at approximately RM1.15 billion, followed by Wilayah Persekutuan with RM1.02 billion. In both states, allocations to *miskin* exceeded RM400 million, indicating a strong prioritisation of low-income households and urban poverty-related assistance. Similarly, Kedah allocated approximately RM82.9 million to *masakin* and RM23.5 million to *fugara*’, while Johor distributed more than RM138 million to *masakin* and RM74 million to *fugara*’. Pahang and Terengganu also demonstrated substantial allocations to these traditional poverty-based categories, further reinforcing the continued emphasis on direct poverty alleviation within zakat administration.

In comparison, zakat allocation to *gharimin* remained relatively lower across most states despite increasing concerns regarding debt-related financial vulnerability. Selangor recorded the highest allocation to *gharimin* at approximately RM84.4 million, followed by Wilayah Persekutuan at RM52.7 million. Kedah showed a notable increase with RM25.2 million allocated to *gharimin*, suggesting growing institutional recognition of debt-induced hardship. However, allocations in other states remained comparatively modest, including Johor (RM4.4 million), Pahang (RM0.93 million), Perak (RM0.93 million), and Terengganu (RM3.96 million). Therefore, the findings indicate that poverty-related categories continue to dominate zakat allocation across Malaysian states, while distribution to *gharimin* remains comparatively limited despite rising debt-related financial vulnerability.

Figure 2: Trend of Zakat Distribution to *Gharimin* from 2020-2023



Source: Jabatan Wakaf Zakat dan Haji [JAWHAR], 2023

Figure 2 presents the trend of zakat distribution to *gharimin* across selected Malaysian states from 2020 to 2023, highlighting the evolving institutional response toward debt-related financial distress during and after the COVID-19 pandemic. The data reported that Selangor

recorded the highest cumulative allocation throughout the four-year period, with a total exceeding RM314 million, followed by Wilayah Persekutuan at approximately RM165 million. The sustained high allocation in these highly urbanised regions may indicate greater exposure to financing commitments, higher household indebtedness, and stronger institutional awareness of debt vulnerability within metropolitan economies. These states appear to recognise that financial hardship is no longer limited to traditional poverty groups, but increasingly affects formally employed individuals burdened by financing obligations during the crisis situation.

Interestingly, Kedah demonstrated the most dramatic relative increase over the study period, rising from only RM60,707 in 2020 to over RM25 million in 2023. This sharp escalation may reflect an institutional transition toward broader recognition of *gharimin* eligibility, particularly in response to prolonged post-pandemic economic pressures. The pattern suggests that certain states may have gradually expanded their operational interpretation of debt-related hardship over time. In contrast, Johor, Pahang, Perak, and Terengganu exhibited more inconsistent allocation patterns, characterised by fluctuations rather than sustained growth. For example, Pahang recorded a significant increase in 2022 before declining sharply in 2023, while Johor maintained relatively moderate allocations throughout the period. These irregular trends may indicate that zakat assistance to *gharimin* in some jurisdictions remains highly situational and dependent on temporary financial pressures rather than long-term institutional strategies.

Another important observation is that several states continued to allocate comparatively small amounts to *gharimin* despite the broader national concern over rising household debt and financial stress after the pandemic. This may suggest that debt-related vulnerability is still interpreted conservatively within certain zakat institutions, where assistance continues to prioritise traditional poverty indicators over contemporary financing-related distress. In particular, the absence of standardised operational criteria for *gharimin* across states contributes to inconsistencies in eligibility assessment across jurisdictions. Some religious councils adopt narrower interpretations that recognise only critical or religiously justified debts, while others apply broader and more inclusive approaches (Ibrahim & Sahrim, 2019). For example, Selangor and Wilayah Persekutuan demonstrate relatively broader operational approaches by recognising selected forms of financial hardship linked to contemporary living and financing pressures, whereas several other states maintain stricter interpretations that prioritise only critical survival-related debts and immediate necessities. Such variation significantly affects the consistency and reach of zakat assistance for indebted individuals.

Moreover, digital integration within zakat institutions remains relatively limited, particularly in the identification and monitoring of debt-related vulnerability. Although digital platforms are increasingly utilised for zakat payment collection, distribution mechanisms in many institutions still rely heavily on manual verification and conventional assessment procedures, which are often time-consuming and prone to administrative inefficiencies (Razali et al., 2022). This technological limitation restricts real-time decision-making and weakens the potential for data-driven targeting. Crucially, many zakat institutions continue to depend on traditional poverty indicators such as income thresholds and visible signs of hardship in determining eligibility. Consequently, individuals experiencing substantial debt obligations but who do not fall within conventional poverty classifications may be excluded from zakat assistance. This issue is particularly relevant in the context of *gharimin* within IFIs, where borrowers may possess regular income yet remain trapped in unsustainable debt cycles arising from financing commitments (Yamaludin et al., 2023).

Taken together, these limitations show that the implementation of zakat distribution for *gharimin* in Malaysia remains varied across states and institutions. Without standardised definitions, integrated databases, and stronger inter-institutional coordination, zakat governance risks becoming increasingly misaligned with contemporary forms of financial vulnerability. These findings therefore reinforce the need for more coordinated, data-driven, and context-sensitive zakat distribution mechanisms capable of addressing the evolving realities of indebtedness in Malaysia.

Role of Islamic Financial Institutions (IFIs)

Islamic Financial Institutions (IFIs) occupy a strategic and multifaceted role within the Islamic social finance ecosystem, functioning not only as providers of Shariah-compliant financial services but also as key intermediaries in the mobilisation and distribution of zakat. Within this framework, IFIs serve as an important institutional bridge connecting financial resources with socio-economic needs, thereby contributing to the broader objectives of equitable wealth distribution and social justice.

A central mechanism through which IFIs operationalise this role is the *wakalah* zakat model, whereby the institution is appointed as an agent (*wakil*) to administer and distribute zakat funds on behalf of contributors, in accordance with the regulatory oversight of State Islamic Religious Councils (Nor Paizin & Abdul Rahim, 2021). This arrangement enables IFIs to extend their functional scope beyond commercial intermediation, positioning them as active participants in zakat distribution. Through this model, IFIs facilitate the systematic channeling of zakat to eligible *asnaf*, including *gharimin*, within a structured and regulated environment.

Beyond their intermediary function, IFIs possess unique informational and operational advantages that enhance their role in zakat allocation. As financial institutions, they maintain extensive data on clients' financial behaviour, repayment patterns, and exposure to credit risk. This positions IFIs to contribute meaningfully to the identification and assessment of individuals experiencing debt-induced financial vulnerability. In particular, their proximity to financing activities allows for a more nuanced understanding of indebtedness, thereby supporting more informed and context-sensitive zakat allocation decisions.

In recent years, the role of IFIs has further evolved with the integration of financial technology (fintech) and digital innovations into Islamic social finance. The adoption of data analytics, automated assessment tools, and digital disbursement platforms enables IFIs to enhance the efficiency, accuracy, and transparency of zakat management processes. These technological capabilities support a more systematic and data-informed approach to identifying eligible recipients, monitoring fund utilisation, and ensuring timely delivery of assistance. In this regard, zakat is increasingly positioned not only as a redistributive instrument but also as a strategic tool for financial stabilisation and resilience building.

Importantly, the role of IFIs is underpinned by the broader ethical and socio-economic mandate of Islamic finance, which emphasises the promotion of *maslahah* (public interest) and the preservation of wealth (*hifz al-mal*). As highlighted by Alsaadi (2021), IFIs are expected to uphold these principles by ensuring that financial activities contribute to societal well-being. In the context of zakat, this translates into a responsibility to facilitate efficient, transparent, and impactful distribution mechanisms that address diverse forms of financial vulnerability, including indebtedness.

Thus, IFIs may support more systematic zakat governance for *gharimin* through financial verification processes, repayment monitoring, and institutional collaboration with zakat authorities. Such coordination may improve the identification of eligible debtors and strengthen the implementation of debt-relief assistance within contemporary Islamic financial settings.

Gharimin in Crisis and Non-Crisis Contexts

The category of *gharimin*, referring to individuals burdened with legitimate debts beyond their capacity to repay, holds a deeply embedded position within Islamic legal and ethical tradition. Its inclusion among the designated recipients of zakat reflects a broader conception of financial vulnerability that extends beyond income insufficiency to encompass debt-induced hardship and socio-economic imbalance. This principle is further reinforced by Prophetic guidance, which affirms the permissibility of zakat allocation to individuals burdened by debt even when they may not fall strictly within income-based poverty classifications. As narrated by the Prophet Muhammad ﷺ:

“Charity is not lawful for the rich, nor for the one who is strong and able to earn, except for the one who is poor or heavily indebted” (Sunan Abu Dawood, Hadith 1633).

This hadith reflects a profound concern for the welfare of debtors, positioning zakat not merely as an act of charity but as a mechanism for restoring financial dignity and preventing social exclusion. Classical scholars such as Al-Qarafi (1994) and Al-Ghazali (1997) emphasised that indebtedness is often circumstantial rather than indicative of financial mismanagement, thereby justifying the provision of institutional support through zakat. In this regard, zakat may serve as a financial support mechanism for eligible *gharimin* by assisting debtors experiencing financial hardship and reducing the risk of prolonged economic vulnerability.

In contemporary contexts, the relevance of *gharimin* can be understood across both crisis and non-crisis economic environments, each shaping the nature and intensity of indebtedness. During periods of economic disruption, such as the COVID-19 pandemic, financial vulnerability tends to intensify rapidly across different income groups. Factors such as job losses, income instability, and business closures contribute to increased reliance on debt for essential expenditures. In such circumstances, zakat serves as a stabilising instrument, facilitating the redistribution of resources to individuals experiencing sudden financial distress. As noted by Ab Rahman et al. (2022) and Kasim et al. (2023), the heightened need for support during such periods underscores the importance of responsive and adaptive zakat mechanisms.

In non-crisis contexts, indebtedness often reflects ongoing financial commitments associated with housing, education, healthcare, and livelihood-related expenses. In these settings, *gharimin* represents a category that captures chronic financial pressure rather than immediate poverty, highlighting the relevance of zakat in supporting longer-term financial stability. Zakat interventions in such contexts contribute to the broader objective of financial rehabilitation, complementing other forms of socio-economic support aimed at enhancing individual resilience and economic participation (Abdul Wahid et al., 2017; Razali et al., 2021).

Overall, the conceptualisation of *gharimin* across crisis and non-crisis contexts highlights the dynamic and multidimensional nature of financial vulnerability within the Islamic framework. Zakat, in this regard, operates not only as a redistributive tool but also as a strategic mechanism for maintaining socio-economic balance, addressing both acute and persistent forms of indebtedness. This perspective reinforces the alignment of zakat practices with the objectives

of Maqasid al-Shariah, particularly the preservation of wealth (*hifz al-mal*) and the protection of human dignity, within an increasingly complex and evolving financial landscape.

METHODOLOGY

This study employs the Straussian Grounded Theory approach developed by Strauss and Corbin (1990) because the study aims to generate a substantive theory explaining the processes, challenges, and institutional dynamics surrounding zakat distribution for *gharimin* within IFIs. The approach is particularly suitable due to the limited empirical understanding and absence of an established theoretical framework addressing debt-related zakat assistance within contemporary Islamic financial settings. Through iterative coding, constant comparison, and theoretical sampling, the study systematically developed conceptual categories and relationships grounded directly in stakeholder experiences and institutional practices, allowing the resulting framework to emerge inductively from the empirical data.

Primary data were collected through semi-structured, in-depth interviews involving four key stakeholder groups: academicians, with expertise in zakat and Islamic finance, officers from zakat institutions, Shariah committee members and top management personnel from IFIs, as well as representatives from debt advisory and financial management agencies operating under Bank Negara Malaysia (BNM). The selection criteria focused on individuals directly involved in zakat governance, Shariah advisory, debt management, financial counselling, eligibility assessment, and operational decision-making related to *gharimin* and zakat distribution practices. Informants were chosen based on their professional experience, institutional authority, and direct engagement with debt-related financial vulnerability, particularly during and after the COVID-19 pandemic. Their professional roles and operational experience provided critical insights into the interpretation of *gharimin*, institutional challenges, governance practices, and the practical mechanisms involved in zakat distribution and debt-relief assistance. To enhance analytical robustness, the study also incorporated secondary data sources, including institutional reports, policy documents, and published statistics. This combination facilitated data triangulation, thereby strengthening the validity and credibility of the findings.

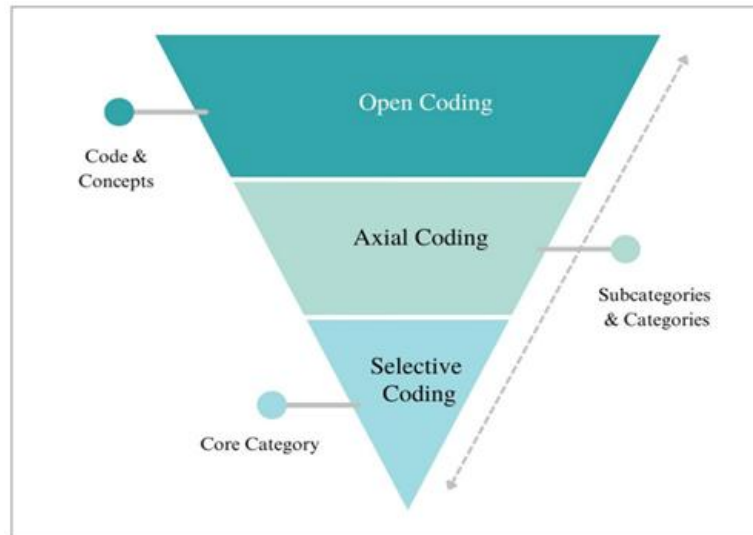
Data analysis followed the systematic procedures outlined by Strauss and Corbin, involving a three-stage coding procedure of Grounded Theory, ensuring a systematic progression from raw data to theory development

- Open Coding: Identification and initial categorisation of concepts emerging from the data
- Axial Coding: Establishing relationships between categories, particularly in terms of conditions, interactions, and consequences
- Selective Coding: Integration of categories into a coherent explanatory framework or core category.

Figure 3 demonstrates how the analysis progressed from open coding, where raw data were broken down into initial concepts and codes, to axial coding, where relationships between categories were established through conditions, interactions, and consequences. This was followed by selective coding, which involved integrating and refining categories into a coherent explanatory framework centred on a core category. The visual representation highlights the iterative and interconnected nature of the coding process, where data collection and analysis occurred simultaneously until theoretical saturation was achieved. This process

ultimately led to the development of a substantive theory that explains the strategic allocation of zakat for *gharimin* within Islamic Financial Institutions (IFIs) in Malaysia as a dynamic, context-responsive, and institutionally mediated process.

Figure 3: The Coding Process of Grounded Theory



Source: Strauss and Corbin (1990)

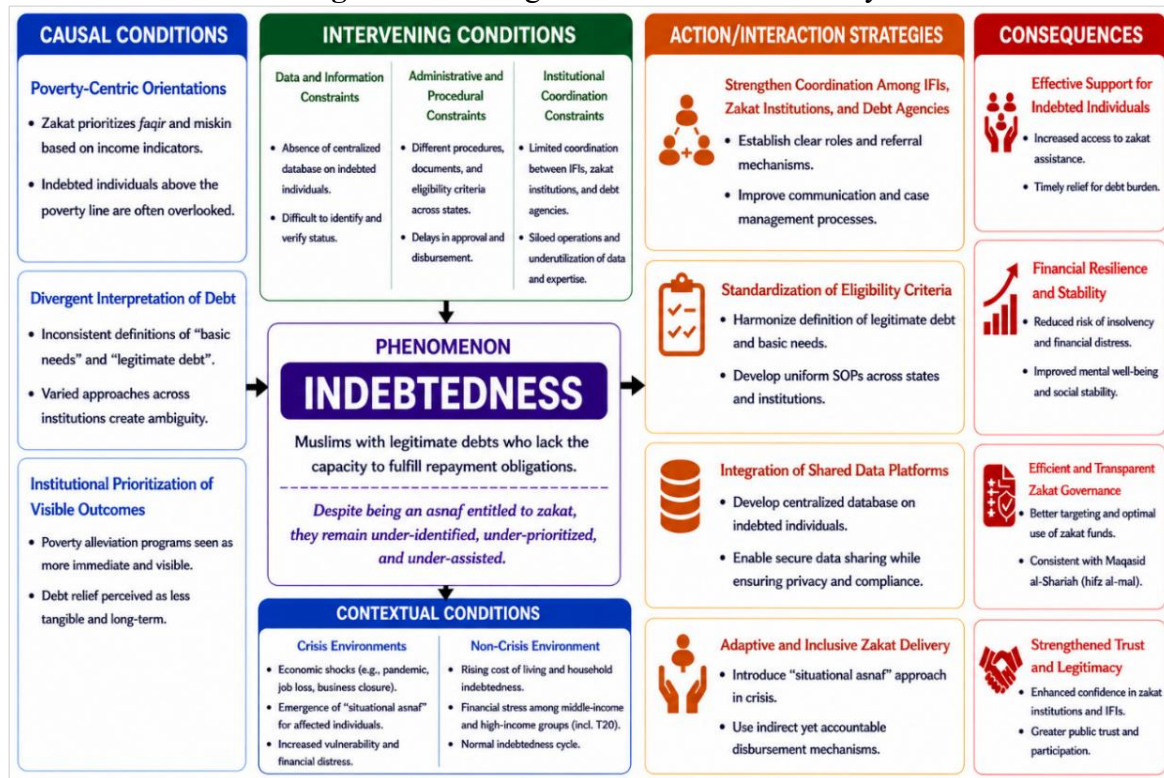
Paradigm Model

Building on the open coding phase, axial coding was conducted using the paradigm model (Strauss & Corbin, 1990) to systematically reassemble the data by establishing relationships between categories. This analytical process organises the findings into five interconnected components: causal conditions, central phenomenon, intervening conditions, contextual conditions, action/interaction strategies, and consequences.

The causal conditions reveal a predominantly poverty-centric orientation and divergent interpretations of legitimate debt, which influence how financial vulnerability is recognised within zakat systems. This gives rise to the central phenomenon where *gharimin*, despite being a legitimate *asnaf* category, remain under-identified and under-prioritised in practice. The response to this phenomenon is further mediated by intervening conditions, including institutional arrangements, administrative processes, and information systems, which shape how zakat is operationalised.

At the same time, the manifestation of indebtedness is influenced by contextual conditions that vary across crisis and non-crisis environments, reflecting both acute and ongoing financial pressures. In response, institutions adopt adaptive strategies such as standardising eligibility criteria, integrating data platforms, and implementing more inclusive zakat delivery approaches. These interactions ultimately lead to outcomes associated with improved support for indebted individuals, enhanced financial resilience, and greater transparency and trust in zakat governance. Overall, the paradigm model highlights that the position of *gharimin* within the zakat system is not static but dynamically constructed through the interaction of conceptual frameworks, institutional mechanisms, and evolving socio-economic contexts. Figure 4 provides a structured explanation of how the issue of indebtedness among Muslims emerges and is addressed within the zakat ecosystem.

Figure 4: Paradigm Model of Current Study



FINDINGS AND ANALYSIS

This section presents key findings derived from in-depth interviews with academicians, Shariah committee members in IFIs, officers from zakat institutions, and representatives of debt agencies. The data were analyzed to understand the institutional dynamics, operational challenges, and potential strategies involved in the zakat allocation process for *gharimin* within Malaysia's IFIs. The findings highlight the fragmented institutional landscape, prioritisation of *gharimin*, and the urgent need for a strategic, data-driven framework to bridge these gaps. These issues underscore the need to reconceptualise zakat distribution beyond traditional poverty paradigms toward a more inclusive model addressing financial distress and indebtedness, in line with the objectives of Maqasid al-Shariah (Ab Rahman et al., 2022, Yamaludin et. al., 2023).

Main Category 1: Emergence of Situational Asnaf

The findings reveal a significant conceptual development in zakat practice, namely the emergence of "situational *asnaf*", which reflects a shift toward a context-sensitive and dynamic interpretation of zakat eligibility. Unlike traditional classifications anchored in static income thresholds such as *fuqara'* and *masakin*, this category captures individuals who become financially vulnerable due to sudden and unforeseen socio-economic disruptions, particularly during periods of crisis. Empirical evidence demonstrates that zakat institutions increasingly recognise that financial vulnerability is not confined to traditionally defined low-income groups. As one informant explained, "*even rich people who experienced job loss and loss of income due to the pandemic will be grouped under situational *asnaf*... normally the situation is temporary and will quit from the title of *asnaf**" (#Z1). This is further supported by observations that "*during the pandemic, we've been receiving zakat applications not only from M40 but also from T20 groups*" (#Z2). These findings indicate a fundamental shift in eligibility

logic, where situational financial distress overrides static socio-economic classification, reinforcing the fluid nature of vulnerability (Hassan & Noor, 2020; Kasri & Putri, 2018).

At the operational level, this reclassification is institutionalised through structured assessment mechanisms. Eligibility is triggered by verifiable income disruptions such as “*“loss of source of livelihood... job termination, reduced salary, or unpaid leave, supported by documentary evidence including termination letters and confirmation of unpaid leave due to the pandemic”*” (#Z1, #Z6). This reflects a procedural translation of situational vulnerability into eligibility decisions, where individuals are granted temporary or one-off assistance, followed by reassessment based on recovery status. Critically, the data reveal that situational *asnaf* is inherently transitional and reversible, rather than a fixed classification. Individuals may enter the category during periods of economic shock and exit once financial stability is restored, indicating that zakat eligibility is increasingly aligned with temporal financial conditions rather than permanent socio-economic identity.

Finally, the findings show that situational *asnaf* is often compounded by debt-related financial pressure, particularly among individuals experiencing simultaneous income loss and repayment obligations. As highlighted by one informant, “*job loss and income reduction force individuals from higher income groups to shift rapidly into lower income groups,*” illustrating how financial shocks accelerate downward mobility and intensify indebtedness. This interaction underscores the expanding scope of *gharimin*, where debt vulnerability emerges as a context-driven condition linked to broader economic instability. This supports the view that zakat, when applied through a situational lens, functions not only as a redistributive tool but also as a stabilising mechanism during systemic shocks (Zal et al., 2021).

Therefore, the emergence of situational *asnaf* demonstrates that zakat categorisation is not static but socially constructed and continuously reinterpreted in response to evolving economic realities. This finding extends existing literature by providing empirical evidence that *gharimin* is increasingly conceptualised as a dynamic manifestation of financial vulnerability, shaped by contextual conditions rather than fixed legal definitions. Consequently, this necessitates the development of more flexible, adaptive, and context-driven allocation frameworks to ensure that zakat remains responsive to contemporary forms of financial distress.

Main Category 2: Institutional and Governance Constraints

The second key finding highlights the role of institutional structures and governance arrangements in shaping the operationalisation of zakat for *gharimin*. The data reveal that zakat distribution is embedded within a multi-layered governance ecosystem, involving zakat authorities, Islamic Financial Institutions (IFIs), and Shariah advisory bodies, each contributing to how eligibility is interpreted, validated, and implemented in practice.

A central theme emerging from the data is the reliance on formalised procedures grounded in Shariah principles. Zakat allocation decisions are not made solely based on individual discretion but are guided by recognised Shariah and institutional guidelines, as reflected in the following statement: “*Decisions are guided by the Qur'an and Sunnah, ijma' (scholarly consensus), Maqasid al-Shariah, and the rulings of the Shariah Committee.*” (#Z6). This demonstrates that zakat governance operates within a normatively structured framework, ensuring that allocation practices remain aligned with Islamic jurisprudence. Such institutionalisation of Shariah governance is consistent with prior studies emphasising accountability, legitimacy, and compliance in zakat administration (Ascarya, 2021).

At the operational level, however, the findings indicate that governance is not entirely based on fixed rules and procedures, but also involves contextual interpretation and institutional discretion in assessing eligibility and financial circumstances, particularly in determining *had kifayah* (basic needs) and financial capacity. Informants emphasised that eligibility assessment requires detailed case-by-case evaluation supported by documentation and verification processes. As noted, institutions require “*Supporting documents and evidence, such as termination letters or confirmation of unpaid leave, are required to validate applicants’ financial conditions, while structured tools such as had kifayah calculations are used to assess eligibility thresholds.*” (#Z4). The findings further show that zakat institutions apply systematic procedures in assessing applications, verifying eligibility, and determining assistance levels through internal administrative processes and operational protocols. This demonstrates that zakat governance functions not only as a Shariah compliance mechanism, but also as an institutional coordination process aimed at ensuring accountability, consistency, and proper distribution practices. From a theoretical perspective, these findings suggest that effective zakat governance requires both adherences to established Shariah principles and sufficient institutional flexibility to respond to evolving socio-economic conditions and contemporary forms of financial vulnerability. Such flexibility aligns with existing literature that characterises zakat governance as both formalised and context-sensitive (Ismail et al., 2018).

The findings further reveal that governance practices are continuously refined and adapted to contemporary socio-economic realities, particularly in response to emerging forms of financial vulnerability. This is reflected in institutional recognition of the need for interpretive refinement, as highlighted by informant: “*A more appropriate interpretation that reflects current conditions is needed.*” (#B4). Similarly, another informant acknowledged that there were no clear guidelines in place, either from zakat regulations or internal procedures, to determine who qualifies as *gharimin*: “*During that period, the zakat institutions were unprepared to address the pandemic crisis, and there were no clear guidelines in place, either from zakat institutions or internal procedures, to determine who qualifies as gharimin. As a result, the absence of these guidelines meant that targeted support for gharimin was lacking.*” (#U1). These findings highlight the importance of developing clearer operational guidelines and more harmonised interpretations of *gharimin* to improve consistency in zakat distribution practices across jurisdictions, particularly in addressing contemporary forms of debt-related financial vulnerability and crisis-related financial distress.

Main Category 3: Conflict of Interest in Zakat Distribution

The third category identifies the presence of institutional tensions in zakat distribution via Islamic Financial Institutions (IFIs), particularly where the administration of zakat intersects with the commercial functions of financial intermediation. The findings indicate that zakat distribution within IFIs is shaped by the need to carefully navigate ethical boundaries, Shariah governance principles, and perceptions of institutional neutrality, in order to preserve the integrity of zakat as a social finance instrument.

Empirical evidence shows that IFIs possess a strong operational capacity to identify financially distressed individuals through internal customer databases and repayment records. As highlighted by one informant, “*the bank wants to use zakat for its customers... they have their database and the capability to identify their customers who are facing financial difficulties*” (#A1). However, despite this informational advantage, the findings reveal significant governance limitations regarding how zakat funds may be utilised within IFIs. Informants

consistently emphasised that IFIs cannot directly use zakat funds to settle financing obligations owed to the same institution. As stated by one participant, *“the bank cannot pay zakat directly to their customers to pay off the outstanding debt”* (#A1). This demonstrates the existence of a structural tension in which IFIs are operationally well-positioned to identify eligible *gharimin*, yet remain constrained by Shariah governance principles and conflict-of-interest concerns.

The findings are further reinforced by the discussion of Fatwa No. 138688, which establishes that zakat funds cannot be used to directly offset debts owed to the same creditor institution under conditional arrangements. The fatwa explicitly states: *“If the zakat was paid to him on the condition that he return it to him for his debt, then the payment is not valid, and the zakat is not forfeited.”* (Fatwa No. 138688) The fatwa further clarifies that zakat distribution remains permissible only when recipients retain full discretion over the utilisation of the assistance without coercive repayment conditions. This jurisprudential position provides an important Shariah foundation against the direct use of zakat funds to repay financing facilities held within the same IFI, even where recipients may qualify as eligible *gharimin*. Consequently, IFIs must ensure a clear separation between charitable disbursement and commercial debt recovery mechanisms.

This tension is further reinforced by institutional concerns regarding reputational risk and perceived organisational benefit. Informants explicitly acknowledged that *“when banks assist their own customers with zakat funds, there will be a conflict-of-interest issue”* (#B4), particularly where zakat distribution may be perceived as indirectly strengthening the financial position of the institution itself. Similarly, another informant cautioned against *“utilizing zakat funds for our own advantage or gaining benefits from zakat”* (#B7). These concerns demonstrate that governance challenges within IFIs extend beyond operational procedures and involve broader ethical considerations relating to institutional legitimacy, transparency, and public trust.

As a result, the findings indicate that IFIs intentionally avoid mechanisms such as direct debt offsetting or conditional repayment arrangements funded through zakat. Instead, zakat assistance is structured in ways that preserve beneficiary autonomy and minimise perceptions of institutional self-interest. As noted by one informant, *“we do not stipulate that it must be repaid to the same bank”* (#B4). This reflects an operational approach that seeks to maintain a distinction between zakat assistance and debt recovery activities.

The findings further reveal that third-party institutional arrangements are increasingly viewed as a governance mechanism for mitigating conflict-of-interest concerns. Informants proposed that independent third-party institutions operating under the supervision of State Islamic Religious Councils (SIRCs) could facilitate zakat distribution to *gharimin* more transparently and neutrally. One informant explained that *“the third-party institution can coordinate with IFIs to channel the zakat fund requiring zakat institutions to deal with only one third party rather than each IFI”* (#A1). Another informant emphasised that *“having a third party in this situation seems like a viable way to refute allegations that the benefits are being directed towards the bank”* (#Z2).

From a theoretical perspective, this category demonstrates that zakat distribution within IFIs operates within a dual institutional logic, where financial institutions must balance their commercial responsibilities with their role in facilitating Islamic social finance initiatives. The findings suggest that the effectiveness of zakat governance within IFIs is not determined solely

by institutional capacity or access to financial data, but also by the ability to navigate ethical constraints, Shariah governance principles, and public perceptions of institutional neutrality. This contributes to the literature by highlighting that conflict-of-interest management constitutes a critical dimension of contemporary zakat governance within Islamic financial ecosystems. This finding contributes to the literature by demonstrating that the effectiveness of zakat distribution in IFIs is not solely determined by operational capacity, but also by the ability to navigate and reconcile competing institutional objectives (Hassan & Aliyu, 2018).

Core Category: Substantive Theory of a Strategic Solutions Framework for Gharimin In Islamic Financial Institutions

The integration of the three main categories; Emergence of Situational *Asnaf*, Institutional and Governance Constraints, and Conflict of Interest in Zakat Distribution via IFIs, gives rise to a substantive theory of a Strategic Solutions Framework for *gharimin* in IFIs. This theory explains how zakat allocation for indebted individuals is not merely a matter of resource distribution, but a systemic process shaped by dynamic classification, institutional structures, and ethical governance considerations.

At the core of this theory is the recognition that the category of *gharimin* has undergone a significant conceptual transformation, as evidenced by the emergence of situational *asnaf*. This finding demonstrates that financial vulnerability is no longer confined to traditional poverty classifications but is increasingly understood as context-dependent and temporally fluid, particularly in response to economic shocks. Individuals who were previously outside the *asnaf* framework may become eligible due to sudden income loss and debt accumulation, thereby requiring a more adaptive and responsive zakat allocation approach. This reclassification serves as the entry point of the theory, highlighting the need for a system that can accommodate evolving forms of financial distress.

However, the ability to respond effectively to this expanded category is mediated by the second finding, which relates to institutional and governance structures. The data indicate that zakat allocation operates within a multi-layered governance system, where Shariah principles, administrative procedures, and institutional coordination interact to determine eligibility and distribution outcomes. While this structure ensures normative legitimacy and accountability, it also introduces procedural complexity and variability in interpretation, particularly in assessing financial capacity and defining legitimate debt. As such, governance does not function as a neutral mechanism but as an active shaping force that influences how *gharimin* is identified, prioritised, and supported. Within the substantive theory, this category explains the institutional conditions that constrain or enable adaptive allocation.

The third category further refines this understanding by highlighting the presence of conflict-of-interest dynamics within IFIs, arising from their dual role as financial intermediaries and zakat distributors. The findings show that IFIs must carefully navigate the boundary between social responsibility and commercial interest, particularly in situations where zakat funds may intersect with financing portfolios. This creates a need for ethical safeguards and governance mechanisms to preserve transparency, neutrality, and public trust. Consequently, zakat distribution is not only a technical or administrative process but also an ethical negotiation, where institutional legitimacy must be continuously maintained. Within the theory, this category represents the normative constraint that shapes how solutions can be designed and implemented.

When integrated, these three categories reveal that the challenge of supporting *gharimin* is fundamentally a problem of classification (who qualifies), coordination (how institutions respond), and ethical governance (how conflicts are managed). The substantive theory therefore proposes a Strategic Solutions Framework that transforms zakat allocation from a fragmented, reactive system into a coordinated, adaptive, and ethically governed model. This transformation is operationalised through a dual logic of:

- Needs-based prioritisation, which ensures that assistance is directed toward individuals experiencing the most urgent and severe financial distress, particularly situational *asnaf*; and
- Data-driven allocation, which enhances consistency, transparency, and efficiency in decision-making across institutions.

These allocation logics are supported by enabling mechanisms such as real-time tracking systems, automated disbursement, and predictive analytics, which collectively institutionalise decision-making, reduce fragmentation, and enable proactive identification of vulnerable individuals. Importantly, these mechanisms do not replace human judgement but rather standardise and strengthen it within an integrated system (Mohamed Salleh et al., 2022).

The outcome of this integrated framework is a zakat allocation model that is more responsive to dynamic and crisis-induced forms of financial vulnerability, enabling timely identification and support of individuals affected by evolving socio-economic conditions. At the same time, the model enhances coordination across institutional actors, fostering greater alignment between zakat institutions, Islamic Financial Institutions (IFIs), and related stakeholders in the allocation process. In addition, it promotes higher levels of transparency and accountability in governance through structured and traceable mechanisms of decision-making and fund disbursement. Overall, the framework ensures stronger alignment with the objectives of Maqasid al-Shariah, particularly *hifz al-mal* (protection of wealth) and the preservation of human dignity (Meerangani et al., 2022, Wahab et al., 2026).

Figure 5 illustrates the substantive theory developed from the grounded analysis, demonstrating how zakat allocation for *gharimin* evolves from a fragmented and poverty-centred system into a strategically coordinated, adaptive, and ethically governed framework within IFIs. The model is structured around three interrelated empirical categories that collectively shape the allocation process.

Figure 5: Substantive Theory of a Strategic Solutions Framework for *Gharimin* In Islamic Financial Institutions



IMPLICATIONS AND RECOMMENDATIONS

The findings of this study carry important implications for zakat institutions and IFIs, particularly in understanding how contemporary debt-related financial vulnerability is interpreted, governed, and operationalised within the zakat ecosystem. The grounded analysis revealed several interconnected institutional issues, including the emergence of situational *asnaf*, fragmented governance practices, and ethical tensions arising from the dual role of IFIs as financial intermediaries and facilitators of zakat-related assistance. These findings suggest that contemporary forms of debt-related financial distress may require more adaptive and context-sensitive zakat assessment approaches alongside existing poverty-oriented mechanisms.

Based on the grounded analysis, the study proposes a substantive theory of a Strategic Solutions Framework for *Gharimin*, which explains how zakat allocation evolves through the interaction of situational financial vulnerability, institutional governance structures, and ethical considerations IFIs. The framework highlights the importance of adaptive governance, institutional coordination, and context-responsive assessment practices in addressing evolving forms of indebtedness within contemporary financial environments. Accordingly, this section discusses the theoretical, methodological, and practical implications of the study, together with recommendations for relevant stakeholders.

Theoretical Implications

This research contributes to the growing body of literature on Islamic social finance by introducing a dynamic, institutionally grounded zakat distribution model tailored to contemporary financial realities. While traditional Islamic scholarship has long emphasized the legitimacy of debt relief through zakat, this study repositions the category of *gharimin* within the framework of strategic social intervention. It highlights the need to align zakat distribution with modern financial structures, where over-indebtedness has become a systemic issue affecting even non-poor individuals. The theoretical model proposed in this study integrates several fiqh principles underlying *gharimin* governance, including prevention of harm (*al-darar yuzal*), public interest (*maslahah*), protection of wealth (*hifz al-mal*), and the classification of needs based on *dharuriyat*, *hajiyyat*, and *tahsiniyat*. These principles are operationalised within contemporary zakat governance through contextual eligibility assessment, institutional coordination, and ethical safeguards against conflict of interest in zakat distribution.

Methodological Implications

This study demonstrates the applicability of grounded theory in developing theory from the ground up in underexplored areas of Islamic finance. By combining in-depth interviews with multiple stakeholder groups, including Shariah scholars, IFI officers, zakat practitioners, and debt agency representatives, and supplementing this with secondary data, the research uncovered nuanced institutional challenges and practical gaps. This approach offers a blueprint for future researchers aiming to explore multi-actor collaboration in Islamic financial systems. Additionally, future studies could extend this work through quantitative validation, using tools such as econometric modeling, simulation techniques, or impact assessment studies to test the effectiveness of the proposed framework across different zakat management environments.

Practical Implications

From a policy and operational standpoint, the study recommends several key strategies for improving zakat distribution to *gharimin*:

- Development of a centralized, technology-enhanced zakat management system: Zakat institutions, in collaboration with IFIs and debt agencies, should invest in a shared digital infrastructure that facilitates real-time beneficiary tracking, automated eligibility verification, and predictive analytics for identifying financial hardship.
- Automation and real-time tracking of zakat disbursements: Leveraging financial technology (fintech) can streamline zakat disbursement processes, minimize administrative burden, and ensure that funds reach eligible *gharimin* without delay—particularly critical during crises.
- Standardization of *gharimin* eligibility criteria across jurisdictions: National-level policy harmonization is needed to address the current inconsistency in defining and prioritizing *gharimin* across states. This would help create uniform zakat policies that uphold both Shariah compliance and operational fairness.
- Strengthening institutional collaboration: Regular coordination between IFIs, zakat authorities, and debt advisory agencies should be institutionalized through memoranda of understanding (MOUs), joint task forces, or shared data agreements. This will help improve information flows and decision-making at the operational level.
- Capacity building for zakat managers and IFI personnel: Training programs should be

developed to enhance institutional understanding of zakat distribution in debt contexts, data governance, and the use of digital tools in social finance management.

CONCLUSION

This study examined the allocation of zakat for *gharimin* within Islamic Financial Institutions (IFIs) in Malaysia, focusing on how eligibility is interpreted and operationalised in contemporary practice. The findings highlight three key dynamics: the emergence of situational *asnaf*, reflecting a shift toward context-sensitive classification; institutional and governance structures, which shape eligibility through formal Shariah principles and contextual judgement; and conflict-of-interest considerations, which necessitate careful ethical governance in zakat distribution.

Using a Grounded Theory approach, the study develops a substantive theory of a Strategic Allocation Framework for *Gharimin*, demonstrating how zakat allocation can evolve into a more adaptive, coordinated, and ethically governed system. The framework emphasises the recognition of dynamic financial vulnerability, supported by structured governance and data-informed mechanisms, enabling more responsive and transparent distribution.

Practically, the study offers guidance for zakat institutions and IFIs to strengthen coordination, standardise assessment, and enhance accountability in allocation processes. While the findings are context-specific to Malaysia and based on qualitative data, they provide broader insights for improving zakat governance in addressing contemporary debt-related vulnerability.

In conclusion, the study reinforces the role of zakat as a strategic instrument for promoting financial resilience, social justice, and the preservation of human dignity, in line with Maqasid al-Shariah.

DECLARATIONS

Acknowledgements The research work was funded by Universiti Teknologi MARA under the Geran Insentif Penyelidikan (GIP) (600-RMC/GIP 5/3 (003/2023) for the project “Developing a Gharimin Recovery Framework for Gharimin of Non-Performing Financing in Islamic Financial Institutions.” The authors also extend their appreciation to all stakeholders and participants who contributed to this study.	Competing Interest The author(s) declare that they have no competing interests.
Authors' contributions Siti Mazlita Yamaludin: Conceptualization, methodology, analysis and investigation. Mohd Rahim Khami Mohd Suffian Mohamed Esa and Azman Abd. Rahman: Review and editing. Sharifah Faigah Syed Alwi: Funding acquisition, supervision. All author(s) read and approved the final manuscript.	Ethics Approval This study was approved by the Research Ethics Committee, Research Management Centre, Universiti Teknologi MARA under reference number REC4/2020/BM Pind.2(2020). Informed consent was obtained from all participants involved in the study.
Data Availability All data generated or analysed during this study are included in this published article.	Use of Artificial Intelligence ChatGPT was used solely to assist with language editing and to improve the clarity of the manuscript. All content, analysis, arguments, and conclusions were reviewed, verified, and approved by the author(s), who remain fully responsible for the final manuscript.

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