

Improvements in the Application of the Tawarruq Munazzam Contract in Malaysian Islamic Banking: An Analysis from a Shariah Perspective

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Abstract

This paper aims to examine the measures taken by selected banks in Malaysia to enhance the implementation of tawarruq munazzam contracts. As a qualitative study, the researcher gathered data through library research and empirical studies. The library research involved analyzing books, articles, and statutes, while the field studies consisted of unstructured interviews with eight participants, including officers and Shariah committees of Islamic Finance Institutions (IFI). The sample group was selected using the purposive sampling method. Consequently, the researcher identified several themes from the interview data, which were subsequently analyzed. Tawarruq munazzam was chosen as a case study due to its prevalence as the most popular financial instrument among Islamic banks in Malaysia. The research findings revealed nine issues related to the tawarruq munazzam contract. Furthermore, the study highlighted the lack of uniformity among the five surveyed banks in terms of their efforts to improve the practice of tawarruq munazzam contracts. Additionally, one unresolved issue identified by the study pertained to the inclusion of wakalah elements. Notably, the study found that one of the banks exhibited the highest level of improvement in the practice of tawarruq munazzam, addressing eight out of the nine issues raised.

Keywords: Shariah Advisor, Islamic Finance Institutions (IFI), Shariah Risk, Organized Tawarruq, Commodity Murabahah.

INTRODUCTION

Islamic banking was established in Malaysia in approximately 1963 as an alternative to conventional banking. The primary objective of establishing Islamic banking was to adhere to Shariah principles and avoid engaging in riba practices (al-Nasser & Muhammed, 2013; Asni, 2021). As per the Malaysian Islamic Banking Act 1983, an Islamic bank is defined as an organization that conducts Islamic financial business. Islamic financial business refers to banking activities that strictly adhere to Shariah principles (BNM, 1983). This definition clearly emphasizes that Islamic banks must abstain from any activities that contradict Shariah principles. Islamic banking serves as an intermediary in the Islamic economic system, aiming to establish a just, equitable, and harmonious society while aligning with the objectives of Shariah (*Maqasid al-Shariah*) (Ishak and Asni, 2020).

To enhance the overall system of Islamic banking, Malaysia has implemented a comprehensive legal framework for the industry known as the Islamic Financial Services Act 2013 (IFSA, 2013). The primary objective of this legislation is to promote financial stability and ensure adherence to Shariah principles. This objective is clearly articulated in clause 28, which states that "(1) every institution must consistently ensure that its aims, operations, business, affairs, and activities are in compliance with Shariah. (2) Compliance with any ruling issued by the Shariah Advisory Council pertaining to specific purposes, operations, businesses, affairs, or activities shall be considered as compliance with Shariah with regard to said aims, operations, businesses, affairs, or activities" (Act 759 IFSA, 2013).

Among the prominent Islamic banking products in Malaysia are the *tawarruq munazzam* contract-based products offered by 16 IFIs (BNM, 2024). This hybrid contract is derived from the *tawarruq fiqhi* contract, as explained in fiqh muamalat (Islamic law of transactions). It has been modified to align with the modern financial system by incorporating elements such as the *murabahah li al-amir bi al-shira'* contract, *wakalah* (representation), an easily marketable underlying asset, *ibra'* (rebate), *ta'wid* (fine), *wa'ad* (promise), and risk reduction for banks (Asni & Sulong, 2018). The concept of *tawarruq munazzam* was selected due to its suitability in facilitating cash liquidity

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for cash-based financial instruments (Asni et al., 2023). Consequently, this concept is compatible with various facilities provided by Islamic banking, including deposits, loans, bonds, and money market instruments (Ahmad et al., 2022).

Although the modification aimed to support the sustainability of Islamic banking operations within the modern financial system, it has faced controversy due to widespread criticism of the contract's compliance with Shariah principles by both local and international Islamic financial researchers (Syahmi et al., 2022; Ali and Hassan, 2020; Yusoff, Ahmad, & Nik Abdul Ghani, 2019; Mohamad & Ab Rahman, 2014). Notably, independent research bodies recognized by the international Muslim community, such as Majma' Fiqh al-Islami (IIFA, 2009) and AAOIFI (2015), have also voiced their concerns.

According to the findings of a study conducted by Asni (2022), there is evidence of Shariah non-compliance in the implementation of products based on *tawarruq* contracts. Several issues have been disputed, including customer engagement, *wa'ad* (promise), commodity asset, *gharar* (uncertainty), cost, and the presence of willing but unable debtors in *tawarruq* products offered by Islamic banking in Malaysia. Additionally, a study by Syahmi et al. (2022) revealed the presence of trickery (*hiyal*) in the implementation of *tawarruq* contracts offered by Islamic banking, posing Shariah risks. In light of these criticisms, this study aims to assess the improvements made by Islamic banking in Malaysia to address and mitigate the Shariah risks associated with the *tawarruq munazzam* contract, as highlighted in previous studies.

In recent research, numerous studies have concentrated on enhancing various aspects of Islamic banking, such as management, governance, technology, the legal system, administration, and service quality. For instance, Ismail (2010), Can et al. (2022), and al-Qemzi et al. (2022) have examined the enhancement of liquidity management in Islamic banking in Indonesia, Turkey, and the UAE. Meanwhile, Noordin and Kassim's (2019) study has highlighted the importance of strengthening the composition of Shariah committees to promote the development of Shariah Governance Framework (SGF) in Malaysia. Additionally, Ahmad et al. (2023) have conducted a comparative analysis of the Shariah governance frameworks of Islamic banks in Malaysia and Pakistan. Ahmed et al. (2022) have suggested that the quality of service provided by workers in Islamic banks should be improved, while Azis and Kamal's (2019) study has indicated the need for improvements in information technology from a customer perspective.

Similarly, Hassan et al. (2018) have found that the administration of al-Rajhi Bank needs to be enhanced. This study, however, differs from previous ones that focused on Shariah risk in Islamic banking products by using the *tawarruq munazzam* contract as a case study. The findings of recent studies highlight the significance of research on the improvement of Islamic banking.

LITERATURE REVIEW

According to BNM (2019), *tawarruq munazzam* refers to a two-stage transaction. In the first stage, the buyer purchases credit from the original seller of an asset. In the second stage, the buyer later sells the asset for cash to a third party. This transaction is called *tawarruq* because the buyer has no intention of using or leveraging the asset, but solely wants to resell it for cash. It is also known as commodity murabahah and is used in products such as deposits, financing, asset and liability management, and risk management.

In 2005, the SAC of BNM approved *tawarruq*-based contracts at its 51st meeting on July 28 (BNM, 2019). However, the resolution made regarding *tawarruq* was only general at that time. On November 17, 2015, BNM issued specific guidelines on the operation of *tawarruq* products, which must comply with IFIs (BNM, 2015). The following diagram depicts the general operation of *tawarruq* contracts as issued by BNM:

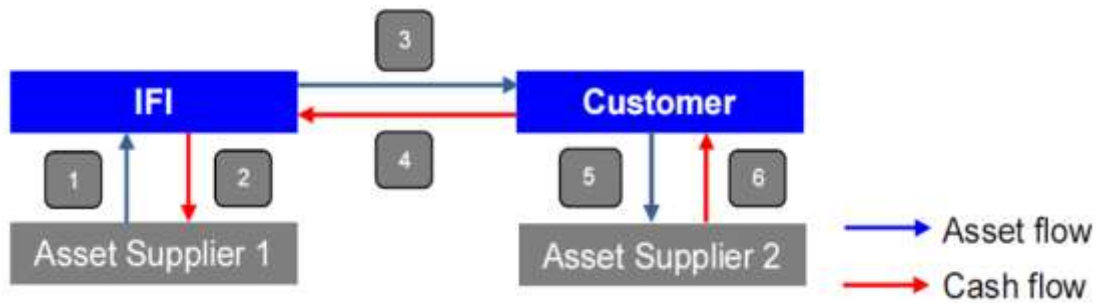


Figure 1. Tawarruq Munazzam financing guidelines issued by BNM (2015).

For instance, when a customer requires financing of RM100,000 from the IFI, the IFI engages in a *tawarruq* arrangement.

The IFI purchases an asset from Asset Supplier 1 at a selling price of RM100,000.

The IFI makes a cash payment to Asset Supplier 1.

Subsequently, the IFI sells the asset to the customer at an agreed selling price of RM120,000 (RM100,000 + profit RM20,000).

The customer makes deferred payments through monthly installments over a period of five years.

Next, the customer appoints the IFI as its agent to sell the asset-to-Asset Supplier 2 immediately at a selling price of RM100,000.

By doing so, the customer obtains the cash of RM100,000 required for financing.

The cash sale from the customer to Supplier Two enables the customer to obtain cash, while the credit sale from the Islamic financial institution (IFI) to the customer creates a financial obligation that the customer must fulfill within the agreed period. These guidelines are generally followed by IFIs licensed under BNM, as all Islamic banking activities in IFIs are subject to the sanctions set by the SAC of BNM (BNM, 2019). According to Mohamad and Ab Rahman (2014), the *tawarruq* contract practiced in Malaysia is a type of *munaẓẓam* because it incorporates the *wakalah* element in the contract. The following is a list of IFIs that utilize *tawarruq*-based contracts:

Table 1. List of IFIs using the tawarruq-based contracts (BNM, 2024).

No	Islamic Banking	Tawarruq-based contracts
1	Kuwait Finance House (Malaysia) Berhad	✓
2	HSBC Amanah Malaysia Berhad	✓
3	Al Rajhi Banking & Investment Corporation (Malaysia) Berhad	✓
4	Alliance Islamic Bank Berhad	✓
5	Bank Rakyat	✓
6	Bank Islam Malaysia Berhad	✓
7	Bank Simpanan Nasional	✓
8	Maybank Islamic Berhad	✓
9	AmBank Islamic Berhad	✓
10	Hong Leong Islamic Bank Berhad	✓
11	Affin Islamic Bank Berhad	✓
12	Bank Muamalat Malaysia Berhad	✓
13	CIMB Islamic Bank Berhad	✓
14	RHB Islamic Bank Berhad	✓
15	MBSB Bank Berhad	✓
16	Standard Chartered Saadiq Berhad	✓

Currently, there are 16 Islamic financial institutions (IFIs) that offer *tawarruq*-based contracts. This makes the *tawarruq munaẓẓam* contract-based product the most prominent product in Malaysia's Islamic financial sector when compared to other contracts.

Shariah Risk in Tawarruq Munazzam

Based on previous studies, there are several criticisms of the *tawarruq munazzam* contract. These include its use in house financing, customer engagement, the inclusion of the *wa'ad* element, commodity assets, the *wakalah* element, *ta'wid* and *gharamah* fines, refinancing, the presence of *gharar* (uncertainty), and the failure to distinguish between different debtor situations. Researchers, such as al-Suweilam (2004), have suggested minimizing the use of the *tawarruq* contract by banks for house financing, as it primarily serves liquidity purposes and is susceptible to fraudulent practices. This recommendation is also supported by AAOIFI (2015). Additionally, some researchers propose that equity-based contracts, such as the *musharakah mutanaqisab* contract, are more suitable for house financing. Bahari et al. (2019) conducted a recent study that supports this claim, stating that the *musharakah mutanaqisab* contract better serves the welfare of clients and aligns with the *maqasid al-Shariah*. Similarly, Ariffin et al. (2015) found that equity-based financing, specifically *musharakah mutanaqisab*, is a more just and equitable alternative to debt-based financing.

AAOIFI (2015) recommends offering the *tawarruq munazzam* contract to clients who are in need of immediate cash and have good intentions. Similarly, BNM (2010) states that any financing should be provided for a valid purpose. Concerning the issue of *wa'ad mulzim* (binding promise), Majma' al-Fiqh al-Islami (IIFA 1998) has ruled that including binding promises in the *murabahah li al-amir bi al-shira'* contract, which is part of the *tawarruq munazzam* contract, does not comply with Shariah. Majma' al-Fiqh al-Islami only permits non-binding promises. Furthermore, al-Quradaghi (2011) criticizes the use of commodity assets in the *tawarruq munazzam* contract, highlighting instances of defective commodities found in international commodity markets. Abu Ghuddah (2008) also notes that there is no guarantee of multiple buyers for the same commodity in the LME medium. Additionally, Ali (2018) points out that *tawarruq* transactions in the international commodity market involve damaged aluminum that has been stored for more than ten years. This commodity is utilized because it cannot be sold in the market.

The inclusion of the *wakalah* element in the *tawarruq munazzam* contract has been criticized by Majma' Fiqh al-Islami. This inclusion has led to the exposure of trick issues in the *tawarruq* contract. Similarly, AAOIFI does not encourage the inclusion of the *wakalah* element in the *tawarruq munazzam* contract. According to Ali (2018), the inclusion of the *wakalah* element has caused similarities between the arrangement in the *tawarruq munazzam* contract and *bay' 'inah*, resulting in the ban of *bay' 'inah* from being substituted in the *tawarruq* contract due to reasoning of Islamic law (*'illah*).

The imposition of *ta'wid* and *gharamah* fines in the *tawarruq munazzam* contract has been criticized by several researchers. Al-Khafif (1997) stated that the imposition of *ta'wid* can lead to the practice of *riba*, as the theoretical benefit brings usury, even if it is converted to punishment. This view was supported by Majma' Fiqh al-Islami (IIFA, 2000) and AAOIFI (2015). According to Sha'ban (1977), debtors who deliberately fail to pay their debts must be given a government-imposed penalty (*ta'zir*). Regarding the imposition of the *gharamah* penalty, al-Quradaghi (2008) stated that the majority of scholars prohibit its imposition, even if the proceeds go to charitable bodies. This is because, when the condition for imposing the *gharamah* is *riba*, the term is considered illegal (*batil*), regardless of whether the proceeds go to charities or not. Similar opinions were expressed by Majma' Fiqh al-Islami (IIFA, 2000) and AAOIFI (2015).

Majma' Fiqh al-Islami (IIFA, 2006) defines *qalb al-dayn*, which is prohibited by Islamic law, as a transaction of sale of goods between the debtor and the creditor, where a new debt is created for the debtor to amortize the first debt, either in whole or in part. This definition is consistent with the study of al-Muni' (2011), which states that *qalb al-dayn* is only available to people who can pay their debts (*musir*). It is used to obtain cash and is not required to pay off the first or past debt. According to Abu Ghuddah (Mish'al, 2014), *qalb al-dayn* is permissible under certain conditions: it should have no connection with the first or past debt, and the purpose of the debt should not be to settle the first or past debt.

In previous studies on the issue of *gharar*, it was found that elements of *gharar* existed in the subject of the contract, sale price, continuity of contract, and *qabd* when studying the implementation of *tawarruq*'s personal

financing contract at Bank Islam Malaysia Berhad (BIMB) (Thaidi, 2014). On the issue of distinguishing the debtors' situation, according to al-Nawawi (1392H), scholars have unanimously agreed (*ijma'*) that it is necessary to give time to poor or incapacitated debtors until they are in a position to pay off their debts.

METHODOLOGY

The study utilizes a qualitative approach, incorporating both secondary information obtained from library sources and primary information gathered through semi-structured interviews. The secondary data encompasses the concept of *tawarruq munazzam* and its implementation in Malaysia, as well as the Shariah risk associated with *tawarruq munazzam*, sourced from books, journals, circulars, and relevant authoritative websites. This data was crucial in constructing the framework for the field study.

For the empirical aspect of the research, the researcher conducted interviews with a total of eight participants, consisting of officials and Shariah committees from five Islamic banks. These interviews aimed to gather comprehensive insights into the measures implemented by the studied banks to enhance the *tawarruq munazzam* contract. The researcher employed a purposive sampling technique to select interviewees with relevant experience and expertise in addressing the study's objectives (Etikan & Alkassim, 2016).

Table 2. The list of interviewees.

Interviewee	Position	Purpose
Interviewees (IV1, IV2, IV3, IV4, IV5)	Officers of Islamic Banks	This group was selected due to their responsibility of drafting an initial Islamic-compliant product in the field of Islamic banking.
Interviewees (IV6, IV7, IV8)	Shariah Committees of Islamic Banks	This group was selected due to their authority in providing product validation.

Once the interview data has been collected and transcribed, the researcher will proceed to analyze it using the qualitative analysis method. The qualitative method is commonly employed to describe the behavior of a research study (Effendi, 2013). Consequently, the researchers will be able to assess the enhancements made by banks to the *tawarruq munazzam* contract in response to the Shariah risk highlighted in prior studies.

RESULT

For the sake of clarity, the results are summarized in Table 3.

Table 3. Interview Results and Themes.

	Results and Quotations	Themes
1.	Regarding the utilization of the <i>tawarruq munazzam</i> contract for house financing products, banks A and B have transitioned to <i>musbarakah mutanaqisab</i> contracts. Here is a statement from one of the respondents explaining the conversion: <i>"The bank has decided to switch from tawarruq munazzam contract to musbarakah mutanaqisab contract for house financing products due to Shariah concerns associated with the former. In light of this, we have followed the guidance of AAIOfI and several scholars by offering the tawarruq munazzam contract only for products that lack alternative options, such as personal financing products. The adoption of the musbarakah mutanaqisab contract for house financing products has garnered significant support, particularly among experts in the field of Islamic finance. While the tawarruq munazzam contract continues to be used for personal financing products, the bank is actively striving to minimize any potential Shariah-related issues associated with the contract."</i>	Convert house financing products from <i>tawarruq munazzam</i> contract to alternative contracts.
2	On the matter of customer engagement in the <i>tawarruq munazzam</i> contract, it was found that only Bank A had effectively addressed the issue. One of the respondents stated, <i>"Due to the Shariah concerns surrounding the tawarruq munazzam contract, the bank restricts its offering to customers who genuinely require significant amounts of cash, such as for home repairs. Additionally, the bank thoroughly investigates each customer's background and the purpose of their financing request, in order to ensure the funds are not used for illicit activities, such as funding brothels or liquor factories. Previously, the bank had not implemented the requirement for customers to apply for Shariah-compliant financing."</i>	<i>Tawarruq munazzam</i> products are exclusively available to customers facing financial necessity.
3	On the matter of <i>wa'ad</i> , it was discovered that only three banks - banks A, B, and C - did not incorporate the <i>wa'ad</i> element into the contract where it had previously been utilized. As stated by one of the participants, <i>"The bank has enhanced the tawarruq munazzam contract by excluding the wa'ad element due to its potential Shariah risk when included in the murabahah li al-amir bi al-shira' contract utilized"</i>	Do not utilize the <i>wa'ad</i> element in the <i>tawarruq munazzam</i> contract.

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	<i>in the tawarruq munazzam contract. The inclusion of wa'ad could also compromise the customer's right, as the bank does not yet possess the asset at the time of contract execution."</i>	
4	<p>In relation to commodity assets, it was discovered that all the banks surveyed have ceased utilizing the international commodity medium and have transitioned to locally-based, Shariah-compliant commodities approved by BNM. This statement was made by one of the respondents:</p> <p><i>"Previously, the bank used an international commodity medium known as LME. However, monitoring became challenging due to the management of commodities overseas and concerns regarding Shariah risk associated with the medium. Considering these factors, the bank has now shifted to the local BSAS medium, which is easier to monitor and has been certified as Shariah-compliant by BNM. It is important to note, however, that the cost of this medium is higher compared to the LME medium."</i></p>	Utilizing BSAS as a platform for acquiring commodity assets.
5	<p>On the issue of <i>wakalah</i>, all the surveyed banks continue to incorporate the <i>wakalah</i> element in the tawarruq munazzam contract within their personal financing products. As stated by one of the respondents,</p> <p><i>"The use of the wakalah element persists in our bank's contracts, despite the emergence of controversial concerns, such as fraudulent practices. This is primarily because the bank has not yet identified an alternative solution to address this issue. Moreover, the inclusion of the wakalah element in the contract holds significant importance for both the bank and the customer's well-being. Eliminating the wakalah element would impose a financial burden on customers, who would then be responsible for covering high shipping costs for assets acquired from overseas, seeking new buyers, and selling the purchased assets back to the bank. Additionally, it serves as a protective measure against the potential depreciation of assets held by the customer over an extended period of time. Therefore, without the presence of the wakalah element, the objective of personal financing cannot be effectively achieved."</i></p>	Utilizing the wakalah element within the tawarruq munazzam contract.
6	<p>On the matter of imposing <i>ta'wid</i> and <i>gharamah</i> fines, it appears that bank A has taken measures to refrain from penalizing its customers. This was confirmed by one of the respondents, who stated:</p> <p><i>"While some banks impose both ta'wid and gharamah fines, and others impose only ta'wid fines, our bank does not impose any fines. In the event of a customer's default, the bank reserves the right to offset any outstanding balance in their Personal Financing-i account against any credit balance in their account with the bank. Additionally, legal action may be taken to recover the unpaid amounts. This may include pursuing bankruptcy or other appropriate legal remedies. The customer will be responsible for all legal costs incurred in the recovery process. It is important to note that legal action against the customer can negatively impact their credit rating, potentially making it more difficult or expensive for them to obtain credit. Our bank does not impose penalties for ta'wid and gharamah fines due to the Shariah risk associated with usury."</i></p> <p>However, banks D and E have chosen to only impose <i>ta'wid</i> fines when it comes to the issue of <i>ta'wid</i> and <i>gharamah</i>. According to one of the respondents:</p> <p><i>"Our bank no longer imposes gharamah fines because we do not wish to incur the cost of distributing the proceeds to charitable causes. We solely impose ta'wid fines to ensure the well-being of the bank and provide compensation."</i></p> <p>Meanwhile, banks B and C also utilize <i>ta'wid</i> in their imposition of fines. However, it was found that there is a slight difference in their approach, as they first contact the customer to assess their ability to afford the fine in the event of default. According to one of the respondents:</p> <p><i>"In cases of non-compliance, we impose ta'wid fines. However, before imposing a fine, we make it a point to contact the customer and assess their situation to determine whether they are able to afford it or not. If they are unable to afford it, we engage in a discussion with the customer."</i></p>	Imposing <i>ta'wid</i> and <i>gharamah</i> fines.
7	<p>Regarding the matter of refinancing, it was discovered that Bank A is the only institution that does not permit the refinancing process in financing <i>tawarruq munazzam</i>, which is based on personal financing products. As stated by one of the respondents,</p> <p><i>"The bank abstains from facilitating refinancing in financing operations to prevent the occurrence of qalb al-dayn, which may give rise to usury-related concerns."</i></p>	Refinancing in <i>tawarruq munazzam</i> contract.
8	<p>On the issue of <i>gharar</i>, all the surveyed banks have addressed the matter by providing detailed information about the assets in terms of type, quantity, and price of commodity sales, which is then presented to customers for their approval. According to one respondent,</p> <p><i>"Previously, customers were unaware of the type, quantity, and price of the asset during the offer to purchase (OTP) agreement. This information only became available after signing the acceptance of purchase (AOP) form, which was based on the commodity sales obtained from the second broker. However, more recently, banks have started disclosing the type, quantity, and price of the asset to customers before they agree to purchase it. This is done to meet the requirements and terms of the sale."</i></p>	<i>Gharar</i> issue in <i>tawarruq munazzam</i> contract financing.
9	<p>Regarding the matter of failing to differentiate between debtors, it was discovered that only banks B and C conducted investigations on the debtors, regardless of whether they were categorized as debtors who defaulted due to difficult</p>	Do not fail to consider the debtors' circumstances.

	circumstances (<i>mu'sir</i>) or those who were capable (<i>musir</i>). According to one of the interviewees, <i>"In cases of non-compliance, we will levy a ta'wid fine. However, prior to imposing the fine, we will first contact the customer to assess their financial capacity. If they are unable to afford the fine, we will engage in a conversation with the customer to address the matter."</i>	
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DISCUSSION

The issues under study are based on the key findings from previous research that identify the challenges surrounding the *tawarruq munazzam* contract in relation to Shariah compliance. Upon analysis, it was discovered that all five banks have made efforts to enhance the implementation of *tawarruq munazzam* contracts in order to adhere to Islamic law and mitigate Shariah risk. However, there were inconsistencies among these banks in addressing the Shariah-related concerns identified.

Regarding the utilization of the *tawarruq munazzam* contract in house financing products, bank A has opted not to use this contract for house financing, instead opting for an *ijarah*-based contract. Meanwhile, bank B is in the process of transitioning from a *tawarruq munazzam* contract to a *musharakah mutanaqisab* contract. The reason behind this shift is the desire to minimize the usage of the controversial contract in banking practices. Both banks perceive *tawarruq munazzam* as a contract that should only be applied to products where no alternative exists. This aligns with the suggestion made by AAOIFI (2015) to limit the use of *tawarruq munazzam* contracts. According to al-Suweilam (2004), banks should restrict the use of the *tawarruq* contract solely for liquidity financing purposes. However, for housing financing, there are numerous other Shariah-compliant contracts that are more suitable. MM home financing has been offered as a superior alternative to many other Islamic home financing products available in the market (Mydin-Meera et al., 2009; Abdul-Razak and Amin, 2013; Asadov et al., 2018). Home financing based on the *ijarah muntabiyah bi al-tamlik* contract and *ijarah mausufah fi al-dhimmah* are considered Shariah compliant (Asni and Sulong, 2018; Hakimah et al., 2015). This proactive step taken by both banks demonstrates their commitment to Shariah compliance, despite the absence of any explicit restrictions from BNM on the usage of the *tawarruq munazzam* contract in house financing.

Regarding customer engagement, the study reveals that only bank A requires thorough evaluation of customers' financial needs, particularly in cases where they require a significant amount of funds to repair a home damaged by a disaster. The bank also conducts background checks to assess customers' intentions behind seeking financing, ensuring that the funds will not be used for prohibited purposes under Shariah. On the contrary, banks B, C, D, and E do not enforce such stringent conditions, as they are not delineated as mandatory in the *tawarruq* guidelines issued by BNM (2015). These banks solely review the financial background of clients to determine whether they are capable of meeting the installment financing requirements. However, Shariah explicitly prohibits the provision of financing for activities that are forbidden by Islamic law, as stated in Surah al-Maidah, verse 2. AAOIFI (2015) and BNM's resolution (2010) also emphasize that financing should be provided for legitimate purposes. Consequently, bank A is commendable for taking proactive measures to safeguard against potential non-compliance with Shariah principles in financing activities.

On the issue of *wa'ad*, the study found that banks A, B, and C did not include the *wa'ad* element in the contract. Although the inclusion of the *wa'ad* element is permitted in the *tawarruq* contract guidelines by BNM (2015), the banks have chosen not to include the concept of *wa'ad* in the contract due to the potential Shariah issues associated with including the *wa'ad* element in the *murabahah li al-amir bi al-shira'* contract. The findings of this study align with the decisions made by AAOIFI (2015) and Majma' al-Fiqh al-Islami (IIFA 1998), which prohibit the inclusion of *wa'ad mulzim* (binding promise) in a sale without possession by the seller. Furthermore, the inclusion of a binding promise in the *murabahah li al-amir bi al-shira'* contract contradicts the hadith of the Prophet (PBUH) that states, "A sale is invalid unless the purchased goods are in the possession of the seller" (al-Bukhari, 1422H). This is because a sale cannot take place if the buyer does not know the condition of the asset and if the seller does not yet own it. Including a promise in the contract denies one of the purposes of a sale, known as mutual consent. In the event of any issues with the asset, the buyer bears the burden as they have promised to make the purchase (al-Misri 1409H).

Moreover, the inclusion of a binding promise in the *murabahah li al-amir bi al-shira'* contract also contradicts the hadith that states, "Both parties have the right to choose (*al-kehiyar*), whether to proceed with the purchase or

cancel it, as long as they have not separated from the negotiation table (*majlis of aqd*)" (al-Bukhari 1422H). One of the purposes of granting this right to the parties is to ensure their satisfaction with the decision to purchase after examining the desired items, the financial situation, and the terms of the agreement. This purpose is compromised when a binding promise is included in the *murabahah li al-amir bi al-shira'* contract, as buyers acquire assets that are not yet owned by the seller and may carry various risks to the assets (al-Rubi, 1411H).

On the issue of commodity assets, the study found that the surveyed banks utilized local commodity mediums as the underlying assets in the implementation of the *tawarruq munazzam* contract. Previously, these banks used international commodity mediums as their underlying assets. However, in 2009, Bursa Malaysia, in collaboration with BNM, introduced Bursa Malaysia Suq al-Sila' (BSAS), an exchange-traded platform specifically designed to facilitate *tawarruq* transactions. This platform is overseen by internal Shariah advisors and the SAC of BNM (Mohamad & Ab Rahman, 2014). This initiative was undertaken in response to criticisms from Islamic scholars, both local and international, regarding the use of international commodity mediums. According to Ali (2018) and al-Quradaghi (2011), a *tawarruq* transaction in the international commodity market involving aluminum, for example, is flawed and involves commodities that have been stored for more than ten years, rendering them unsellable in the market. Additionally, the standard operating procedure (SOP) at LME discourages the delivery of assets to customers through *tawarruq* contracts. The involvement of brokers in the LME is also associated with uncertainties in avoiding *bay' inah* transactions or transactions involving the same broker (Dusuki, 2010).

According to Abu Ghuddah (2008), there is no guarantee that multiple buyers will sell the same commodity in the LME market. As a result, disclosing this information carries potential Shariah risk when using the LME as the underlying asset. Despite the higher fees charged by BSAS compared to the international commodity platform, and the fact that they are not mandated by BNM's *tawarruq* guidelines, all the banks studied have taken proactive measures to safeguard Shariah compliance in *tawarruq* transactions.

Regarding *wakalah*, all the banks studied still include the *wakalah* element in the *tawarruq* contract, where the client acts on behalf of the bank to sell the assets purchased from the bank to a third party. The inclusion of the *wakalah* element serves several purposes, including adhering to the *tawarruq* contract guidelines issued by BNM (2015), facilitating asset sales as banks are experts in the commodity platform, and saving time by avoiding the risk of depreciation in underlying assets (Ahmad et al., 2017). However, the inclusion of the *wakalah* element in the *tawarruq* contract has caused it to be distinguished as different from the original concept. This discrepancy has led to different legal interpretations of *tawarruq munazzam* (Mohamad & Ab Rahman, 2014). Notably, fatwa institutions such as Majma' Fiqh al-Islami (IIFA, 2009) and AAOIFI (2015) prohibit the inclusion of the *wakalah* element, as it was not originally required but added for the purpose of contract facilitation, risk reduction, and guaranteed profit. These institutions argue that the objective of *wakalah* is a ploy to earn more than the initial capital, resembling the concept of usury (Umar, 2015). The study found no changes made by the banks studied regarding the issue of *wakalah*.

Regarding *ta'wid* and *gharamah* fines, bank A does not impose any fines of either kind, as they are considered against Shariah principles. Banks D and E only impose *ta'wid* fines, as allowed by BNM, but do not impose *gharamah* fines as they go against Shariah. Banks B and C also impose *ta'wid* fines, but there is a slight difference compared to the practices of banks D and E. Banks B and C will contact the customer first to assess the situation and determine their ability to pay in the event of default. Investigating debtors, whether they are facing difficulty (*mu'sir*) or are capable (*musir*), is in accordance with Shariah principles. If a customer has the ability to pay but deliberately misses an installment payment, they will be required to pay *ta'wid*. However, if the customer is in a difficult situation, the bank will discuss with them to determine a suitable solution or timeframe. This concept aligns with Shariah because it is a consensus (*ijma'*) to allow debtors in difficult circumstances an extended period of time to repay their debts (al-Nawawi, 1392H).

From a Shariah perspective, imposing *ta'wid* is required and can be considered as income for the bank. This view is supported by scholars such as Al-Zarqa (1985), Al-Darir (1985), Al-Zuhayli (1998), Uthmani (2003), Al-Ba'li (1996), Al-Zaftawi (1997), and the majority of Shariah Committees in Islamic banks. They believe it is

permissible to charge late fees to customers and consider it as income for the bank (Norazlina and Ridzwan, 2019; Asni et al., 2022).

As for the practice of imposing *gharamah* fines by banks on customers who pay installments late, the proceeds from such fines are not kept by the bank but are instead directed to charities according to the Shariah perspective. Al-Qurradaghi (2008) states that the majority of scholars, both past and present, prohibit the imposition of such fees even if they are donated to charities. This is because if the conditions for imposing the fine are considered usury, then the conditions are invalid regardless of whether the proceeds go to charities or not. This position is also in line with the opinions presented by Majma' Fiqh al-Islami (IIFA 2000) and AAOIFI (2015). Therefore, Bank A's approach of being cautious in imposing fines is commendable. Banks D and E can emulate the practices of Banks B and C in considering the debtor's situation, whether easy or difficult, as this aligns more closely with the objectives (*maqasid*) of Shariah when imposing fines.

In the matter of refinancing, banks C, D, and E offer *tawarruq munazzam* contracts for house financing products. These three banks have approved the refinancing process of home financing by signing a new contract that includes a clause requiring the settlement of the old debt. The actions taken by these banks are in accordance with the *tawarruq* guidelines approved by BNM. On the other hand, banks A and B use contracts other than *tawarruq munazzam* for their house financing products and do not allow refinancing. Based on the findings, banks A and B have taken a proactive approach to ensure compliance with Shariah principles by refusing to refinance. Meanwhile, banks C, D, and E have been involved in the issue of *qalb al-dayn* by requiring new debt to settle an old debt. This is in line with the ruling of Majma' Fiqh al-Islami (IIFA, 2006) which prohibits *qalb al-dayn* as it involves the sale of goods between the debtor and the creditor, resulting in the creation of new debt to amortize the original debt. This is also consistent with the study conducted by al-Muni' (2011), which states that *qalb al-dayn* should only be available to individuals who are capable of paying their debts (*musir*) because it involves obtaining cash without requiring the debtor to pay off their original debt. According to Abu Ghuddah (Mish'al, 2014), *qalb al-dayn* is permissible under certain conditions that are unrelated to the original debt and the purpose of the new debt is not to settle the original debt.

Regarding the issue of *gharar*, all five banks have addressed this issue by explaining the nature, quantity, and price of the asset in the offer to purchase (OTP) agreement. Previously, customers were only informed about these details after the bank sold the asset to a third party. This is in accordance with BNM's (2015) *tawarruq* guidelines, which require the specification of the commodity being traded. This is also consistent with the study conducted by Buang (2000), which states that the seller must clearly state the nature, condition, price, and quantity of the asset before agreeing to a sale offer.

In terms of differentiating between debtors, it was found that only banks B and C investigate whether the debtors are in a difficult (*mu'sir*) or capable (*musir*) situation. This is because according to the Shariah perspective, it is agreed upon (*ijma'*) to provide a grace period to debtors who are facing difficulties or are unable to pay their debts (al-Nawawi 1392H). Therefore, it is recommended that banks D and E follow the example set by banks B and C in this matter.

This study has a positive impact as it sheds light on the improvements made in the practice of *tawarruq* in Islamic banking in Malaysia. It also enhances public confidence in Islamic banking in Malaysia, as continuous efforts are made to improve the contracts offered, particularly those involving *tawarruq*.

Table 4. Improvements in Tawarruq Munazzam product.

No	Improvements in tawarruq munazzam product	Bank Studied				
		A	B	C	D	E
1	Conversion house financing products based on <i>tawarruq munazzam</i> contract to other contracts.	✓	✓			
2	<i>Tawarruq munazzam</i> products are only offered to customers who are in need.	✓				
3	Not use <i>wa'ad</i> element in <i>tawarruq munazzam</i> contract.	✓	✓	✓		
4	Use BSAS as a medium to obtain commodity assets.	✓	✓	✓	✓	✓
5	Not use the <i>wakalah</i> element in the <i>tawarruq munazzam</i> contract.					
6	Not imposing <i>ta'wid</i> and <i>gharamah</i> fines.	✓				
7	Not allow the refinancing process in <i>tawarruq munazzam</i> financing	✓				

8	Avoid <i>gharar</i> issue in <i>tawarruq munazzam</i> contract financing.	✓	✓	✓	✓	✓
9	Distinguish the debtors' situation.		✓	✓		

CONCLUSION

This paper aims to examine the measures taken by selected banks in Malaysia to enhance the implementation of *tawarruq munazzam* contracts. *Tawarruq munazzam* was chosen as a case study due to its prevalence as the most popular financial instrument among Islamic banks in Malaysia. The research findings revealed nine issues related to the *tawarruq munazzam* contract. Furthermore, the study highlighted the lack of uniformity among the five surveyed banks in terms of their efforts to improve the practice of *tawarruq munazzam* contracts. Additionally, one unresolved issue identified by the study pertained to the inclusion of *wakalah* elements. Notably, the study found that one of the banks exhibited the highest level of improvement in the practice of *tawarruq munazzam*, addressing eight out of the nine issues raised.

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