

The Application of *Al-Tawarruq* in Personal Financing: Evidence from Islamic Banks in Malaysia

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ABSTRAK

Bay' al-tawarruq is among the Shariah contracts that has become increasingly popular in the modern financing of Islamic banking products. However, the application of this contract among the Islamic banks in Malaysia demonstrates notable variations in practice. Therefore, this study focuses on the implementation of personal financing products involving these contracts and determines their significant challenges. Bank Islam Malaysia Berhad (BIMB) and Bank Muamalat Malaysia Berhad (BMMB) are selected as the sample Islamic Financial Institutions (IFIs) to examine the application of the *al-tawarruq* contract. This study employs a qualitative approach based on content analysis. The data obtained is then analysed descriptively. This study employs a qualitative approach based on document and content analysis, using product manuals, policy documents, and regulatory guidelines. The findings reveal that both banks extensively use *bay' al-tawarruq* in personal financing to ensure Shariah compliance, despite criticisms and operational challenges, such as Shariah alignment, commodity validation, and overreliance on a single contract. The study highlights the need for diversification and continuous improvement in Shariah-compliant financing models to maintain industry credibility and sustainability.

Keywords: *Bay' al-Tawarruq*, *Murabahah*, Personal Financing, Islamic Banks

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INTRODUCTION

The development of the Islamic banking system in Malaysia in offering personal financing products based on *bay al-tawarruq* shariah principles is currently significant in line with contemporary market development and changes of the times. In the development of Islamic Financial Institution (IFIs) on personal financing products offered so far have provided convenience and alternatives to the Muslim community rather than using conventional products

(Ahmad & Ismail, 2011). In Islamic banking, sale and purchase contracts such as *Bay' al-tawarruq* are among the mechanisms frequently used, especially for personal financing.

According to Accounting and Auditing Organization for Islamic Institutions (AAOIFI), *bay' al-tawarruq* defines *al-tawarruq* as well as buying an item at the same price in the same price, there is a *musawamah* or *murabahah* and then sells in cash to parties other than the seller of origin for the purpose of getting cash. Similarly, Abd Allah Sulaymān al-Manī' characterises *al-tawarruq* as a transactional method for an individual in need of cash to acquire it without resorting to usury (*riba*). This is achieved by purchasing a commodity at a deferred price, which includes a profit margin, and then immediately selling it to another party for a lower cash price, provided the buyer is not the original seller.

These two shariah contracts have been extensively adopted by the IFIs in Malaysia, especially in personal financing products. Consequently, this study aims to examine the application of shariah contract *bay' al-tawarruq* in personal financing products offered by two prominent Islamic banks in Malaysia; Bank Islam Malaysia Berhad (BIMB) and Bank Muamalat Malaysia Berhad (BMMB).

METHODOLOGY

This study adopts a qualitative research design, focusing on document and content analysis to explore the implementation of *Bay' al-tawarruq* in personal financing at Bank Islam Malaysia Berhad (BIMB) and Bank Muamalat Malaysia Berhad (BMMB). Data were collected from a variety of sources including official product brochures, policy documents, Shariah resolutions, regulatory guidelines from Bank Negara Malaysia (BNM) and AAOIFI, and relevant academic publications. The analysis involved systematically reviewing the operational procedures, supporting contracts, and documentation practices of both banks. The findings were then synthesized to provide a comprehensive understanding of best practices and challenges in the application of *Bay' al-tawarruq* for personal financing in IFIs in Malaysia.

LITERATURE REVIEW

Definition of *al-Tawarruq*

In the tradition of Islamic jurisprudence (*fiqh*), the concept of *al-tawarruq* in its origin was only discussed in depth by jurists, Fuqaha' of the Hanbali school. Although other schools such as Hanafi, Maliki, and Shafi'i did not use the term directly, they also discuss similar forms of transactions in their conversation about *Bay 'Al-' Inah* and *Bay 'Al-' Ajal*. For example, the Hanafi school considers a transaction called *al-tawarruq* by the Hanbali school as a part of *Bay 'Al-' inah*. This indicates that inter-school differences are largely terminological rather than conceptual (Asmak et. al, 2010).

From a linguistic perspective, the term *al-tawarruq* comes from Arabic words *al-wariq*, which refers to silver coins or dirhams. According to Ibn Faris, these words have two meanings of principles. First, it is related to the principal leaves (*al-waraq*), which symbolize fertility and greenery. Second, he refers to the color, especially the silver colour. Words *al-wariq* are also mentioned in the al-Quran:

فَابْعَثُوا أَحَدَكُمْ بِوَرِقِكُمْ هَذِهِ إِلَى الْمَدِينَةِ

"So, send one of you with this silver coin (*wariq*) of yours to the city...."

(*al-Kahf*, 18: 19)

Broadly, the term *al-tawarruq* carries the intention of efforts to get cash, the same is in the form of silver, gold, or paper.

From a juristic (*fiqh*) standpoint, *al-tawarruq* is defined as a form of buying and selling transactions that aim to get cash. This process involves the purchase of goods resiliently, then the goods are sold in cash to third parties at a lower price. This third party is not the seller of the origin of the item. A prominent *fiqh* expert, al-Manī (2015), explains that *al-tawarruq* is a mechanism used by someone to get cash without engaging in usury (*riba*). The method entails buying goods at a deferred price that includes a profit margin and then selling them to another party for immediate cash (Nurhisam, 2016).

This transaction is called *al-tawarruq* because the main purpose is not to own or use the item, but solely to get cash (*al-wariq*). This concept reflects the cunning in managing the transaction of authority while obeying the principles of shariah (Asmak et. al, 2010). BNM from is Shariah Resolutions in Islamic Finance defines *al-tawarruq* as a contract consisting of two sale and purchase contracts. The first involves the sale of an asset by the seller to the buyer in a formidable (delayed pay). Subsequently, the buyer in the first buying and selling will sell the same assets to third parties in cash and as well (BNM, Shariah Resolutions in Islamic Finance, 2010)

The AAOIFI laid the term *al-tawarruq* as the process of purchasing a commodity at a tough price determined through *musawamah* (bargaining) or *murabahah* (selling with profit) and then selling the commodity to third parties at cash prices for the purpose of obtaining cash. In contrast, *Inah* refers to the process of purchasing a commodity at a tough price and sells it to the same party (rather than who the commodity was purchased) at a lower cash price (AAOIFI Shari'ah Standard, Monetization (Tawarruq), No.30, 2006).

Types of *al-Tawarruq*

Al-tawarruq can be categorized into several forms based on its implementation. The first type is referred to as *al-tawarruq al-Fardi* or *al-tawarruq al-Fiqhi*. In this form, a buyer gets goods on an installment basis from the first seller, then sells them to third parties in cash at a lower price. The main characteristic of this transaction is the absence of a relationship between the seller of origin and the second buyer (third party). Most scholars permit this form in theory, but there was a legal debate when it was used as a fixed mechanism to obtain cash financing.

The second type is the application of *al-tawarruq* in the Islamic Authority System, known as *al-tawarruq al-Masrifi* or *al-tawarruq al-Munazzam*. In practice, there is a possibility that the final buyer acts as an initial seller representative, or vice versa where the initial seller represents the final buyer in the transaction process. This second type often causes shariah problems because it involves more complex arrangements than individual forms (Ahmad et.al, 2020).

Views of Schools and Contemporary Scholars on *al-Tawarruq*

Views of Classical Scholars

In the Hanafi school, the two main characters are Abū Yūsuf and Muhammad bin Al-Hasan giving a vision of *al-tawarruq* status. Abū Yūsuf confirmed it if it involved three parties, while Muhammad bin Al-Hasan considered him to be reprehensible (*makruh*) if it only involved two parties. Ibn Hummam adds to the nuance by declaring the necessity of this transaction depending on the seller's knowledge about the true intention of the buyer - If the seller does not know the intention to get cash, the transaction is deemed permissible (Ahmad et al., 2017). The Maliki school did not discuss *al-tawarruq* explicitly. However, through analysis of their discussions on *buyū' al-'ajal* (deferred sales), it can be inferred that they tended to permit it, as

they did not include such transaction forms in the category of prohibited sales. The Syafi'i school shows a more open stance. Although they do not discuss *al-tawarruq* specifically, they permitted *bay' al-'inah* whose structure is tighter. Imam al-Shafi'i and al-Nawawi opined that the second sale at a different price constitutes a new, valid contract (Aprianto & Nazilah, 2023).

The Hanbali school explained the excitement of interesting opinions. Al -Bahūtī requires him as a solution to the needs of the authority, while Ibn Taymiyyah quotes two narrations from Imam Ahmad - one permitting and another discouraging it. Ibn Taymiyyah herself tends to be a view that is a matter of referring to the words of 'Umar Ibn' Abd Al-'Azīz who equates it with "the sibling of usury" (Ahmad et.al, 2020).

Views of Contemporary Scholars

Majma 'al-Fiqh al-Islāmī shows a significant evolution of views. At the 15th trial, they require traditional *al-tawarruq* (without initial agreement), but in the 17th trial it forbids an organized form (*al-tawarruq al-Munazzam*) which is practiced by financial institutions.

On the other hand, several prominent Middle Eastern banks such as HSBC Amanah and Arab National Bank continue to practice *al-tawarruq al-Munazzam* with the support of scholars such as Dr. Mūsā Adam 'Isā and Dr. Sulayman Naṣir Al-'ulwan. Meanwhile, scholars like Dr. Khalid Al-Musyayqah and Dr. Muhammad Al-Syaybanī rejected this practice because it was considered to deviate from the principle of shariah (Mokal et al., 2024).

Evidence and Scholarly Debate on Bay' *al-Tawarruq*

Opinion Permitting Al-tawarruq Transactions

Al-Quran

وَأَحَلَّ اللَّهُ الْبَيْعَ وَحَرَّمَ الرِّبَا

"But Allah has permitted trade and has forbidden interest "

(*al-Baqarah*, 2: 275)

This verse establishes the general principle of the permissibility of all forms of trade if there is no specific text prohibiting it. The term '*al-bai*' (trade) in this verse is comprehensive, covering various types of transactions, including *al-tawarruq*. Additionally, verse 282 in the same chapter regarding deferred transactions provides a basis for the deferred payment mechanism in *al-tawarruq*.

Hadith

A narration from Abu Hurairah RA recounts that the Prophet S.A.W said:

عن أبي هريرة رضي الله عنه أن رسول الله صلى الله عليه وسلم استعمل رجلا على خيبر فجاءه بتمر جنيب، فقال رسول الله صلى الله عليه وسلم: أكل تمر خيبر هكذا. قال لا، والله يارسول الله إنا لناخذ الصاع بالصاعين و الصاعين بالثلاثة. فقال رسول الله صلى الله عليه وسلم: لا تفعل، بع الجمع بالدرهم ثم ابتع بالدرهم جنيبا.

It was narrated from Abi Hurairah RA, that the Prophet SAW inaugurated a friend as an officer in Khaibar. The friend brings a date called (Janīb). Prophet SAW asked the friend: "Are there all Khaibar dates like this?" The friend answered: "By Allah, not O Messenger of Allah We bought this date one ṣā with this date of date as many as two ṣa' and if we buy these dates two ṣā in return for this date of date three

ṣā". Prophet SAW w said: "Don't do it like that. But sells all the dates with dirhams, then buy with the dirham dates Janīb".

Narrated by Abu Hurairah RA

This hadith shows the way Islam regulates transactions to avoid usury. The scholars see this as a basis for transactions such as *al-tawarruq* which involves the exchange of assets and eyes legally.

Arguments of Those Who Do Not Permit Bay' Al-tawarruq

Ibn Taymiyyah considers the sale and purchase of *al-tawarruq* a transaction that is always carried out by a group that is dealing with a state of pressure, that is a situation where customers are very in need of cash. They are the al-Quran, hadith and views related to the sale and purchase of these groups.

Al-Quran

وَأَحَلَّ اللَّهُ الْبَيْعَ وَحَرَّمَ الرِّبَا

"Allah has justified the sale and purchase and forbids usury"

(*al-Baqarah*, 2: 275)

In this verse Allah S.W.T has forbidden usury, while *Bay 'al-Inah* and *al-tawarruq* are the most almost usury intermediaries, and he is something for an illegitimate case and the law is also haram.

Al-Hadith

عن ابن عمر رضي الله عنهما قال: سمعت رسول الله صلى الله عليه وسلم يقول: " إذا تبايعتم بالعينة وأخذتم أذناب البقر ورضيتم بالزرع وتركتم الجهاد سلط الله عليكم ذلا لا ينزعه حتى ترجعوا إلى دينكم.

Instead of Ibn Umar Ra said, I heard the Prophet SAW said: "If you do the contract using Bay *'Al-inah* and take the tails of the ox and leave jihad, surely Allah will put humiliation to you who will not be appointed so that you return (repent) to your religion".

In addition, Abū Hurayrah RA narrated that the Prophet SAW said:

قال علي : قال ابن عيسى هكذا حدثنا هشيم قال : سيأتي على الناس زمان عضوض بعض الموسر على ما في يديه ولم يؤمر بذلك. قال الله تعالى : ولا تنسوا الفضل بينكم. وبياع المضطرون وقد نهى النبي صلى الله عليه وسلم عن بيع المضطر وبيع الغرر وبيع الثمرة قبل أن تدرك.

"Ali said: Ibn Isa said, this is what we have been discussed by Husayim. The Prophet SAW said:" There will be an era that applies in the tyranny and cruelty. At that time, the rich man was stingy about what they had, while it was not something that was ordered to him. Allah SWT said: "Don't forget your fellow mind". Then the group that is in a state of push and sell with the rich. Whereas the Prophet SAW forbade the sale and purchase of people who were pressed, the sale of something that was uncertain and the sale of fruit before being obtained "

Narrated by Abū Hurayrah RA

Ibn Qayyim explained that there were three parts in this transaction, namely:

- i. If the person in need is forced to buy something at a tough price, then sell it back to his master, then this is *Bay 'Al-Inah*; and
- ii. If he sells to people other than his master, he is recognized as bay' *al-tawarruq*; and
- iii. If it is sold to the third party where this third party has a relationship with the buyer and seller, then these three parts are used by people who practice usury. "Scholars who reject bay' *al-tawarruq* argue that the goal is to obtain cash, where the buyer ends up acquiring more cash than they started with essentially trading money for more money, which constitutes usury. The commodity is merely an intermediary, and its ownership is not the true objective.

The Concept of Financing in Islam

In matters of muamalat, there is no one proposition that gives detailed explanation of financing, either than the al-Quran or al-Sunnah. Explanations of financial dealings (*Muāmalat Māliyyah*) are only given in the form of maxims and general principles (Syibir, 2000). Therefore, the detailed explanation of the funding is not in the al-Quran and al-Sunnah because all *muamalat* affairs are only based on general principles such as *Qaedah al-Taradīs* and the prohibition of usury.

Nevertheless, the concept of financing can be explained based on the concept of loans because both have almost a similar objective, it provides ease of credit for those who need it. The difference between loans and financing is of aspects principle of shariah which is used in which loan is based on the principle of *al-qard al-hasan* as in the BIMB. When financing is also based on other principles such as the principle of selling, rent or partnership (Mahmud Saidun, 1994).

Shariah Application in Islamic Banking Financing

The business practices of IFIs should be based on the avoiding of several elements or criteria that are prevented by Islam. These elements are usury (*riba*), ambiguity (*gharar*), gambling (*maysir*), and speculation. Making these elements need to be shunned by Islamic banking institutions in offering financing, so the principle of buying and selling is practiced in Islamic financing based on the Word of Allah:

الَّذِينَ يَأْكُلُونَ الرِّبَا لَا يَقُومُونَ إِلَّا كَمَا يَقُومُ الَّذِي يَتَخَبَّطُهُ الشَّيْطَانُ مِنَ الْمَسِّ ذَلِكَ بِأَنَّهُمْ قَالُوا إِنَّمَا
الْبَيْعُ مِثْلُ الرِّبَا وَأَحَلَّ اللَّهُ الْبَيْعَ وَحَرَّمَ الرِّبَا فَمَنْ جَاءَهُ مَوْعِظَةٌ مِنْ رَبِّهِ فَانْتَهَى فَلَهُ مَا سَلَفَ
وَأَمْرُهُ إِلَى اللَّهِ وَمَنْ عَادَ فَأُولَئِكَ أَصْحَابُ النَّارِ هُمْ فِيهَا خَالِدُونَ

"Those who consume (transact with) usury cannot stand, except like people standing staggering because of the possession of the devil. Thus, it happened because they said that buying and selling was the same as usury. In fact, God has justified buying and selling and forbids usury. Anyone who has reached him a warning from his Lord (regarding usury), then he stops so that what he has gained first belongs to him and his affairs (whatever) to God. Who repeats (usury transactions), they are residents of hell. They are eternal in it".

(*al-Baqarah*, 2: 275)

To make sure the financing that is given in line with shariah, the certain shariah principles have been used as underlying contracts to Islamic financing such as *Bay' al-tawarruq*, *Bay' Bi Thaman Ajil*, *Bay' Al-Murābahah* and so on. In addition to the sale and purchase contract, there is also a financing that is realized based on the contracts, it is based on the principles of *al-*

Mudārabah and *al-Musyarakah*. The forms of Islamic financing according to instrument groups using various Shariah principles are shown in Table 1.

Table 1
Financing Contracts According to Islamic Shariah

Type of Financing	Financed Products	Shariah Principle
Equity Financing	Working Capital	<i>Al-Mudarabah, al-Musharakah</i>
	Project	<i>Al-Mudarabah, al-Musyarakah, Musharakah Mutanaqisah</i>
	House	<i>Musharakah Mutanaqisah, Ijarah Muntahiyah Bittamlik (IMBT), Commodity Murabahah, Istisna', Bay' Bithaman Ajil</i>
Term Financing	Vehicle	<i>Ijarah, Ijarah Muntahiyah Bittamlik, Commodity Murabahah, Musharakah Mutanaqisah, al-tawarruq</i>
	Property	<i>Bay' Bi Thaman Ajil, Musharakah Mutanaqisah, Murabahah</i>
	Personal	<i>al-tawarruq, Bay' al-'Inah, al-Qard al-Hasan</i>
	Islamic Export Credit Refinancing	<i>Murabahah, Bay' al-Dayn, Commodity Murabahah</i>
Trade Financing	Islamic Bills Receivable Letter of Credit Facility	<i>Murabahah, Bay' al-Dayn, al-Wakālah, Kafalah</i>
Investment Account	Saving Account Islamic Deposits	<i>Wadiah, Qard, Wakalah, Mudarabah, Wakalah, al-tawarruq</i>

Source: Authors' Analysis

Based on the author's analysis of 16 Islamic banks in Malaysia, all banks use the *al-tawarruq* contract for personal financing. It can be referred in Table 2.

Table 2
Offering of Personal Financing by Islamic Banks in Malaysia

Bank Name	Offers Personal Financing	
	Yes	No
Affin Islamic Bank Berhad	√	
Al Rajhi Bank	√	
Alliance Islamic Bank Berhad	√	
Asian Finance Bank Berhad	√	
Bank Islam Malaysia Berhad	√	
Bank Muamalat Malaysia Berhad	√	
CIMB Islamic Bank Berhad	√	
Hong Leong Islamic Bank Berhad	√	
HSBC Amanah Malaysia Berhad	√	
Kuwait Finance House (Malaysia) Berhad	√	
Maybank Islamic Berhad	√	
OCBC Al-Amin Bank Berhad	√	
Public Islamic Bank Berhad	√	
RHB Islamic Bank Berhad	√	
Standard Chartered Saadiq Berhad	√	
AmBank Islamic	√	

Source: Authors' Analysis

DISCUSSION OF FINDINGS

Personal Financing Based on Bay'al-Tawarruq at Bank Islam Malaysia Berhad (BIMB) and Bank Muamalat Malaysia Berhad (BMMB)

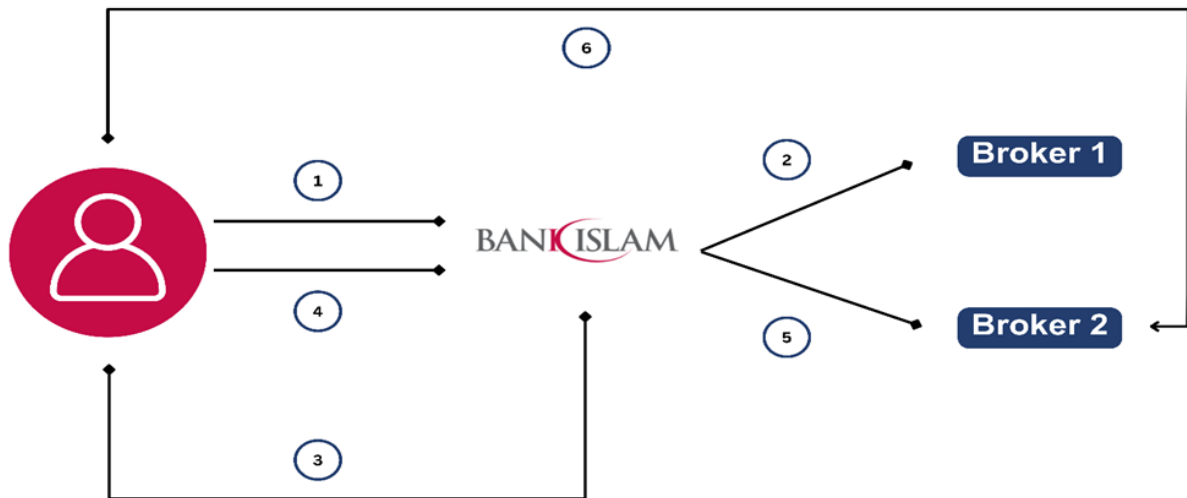
BIMB and BMMB are among the Islamic banking institutions in Malaysia that apply the bay' *al-tawarruq* contract in their financing products. BIMB has specifically utilised the *al-tawarruq* concept in offering personal and housing financing. The implementation structure involves a process where the customer applies for financing, the bank purchases a commodity from the market (e.g., the London Metal Exchange, LME) and then sells it to the customer on a deferred basis. The customer then appoints the bank as an agent (*wakil*) to sell the commodity to a third party, and the sale proceeds are credited into the customer's account (Fadilah & Nuzul Baharudin, 2014).

Furthermore, BIMB also applies the *al-tawarruq* concept in personal and housing financing. This bank is also listed among the financial institutions that use this concept in financing (Fadilah & Nuzul Baharudin, 2014). The use of bay' *al-tawarruq* at BIMB reflects positive development in the Islamic banking industry in Malaysia, which is increasingly inclined to use financial instruments considered more compliant with Shariah requirements. In terms of product structure and flexibility, BIMB is seen as more prominent in terms of transparency and Shariah-based documentation. Emphasis on comprehensive documentation allows BIMB to present a more transparent product implementation, trusted by customers and Shariah authorities.

A study by Kasmon (2014) adds that BIMB uses palladium as its commodity, while RHB Islamic Bank uses prepaid credit. Although both are not contrary to AAOIFI guidelines in terms of commodity type, BIMB uses a foreign commodity, which is less recommended by AAOIFI. Additionally, customers at both banks appoint the financial institution as an agent before taking ownership of the commodity, which does not meet AAOIFI's conditions on representation. The study also emphasises the importance of more detailed guidelines and oversight of financial institutions' operational compliance to ensure each transaction genuinely reflects the dictates of Shariah law and its higher objectives (*maqasid*).

Figure 1 below explained the modus operandi of the *al-tawarruq* commodity in personal financing products carried out by the BIMB:

Figure 1
Modus Operandi of Commodity al-Tawarruq by BIMB



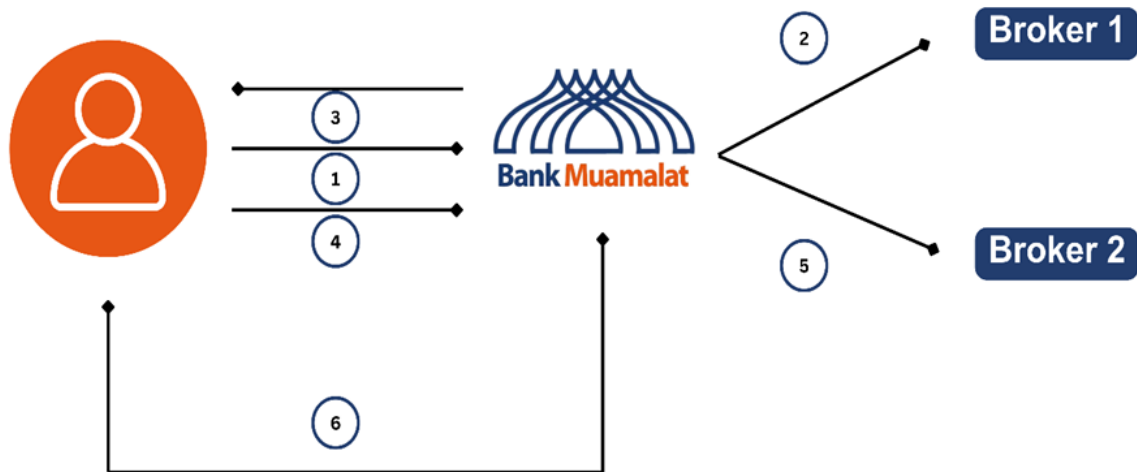
Source: Bank Islam Malaysia Berhad

The following is a concise and structured description of the *al-tawarruq* based financing process:

- 1) Financing Application
The customer applies for a financing product utilising the *al-tawarruq* concept from the bank.
- 2) Transaction Documentation
The bank obtains and completes the necessary *al-tawarruq* transaction documents from the customer.
- 3) Commodity Purchase by the Bank
The bank buys a commodity (e.g., metal) from the London Metal Exchange (LME) via Broker 1.
- 4) Commodity Sale to the Customer (*Murabahah*)
Under a *Murabahah* contract, the bank sells the commodity to the customer at a deferred sale price (i.e., cost price plus the bank's profit margin).
- 5) *Wakalah* Appointment by the Customer
The customer appoints the bank as an agent (*wakil*) through a *Wakalah* contract to sell the previously bought commodity on their behalf.
- 6) Commodity Sale by the Bank (as Agent)
Acting as the agent, the bank sells the commodity to Broker 2 in the open market.
- 7) Proceeds Credited
The proceeds from the sale of the commodity (known as *al-wariq*) are credited to the customer's account.
- 8) Repayment by the Customer
The customer repays the bank in instalments, according to the agreed-upon principal financing amount and profit.

The following is also a modus operandi *al-tawarruq* for personal financing carried out by BMMB based on the release of Mahyudin and Che Seman (2014).

Figure 2
Modus Operandi of the *al-Tawarruq* Transaction at BMMB



Source: Bank Muamalat Malaysia Berhad

Figure 2 above provides a concise and structured description of the *al-tawarruq* based financing process:

- 1) Customer Application and Purchase Requisition
The customer approaches the bank to apply for financing by submitting a formal purchase requisition and completing all required documentation.
- 2) Bank's Commodity Purchase
Based on this requisition, the bank proceeds to purchase a commodity from the First Commodity Trader.
- 3) Murabahah Sale to Customer
The commodity acquired by the bank is subsequently sold to the customer via a Murabahah contract.
- 4) The customer subsequently appoints the bank as their agent (*wakil*) to sell the commodity on their behalf to a third-party buyer.
- 5) Cash Sale by Bank (as Agent)
Acting as the customer's agent, the bank executes the sale of the commodity to a Second Commodity Trader for cash.
- 6) Proceeds Credited to Customer
The proceeds from this sale are deposited by the bank into the customer's account.

A customer in need of cash visits the Bank to obtain financing facilities. As a preliminary step, the customer submits a purchase requisition accompanied by a binding commitment to purchase a specified asset from the Bank. Concurrently, the customer grants the Bank a limited power of attorney to receive and manage the buy-sell transaction of the said asset on their behalf. The Purchase Requisition submitted by the customer is final and irrevocable once issued. Several related documents are also required in this process, including:

- i. Purchase Request:
This document states the customer's intention to purchase a commodity and simultaneously requests the bank to procure the said commodity first.
- ii. Binding Promise to Purchase (*Wa 'd Mulzim*):

This is a formal commitment from the customer to buy the commodity acquired by the bank from the first commodity trader at a pre-agreed sale price, immediately after the bank executes the purchase.

iii. Specific Agency for Contract Execution (*Wakālah Khāṣṣah*):

At this stage, the customer appoints the bank as a special agent with limited power to perform a specific task: to execute the purchase agreement for the commodity from the bank itself. In other words, the bank acts on behalf of the customer to accept the commodity and subsequently enter a *Murabahah* sale contract with itself (the bank).

Now, the customer also issues a formal letter of appointment authorising the bank to act as their agent to sell the commodity to another commodity trader after the *Murabahah* sale is finalised. Based on the purchase request submitted by the customer, the bank executes the purchase of the commodity from the commodity trader (first trader) at the cost price, which is equivalent to the amount of financing requested by the customer. As proof of transferred ownership, the commodity trader delivers a Commodity Holding Certificate along with a delivery order to the bank.

Pursuant to the Binding Promise to Purchase (*Wa 'd Mulzim*) provided by the customer, the bank sells the commodity to the customer under a *Murabahah* contract, i.e., at a sale price encompassing the cost price plus the bank's profit margin. This amount is payable by the customer to the bank on a deferred or instalment basis. As a restricted agent appointed by the customer, the bank executes the purchase of the commodity on the customer's behalf through the *Murabahah* sale contract.

The customer also appoints the Bank as an agent (*wakālah*) to execute the sale of the acquired commodity to another commodity trader. Based on this letter of appointment, the bank sells the commodity on the customer's behalf to a Second Commodity Trader. Upon completion of the sale with the commodity trader, the bank transfers the proceeds, which amount to the value of the financing, into the customer's designated account.

Significant Challenges in Current *al-Tawarruq* Practice

Although most IFS in Malaysia including BIMB and BMMB implement *al-tawarruq* contract, this study found three challenges and criticisms in the current practice of *al-tawarruq* as below:

Shariah Compliance Issues and Scholars' Perceptions

The application of *Bay' al-tawarruq*, especially in the form of Organized *al-tawarruq (al-tawarruq al-munazzam)* is often criticized for allegedly containing elements that resemble *riba* and legal stratagems (*hilah*), as well as for not fulfilling the objectives of *maqasid syariah*. Many international fatwa bodies such as the OIC Fiqh Academy and AAOIFI have prohibited *al-tawarruq*, which has somewhat affected the reputation of IFSs at the global level (Yusoff et al., 2016). Although BNM allows its use, there is a lack of alignment with international standards (Fa-Yusuf, & Ndiaye 2017).

Commodity Issue

Al-tawarruq commodities do not actually exist but are merely documents processed by parties from one place to another, or the same commodity is used in multiple *murabahah* transactions, which renders *al-tawarruq* invalid and prohibited. It results in obtaining money for money without any real exchange taking place. For example, in international markets such as the London Metal Exchange (LME), it has been found that commodities like metals are never actually transferred in ownership or delivered to the buyer. The same commodity can be sold multiple times in a short period electronically, without any physical delivery or real ownership

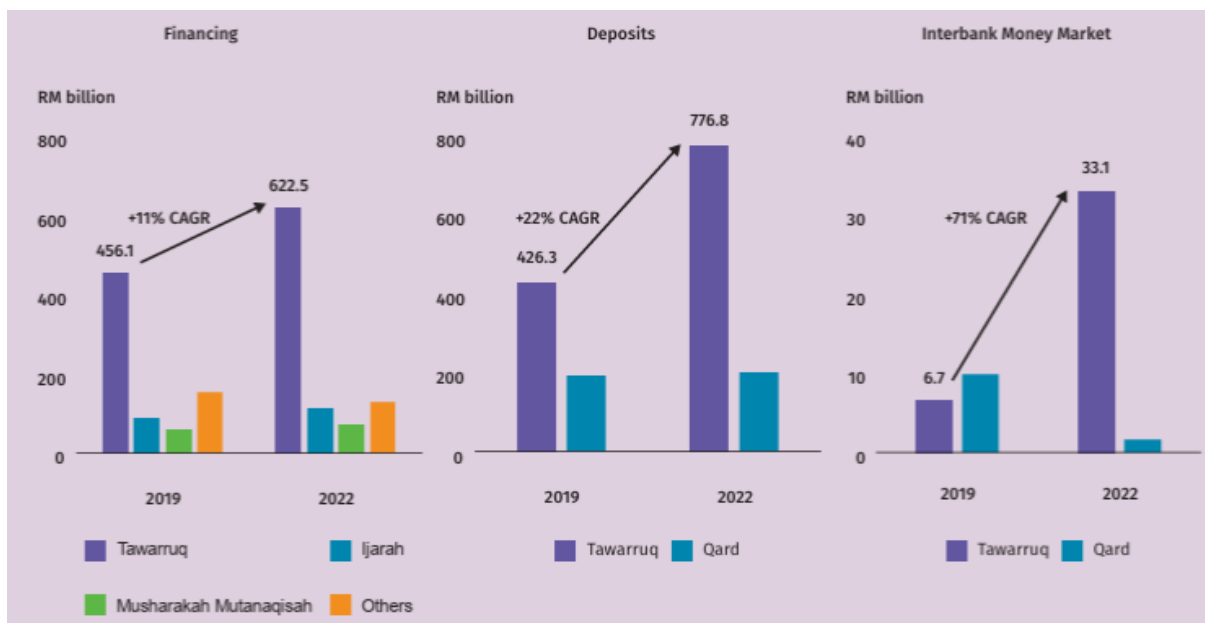
(Abbasi & Aziz 2023). Additionally, there have been cases where the commodities used are damaged or junk metals that have no market value, merely to fulfill contract documentation requirements. This raises doubts as to whether the transactions truly involve valuable and existing goods (Ahmad et, 2020). In fact, some transactions only involve the exchange of certificates or documents, without any physical movement of assets. The same broker controls both parties in the transaction, making the process merely a paper cycle with no real value.

Overreliance & Lack of Innovation

Ishak et.al., (2025) said that excessive reliance on *al-tawarruq* has led to a lack of product innovation and has hindered the development of more authentic Islamic financing instruments. BNM (2022) has urged Islamic banks to diversify beyond *al-tawarruq* based products and promote non-commodity Shariah contracts to reduce reliance and market risk. However, *al-tawarruq* is deeply entrenched in current Islamic finance practices, so abrupt changes could disrupt operations and customer expectations. Some believe alternative products are less efficient and riskier in terms of Shariah compliance. Thus, the consequences of *al-tawarruq* overuse should be assessed using the principle of *maalat*, focusing on real-world outcomes. BNM (2022) also highlighted the significant increase in the use of *al-tawarruq* contracts across financing, deposits, and the interbank money market in Malaysia from 2019 to 2022. *Al-tawarruq* dominates all three segments, with compound annual growth rates (CAGR) of 11% in financing (rising from RM456.1 billion to RM622.5 billion), 22% in deposits (from RM426.3 billion to RM776.8 billion), and a striking 71% in the interbank money market (from RM6.7 billion to RM33.1 billion). As illustrated in Figure 3, these upward trends confirm the growing dominance of *al-tawarruq* across key Islamic finance segments in Malaysia. This trend highlights the growing reliance on *al-tawarruq* compared to other shariah contracts such as *ijarah*, *musharakah mutanaqisah*, and *qard*.

Figure 3

Trend and composition of al-Tawarruq and other Shariah contracts



Source: Bank Negara Malaysia (2022)

CONCLUSION

In conclusion, this study demonstrates that the *bay' al-tawarruq* contract plays a significant role in the provision of personal financing by Islamic banking institutions in Malaysia, particularly at BIMB and BMMB. Despite various challenges and criticisms, both banks continue to adopt *bay' al-tawarruq* as the main mechanism in their financing products. The study also found that the implementation of *bay' al-tawarruq* in both institutions involves a structured operational process, compliance with Shariah documentation, and the use of supporting contracts such as *Wakalah* and *Wa'd Mulzim* to ensure transactions are conducted in accordance with Shariah requirements.

However, this study also highlights several key issues such as shariah compliance issues and scholars' perceptions, commodity issue, and overreliance and lack of innovation which may hinder product innovation and affect the reputation of the Islamic banking industry at the global level. Therefore, enhancements in monitoring, operational guidelines, and the diversification of Shariah contracts - particularly regarding the *al-tawarruq* contract - are essential to ensure that the implementation of *bay' al-tawarruq* genuinely fulfills the objectives of Shariah. This aligns with the recommendations provided by BNM. So that the Muslim community is not confused with the conventional products. Overall, this study meets its objectives by providing a comprehensive overview of the application of *bay' al-tawarruq* and its challenges in personal financing at IFs in Malaysia.

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