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Article

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Experts' views on *hiyal* in Malaysian Islamic banks: the case of *tawarruq*-based deposit products

Experts' views
on *hiyal*

289

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Abstract

Purpose – There are two purposes to this study: first, to identify the status of *hiyal* (legal devices) in the offering of deposit products based on the *tawarruq* contract in the Malaysian Islamic banking industry and second, to identify the reasons for the widespread offering of *tawarruq*-based deposit products by Malaysian Islamic banks (IBs).

Design/methodology/approach – The study uses the qualitative method that involved interviews with Malaysian Shari'ah experts and Islamic banking operations experts.

Findings – The findings show that Malaysian IBs resolved to use the *tawarruq munazzam* contract in deposit products due to several constraints in the existing banking system and in view of customer preferences.

Research limitations/implications – This study solely focuses on *tawarruq*-based deposit products due to its extensive application in the Malaysian Islamic banking industry.

Practical implications – The implication of the study is that more stringent procedures are required in the offering of *tawarruq*-based deposit products as they are extensively utilised and have sparked controversy among Shari'ah scholars. Moreover, to retain Malaysia's Islamic banking reputation and trustworthiness, new and less controversial contracts must be developed.

Originality/value – This paper discusses the extensive usage of *hiyal*-based contracts such as *tawarruq* in Islamic banking institutions' deposit products, with justifications from Malaysian Islamic banking experts. The widespread use of the *tawarruq munazzam* contract in deposit-based product offerings is based on a reasonable view considering the constraints that Malaysian Islamic banking is currently facing, with strict operation procedures by Bank Negara Malaysia to ensure real operations and to avoid fictitious elements. This paper reveals the use of *tawarruq munazzam* in deposit products which allows the Islamic banking industry to operate effectively under Malaysia's dominant conventional banking system.

Keywords *Hiyal, Makhārij, Maṣlaḥah, Salam contract, Tawarruq munazzam*

Paper type Research paper

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Introduction

The term *hiyal* has two connotations: one positive and one negative. In its positive connotation, *hiyal* refers to wisdom in finding a solution to achieve a specific goal that is not contrary to the Shari'ah (Islamic law). These are known as *hiyal mashru'ah* (Ibn Nujaym, 1983). The negative connotation of *hiyal* refers to the use of a practice that is allowed in Shari'ah, but as a subterfuge for achieving an illegal purpose. This is referred to as *hiyal ghayr mashru'ah* (Ibn Qudamah, 1968). Shari'ah scholars have differing views on the acceptance of Shari'ah contracts that contain *hiyal* (legal devices). Hanafi and Shafi'i scholars are more open to accepting them, unlike Maliki and Hanbali scholars (KMAIA, 1989; Khir *et al.*, 2010).

Hiyal-based contracts are utilised in the structuring of Islamic banking products. For instance, the *tawarruq* contract, which consists of two sale and purchase contracts, is executed to obtain liquidity. Shari'ah scholars agreed on the fact that the *tawarruq* contract features the *hiyal* concept since the transaction is not aimed at the underlying asset but, rather, at obtaining cash from the sale and purchase of the asset (Abozaid, 2016).

Opinions about *tawarruq munazzam* (organised *tawarruq*) differ amongst Shari'ah and Islamic banking operations experts. Some consider it forbidden, while others allow it with restrictions. Despite that, the use of the *tawarruq* contract is ubiquitous in Islamic banking operations. Accordingly, this study aims at

- (1) Examining the status of *hiyal* in the offering of deposit products based on the *tawarruq* contract in the Malaysian Islamic banking industry;
- (2) Identifying the reasons for the widespread offering of *tawarruq*-based deposit products by Malaysian Islamic banks (IBs).

To achieve the aims of the study, interviews were conducted with experts involved in Malaysian Islamic banking operations to find out the real contextual use of *hiyal*-based contracts, with an emphasis on *tawarruq*-based deposit products.

The paper is organised into five sections. Following the introduction, the second section provides a literature review on controversies about the *tawarruq* contract and its usage in Malaysian Islamic banking operations. The research methodology is presented in the third section. The next section highlights the research findings and proceeds to the research discussion in the fifth section. Lastly, the sixth section draws the research conclusion.

Literature review

Controversies about the tawarruq contract

The classical *tawarruq* arrangement consists of two unrelated contracts. A person in need of liquidity purchases a commodity on credit and then looks for someone else to buy it from him on spot. He ends up with cash and a debt that is normally larger than the cash amount. The *tawarruq* contract was recognised by the majority of classical Shari'ah scholars as permissible on the basis of the general permissibility of sale and purchase transactions except for what has been excluded by specific evidence (KMAIA, 1989). The majority did not consider the goal of the seeker of liquidity to affect the legality of either of the constituent transactions (KMAIA, 1989; Ahmad *et al.*, 2017). On the other hand, Ibn al-Qayyim and Ibn Taymiyyah did not allow the *tawarruq* contract since they considered it to be a form of detrimental transaction and a sin committed vis-à-vis Allah (SWT) (KMAIA, 1989; Ahmad *et al.*, 2017).

The form of *tawarruq* used by IBs today is called *tawarruq munazzam* (organised *tawarruq*) since the IB acts as the agent of the original buyer in seeking a buyer for the second sale

transaction and due to other elements of pre-arrangement (Hasan, 2011). As a consequence, contemporary Shari'ah authorities differ over the permissibility of *tawarruq munazzam*.

On the level of organisations, the International Islamic Fiqh Academy of the Organization of Islamic Cooperation (IIFA-OIC) in its resolution no. 179 (5/9) confirmed that two types of *tawarruq* (organised and reverse) are prohibited due to potential fictitious elements that could occur in the transaction (IIFA, 2009; GFR, 2016). The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), on its part, in its Shari'ah Standard No. 30 on Monetization (*Tawarruq*) allows restricted use of *tawarruq munazzam* in Islamic financial institutions – that is, only when faced with the risk of liquidity shortages that might interrupt operations and result in customer losses (AAOIFI, 2017). On the other hand, Bank Negara Malaysia (BNM) in its *tawarruq* document policy permits the use of *tawarruq* contracts in Malaysian Islamic banking operations without imposing usage restrictions on deposit and financing products (BNM, 2018).

As for individual contemporary Shari'ah experts, they too vary in their acceptance of *tawarruq munazzam* in Islamic banking operations (Mohamad and Ab Rahman, 2014). Būṭī (2009) Ibn Bāz (2001) expressed positive acceptance of the usage of *tawarruq munazzam* in Islamic banking operations by emphasising the adherence of the *tawarruq* contract to Shari'ah-compliant selling and purchasing principles. In addition, Muhammad and Bakar (2021) in their study suggested that the use of the *tawarruq* contract be expanded due to its great potential in Islamic banking operations.

However, some Shari'ah scholars oppose the usage of *tawarruq munazzam* in Islamic banking products. According to Uthmānī (2009), Zuhaily (2009) and Bouheraoua (2009), *tawarruq munazzam* contracts pose significant Shari'ah risks in that the buyers have no productive economic interest in the contract's object of sale. The usage of *tawarruq munazzam* in Islamic banking products is seen as a form of *ribā* (interest-based transaction) (Fa-Yusuf and Ndiaye, 2017) and is thus perceived as a reason for customers to doubt the credibility of the Islamic banking industry (Globe Newswire, 2014). Similarly, the claim that the *tawarruq* contract does not stimulate the economy since it is not intended for commodity transactions has become one of the arguments for forbidding its use in Islamic banking products (Siddiqi, 2007; Umar, 2016). Furthermore, according to Fa-Yusuf and Ndiaye (2017), the utilisation of *tawarruq munazzam* in deposit products impedes the widespread adoption of true risk-sharing products such as *muḍārabah* and *musharakah*.

Use of the tawarruq contract in Malaysian Islamic banking operations

Tawarruq contracts are widely used in the offering of Malaysian Islamic banking financing and deposit products, as shown in Table 1. According to a BNM (2021), 60% of customer deposits in IBs are channeled into *tawarruq*-based fixed deposit products. According to these statistics, these deposit products are well received by customers.

It is the flexibility of *tawarruq* contracts in delivering diverse Islamic banking products that is seen as a “magic lamp” to the Islamic banking industry, enabling its widespread use in both deposit and financing products (Ahmad *et al.*, 2017). According to Khir *et al.* (2010), *tawarruq* contracts fall within the scope of flexibility in Islamic finance, but a transition should be sought to less controversial contracts in the future.

Methodology

Research design

This is a qualitative study. To achieve the objectives of the study, researchers conducted in-depth and semi-structured interviews with relevant informants to explore their perspectives on a particular situation. This method is very useful when detailed

Table 1.
Tawarruq-based
deposit products in
Malaysian
Islamic banks

Bank	Current account and savings account (CASA)		Term deposit <i>Tawarruq</i>
	<i>Qard</i>	<i>Tawarruq</i>	
Affin Islamic Bank Berhad	✓	✓	✓
Al-Rajhi Bank	✓	✓	✓
Alliance Islamic Bank Berhad	✓	✓	✓
AmBank Islamic Berhad		✓	✓
Bank Islam Malaysia Berhad	✓		✓
Bank Muamalat Malaysia Berhad	✓	✓	✓
CIMB Islamic Bank Berhad		✓	✓
Hong Leong Islamic Bank		✓	✓
HSBC Amanah Malaysia Berhad	✓		✓
Kuwait Finance House (M) Berhad	✓		✓
Maybank Islamic Berhad	✓	✓	✓
MBSB Bank		✓	✓
OCBC Al-Amin	✓	✓	✓
Public Islamic Bank Berhad	✓		✓
RHB Islamic Bank		✓	✓
Standard Chartered Saadiq	✓	✓	✓

Source(s): Affin Islamic (2022), Al-Rajhi (2022), AIBB (2021), Ambank Islamic (2022), BIMB (2022), BMMB (2022), CIMB Islamic (2022), HLIB (2022), Amanah (2022), KFH (2018), Maybank (2021), MBSB (2022), Al-Amin (2022), PIBB (2022), RHB (2021), Standard Chartered (2022)

information is needed regarding the context of a problem in an area (Rowley, 2012). In this study, the experts interviewed were those with experience in Islamic banking operations in Malaysia as well as Shari'ah experts.

Informants' background

In this study, nine Islamic banking experts were interviewed, including members of the Shariah Advisory Council (SAC) of BNM, Shariah Committee (SC) members of IBs and IB executives, as detailed in Table 2. The participants of this study were selected on the basis of their direct involvement in Islamic banking operations, their experience and their familiarity with the requirements of Malaysian IBs. Interview data can describe the context of the *hilah* contract application in Malaysia. Thus, the conclusions made are not only based on the theory of *hiyal* (pl. of *hilah*) but also rely on current banking practices in Malaysia.

Research and analysis process

To achieve the research objectives, semi-structured questions were developed to help and encourage the informants to describe problems based on their views and experiences. To ensure the trustworthiness of the interview questions, they went through several processes as proposed by Bogdan and Biklen (2007), including validation of interview protocol by field experts, preliminary study and validation of interview data by research participants.

All informants agreed to be interviewed face-to-face at the place and time agreed upon. The interview process of all informants took about 30 min to an hour with voice recording. The interview process began with a brief description of the study and its purpose.

Table 2.
Background of
informants

Code	Position in organisation	Category
P1	Member of the Shariah Advisory Council	BNM
P2	Shariah Risk Management Executive	Islamic Full-fledged Bank
P3	Senior Manager Treasury Operation	
P4	Shariah Review Executive	Islamic Subsidiary
P5	Member of the Shariah Committee	
P6	Member of the Shariah Committee	Islamic Window
P7	Shariah Advisory and Research Executive	
P8	President of Islamic Banking	
P9	Vice President of Islamic Banking	

Source(s): Authors' own

The interview data were transcribed by the researchers and validated by the research participants. The data were then analysed and summarised to identify similar patterns and themes in informants' answers using thematic analysis as suggested by [Braun and Clarke \(2006\)](#). The process included becoming familiar with the data, generating initial codes, searching for themes, reviewing themes, defining and naming themes and producing the reports. Thus, this study meets the criteria of credibility and integrity. The study found some key themes of the study results.

Findings

All the informants agreed that the *tawarruq* contract relates to the *hiyal* concept and is important in the offering of Malaysian Islamic banking deposit products. The study concluded three important causes for the *tawarruq* contract usage in Malaysian Islamic banking deposit products, as discussed below.

Makhārij

When it comes to the use of the *tawarruq* contract, Islamic banking experts prefer the term *makhārij* (way out of a constraint) over *hiyal* since it is more suitable as a way out for Malaysian deposit products. Informants P1, P2 and P6 said:

P1: For me, *tawarruq* is equivalent to *makhārij*.

P2: So, for me when we talk about *hīlah*, we are talking about *makhārij*. The permissible *hīlah* is equivalent to *makhārij*.

P6: Because [*hiyal*] is *mujmal* [ambiguous term], there is *ḥalāl* [*hiyal*] and there is *ḥarām* [*hiyal*]. As for *makhārij*, the term is lighter.

In addition, the use of the *tawarruq* contract is seen as a form of *makhraj* (way out) to the constraints faced by the Islamic banking industry and it goes beyond classical *fiqh* (Islamic jurisprudence) discussions. This was stated by informant P1:

P1: I prefer to put *hiyal* in a broader context. Because what we read in the *turāth* [heritage] books happened on a personal level. But today, *hiyal* is already institutionalised. There is no discussion in *fiqh* books.

Additionally, in describing the use of *tawarruq* contracts in Islamic banking, informant P5 was of the opinion that there should be no problem with the contract being applied in Islamic banking operations as it was a contract that complied with Shari'ah criteria. The statement by informant P5 is as follows:

P5: My opinion, if it [*tawarruq* operation] is not against Shari'ah, then it can be used.

In Islamic banking operations, the term *hiyal*, which carries a negative connotation is avoided. Islamic banking institutions discuss the *tawarruq* contract that features the *hiyal* concept in the form of solutions to Islamic banking product offerings and operations. According to informants P2 and P4:

P2: [*Tawarruq*] is more a solution to a product.

P4: We are not discussing the thing [contract] *hilah* or not. It's more of a solution.

Meanwhile, the use of *makhraj* was described by informant P8 as a solution to Islamic banking product offerings by stating that *tawarruq*-based deposit products are preferred by customers over *qard* (benevolent loan) contract-based deposit products. Informant P8 said the following:

P8: As a comparison, our deposit portfolio is about RM4 billion, out of that, *qard* is RM30 million only. So, what does that tell you when it comes to *qard*?

Furthermore, the *hiyal* parameters outlined by some researchers do not serve as a guide to Islamic banking operations. IBs instead attach more importance to the products offered in compliance with BNM's *tawarruq* policy document. Informant P4 confirmed that the bank practices *tawarruq* as approved by its Shari'ah committee.

P4: We cannot relate whether we practice *hiyal* [or not]. . . at the bank level, whatever the Shari'ah committee allows, that's what we operate with now... Since it [*tawarruq* contract] is approved, if it contains *hiyal*, we consider it to be *hiyal* that is allowed.

According to the informants involved in Islamic banking operations, the *tawarruq* contract is executed in accordance with BNM guidelines, with strict risk management in its operation. For example, in commodity transactions, IBs allow customers to take ownership of the commodity. The informants noted the following:

P2: Customers can [take delivery of the *tawarruq* commodity], he is [then] responsible for the cost of delivery.

P4: He [the customer] has to bear all [related] delivery costs. We can say that the thing [commodity] is there, but you have to go get it.

P8: We put [the option to take the delivery of the commodity] in our requirement. If they [customers] want to take delivery, they need to tell us upfront. We have no problem [about customers] taking delivery of the commodity; the option is there.

In addition, informant P3 stated that Islamic banking has a system that can ensure that commodities involved in the sale and purchase transaction under the *tawarruq* contract are real:

P3: But we lock [the sequence of *tawarruq* in the system]. Because we have this internal system, when the *tawarruq* transaction is completed, it will be updated in the database, which [notifies us] it is already completed.

However, Islamic banking expert informants among the Shari'ah committees of Malaysian IBs suggested that Islamic banking should shift to *hiyal*-free contracts in offering Islamic banking deposit products. Informants P1, P5 and P6 said:

P1: But it [*tawarruq*] is not preferable, and such a contract should have a time limit for us to overcome all the constraints that exist. Then we do our best. We cannot depend on products in the form of *makharij* or *hiyal* like this forever.

P5: But we must see whether it is something that we can use widely, or periodically. . . There should be phases where the industry [Islamic banking] has matured, this contract [*tawarruq*] should not even be required.

P6: Our concept is *al-khuruj min al-ikhtilaf mustahab* [avoidance of areas of juristic disagreement is recommended]. If we can move on to a less controversial [contract] then we move on.

The banking system in Malaysia

The banking system in Malaysia adopts a dual banking mode whereby IBs operate side-by-side with conventional banks (CBs). The Islamic banking system can be categorised into three forms of operations, namely full-fledged Islamic, Islamic subsidiary and Islamic window. In Malaysia's pluralistic society, banking products offered by CBs are gaining more attention among customers. This is due to the longer presence and experience of CBs compared to IBs as well as the availability of competitive products that benefit customers.

In this regard, based on the history of the banking system in Malaysia, the Islamic banking experts interviewed believe that it is difficult for IBs to attract the attention of bank customers who are already familiar with the conventional banking system.

Since IBs have IT systems and operating procedures to execute Shari'ah contracts, they have no restrictions on introducing products based on other contracts as long as they comply with Shari'ah criteria. This corresponds to the statement of informant P3:

P3: The bank does not have a problem to switch to another contract as long as it does not violate Shari'ah.

However, considering that the banking system in Malaysia is dominated by CBs, the *tawarruq* contract has become an Islamic banking option to be widely applied in Islamic banking product offerings. P7 and P8 pointed out:

P7: We are not ready to be there yet [profit-sharing-based deposit]... I mean ideally, we want deposits to be based on *mudharabah*. For depositors as investors, we will share the return. Ideally so, yes, we are aware of that. But to get there, we must start slowly. That's what I mean, my opinion, *hiyal* in today's context is a necessity.

P8: The main issue is that there is always the notion that Islamic banks want to do this [*hilah*]... But that is not the intention. The intention is that we have to look in the context of how we build Islamic banks.

Furthermore, in the interviews conducted, the Islamic banking experts stated that the use of *tawarruq* can boost the development of IBs in Malaysia as well as encourage Malaysian bank customers to choose Islamic banking products over those of CBs. According to informants P2 and P6, the objective is:

P2: To remain competitive for the product, yet the product remains Shari'ah-compliant. . . if the thing [*tawarruq*] is controversial, yes, it is true. . . but at least when doing it this way, it's like preventing the flow of funds to the conventional [system].

P6: First, *tawarruq* is used as an avoidance of *riba*. Second, to move the economy. Third, to be able to avoid the accusation of *riba al-qard* (interest-based loan).

Customer preferences

Customers in Malaysia are still unaware of the use of Shari'ah contracts in Islamic banking products. Banking customers are sceptical of products based on risk-sharing contracts, according to informants P2, P8 and P9. In their statements, they said:

P2: [*Tawarruq* usage enables] the offering of a variety of products, and meets the product requirement of the customer. Because the customer is not very comfortable with products that do not guarantee profit.

P8: When we offered *mudārabah* before, and we offered *qard*, then the Muslims themselves had problems. They are the ones who said that it is not right. It is the failure of the customer to understand the Islamic bank.

P9: ...It's not that the industry does not produce profit-sharing *mudārabah* products, but it does not get a [good] response. So that's why the bank does according to the customer's wishes. Go for sale-based [products].

Besides that, banking customers are most likely to choose deposit products that are able to guarantee their deposits, cash liquidity and profitability simultaneously. As a result, customers choose *tawarruq*-based deposit products that meet those criteria over other deposit products. Informant P1 claimed that:

P1: There are three [indicators] that depositors always want, [first] capital guarantee. ... second, liquidity... third, profit.

This indicates that deposit products based on the *tawarruq* contract are offered in IBs, giving customers the option to deposit their money while earning fixed profits from Shari'ah-compliant products.

Discussion

In Malaysia, Shari'ah experts refer to the usage of the *tawarruq* contract in Islamic banking products as *makhārij*. This is due to the fact that the phrase *makhārij* is more synonymous with the term *ḥiyal mashrū'ah*, as it indicates a positive connotation, rather than the term *ḥiyal*, which has two connotations, positive (*ḥiyal mashrū'ah*) and negative (*ḥiyal ghayr mashrū'ah*). Besides, *makhārij* is employed as a means of circumventing the constraints imposed by the current Islamic banking system.

In Islamic banking operations, banks do not focus on the *ḥiyal* status of a contract. Rather, they concentrate on finding solutions to customers' needs in terms of product offerings and are concerned about customer responses. The solutions proposed must comply with BNM standards and meet the demands of Malaysian customers. Malaysian customers prefer to choose deposit products that are less risky while offering guaranteed deposits, liquidity and profits simultaneously (Muneeza, 2019). Thus, profit-sharing contracts do not meet customer demands since, according to the Islamic Financial Services Act (2013) (IFSA, 2013), they are categorised as investment products that cannot guarantee customer deposits. Meanwhile, the *qard* contract does not fulfill the demands of the customer since no profit can be guaranteed to the customer.

Based on these competitive characteristics, the *tawarruq* contract has become a suitable solution for deposit products in IBs as it strongly matches the preferences of the majority of Malaysian customers. Customers benefit from *tawarruq*-based deposit products in the same way that they benefit from CBs' deposit products. However, the two products operate differently. In CBs' deposit products, the profit yields are dependent on *ribā* transactions. Meanwhile, in IBs, *tawarruq*-based deposit products are structured using genuine Shari'ah-compliant sale and purchase transactions (Ahmad et al., 2020). As a result, the availability of deposit products based on the *tawarruq* contract provides Malaysian customers the option of choosing Islamic banking deposit products over conventional banking deposit products (Chowdhury et al., 2020).

Clearly, Malaysian IBs employ *makhārij* in deposit product operations to fulfill the demands of Malaysian customers as well as react to market constraints and the complicated modern financial environment (Hamour et al., 2019). The use of *tawarruq* contracts by

Malaysian IBs is a form of *makhārij* that meets *hiyal* parameters (Khair *et al.*, 2010; Syed and Omar, 2017) as well as complying with the BNM *tawarruq* policy document (BNM, 2018). Furthermore, the *tawarruq* operation is governed by proper Shari'ah risk-control mechanisms. The way that *tawarruq* is strictly practiced by IBs may help to reduce the prohibited elements that may have otherwise arisen in the operations (Shaharuddin, 2019; Chowdhury *et al.*, 2020).

However, the widespread use of *tawarruq* contracts in Islamic banking products needs to be reconsidered. This is so because these contracts are controversial and not accepted by Shari'ah scholars globally (Alkhan and Hassan, 2019). AAOIFI Shari'ah Standard no. 30 on Monetization (*Tawarruq*), item no. 5/1, states that a *tawarruq* contract is only to be utilised in situations of necessity (*darūrah*) and is restricted to financing product offerings. Furthermore, some Shari'ah experts are opposed to the *tawarruq* contract structure as it is not aimed at the commodity (Sharaiyra and Haswa, 2019; Alkhan and Hassan, 2019) and consider it a form of fraud (Hamour *et al.*, 2019) and a trick to circumvent the prohibition of *ribā* (Sharaiyra and Haswa, 2019; Smolo and Musa, 2020). Moreover, Islamic banking operations are exposed to the risk of Shari'ah non-compliance due to *tawarruq* contracts deviating from the original objectives of commodity sale and purchase contracts (Alkhamees, 2017; Bakar and Mansoor, 2020). In the long term, this may harm the reputation of the Islamic banking industry (Kahf and Habbani, 2016; Ahmad *et al.*, 2017).

Besides, the extensive usage of *tawarruq* contracts has caused the Islamic banking industry to become over-reliant on debt-based contracts (Alkhan and Hassan, 2019) and thus violating the sustainability of Islamic finance objectives (Ahmad *et al.*, 2020). It is argued that the scenario has resulted in Islamic banking operations and functions being no different from conventional banking operations (Maali *et al.*, 2020), with the exception of the adoption of Islamic terminologies to hide *ribā* transactions and evade Shari'ah restrictions (Ahmad *et al.*, 2017).

Additionally, it is said that the excessive usage of *tawarruq* contracts contributes to debt proliferation and the occurrence of economic crises (Bouslama and Lahrichi, 2017). As a result, the *tawarruq* contract is seen as an inefficient mode of accumulating wealth since money does not flow to the most productive projects (Alkhamees, 2017) while at the same time impeding the growth of contracts based on profit and loss (Hidayah *et al.*, 2019).

Negative allegations concerning the Shari'ah compliance status of *tawarruq* contracts in Islamic banking operations, as well as criticisms about the impact of excessive use of *tawarruq* on Islamic banking reputation have stimulated Shari'ah scholars to advise IBs to shift away from *tawarruq*-based products (Asni and Sulong, 2018; Smolo and Musa, 2020; Ahmad *et al.*, 2020). This is crucial considering the *tawarruq* contract is not internationally recognised, posing a long-term threat to the global aspirations for Malaysian Islamic banking (Ali and Hassan, 2020). This statement aligns with the views of the Shari'ah experts interviewed in this study.

Furthermore, the parameters developed by Khair *et al.* (2010) related to *hiyal*-based contracts categorise *tawarruq* as a *rukhsah* (facilitation) contract since it incorporates the concept of *hiyal*. This contract is viewed as a necessity for Islamic banking operations seeking to compete in Malaysia's banking landscape. However, IBs should not utilise the *tawarruq* contract in their product offerings permanently; instead, they should work to overcome the constraints (Ahmad *et al.*, 2017) and shift to more Shari'ah and economy-friendly contracts in the future (Khair *et al.*, 2010).

Due to the obvious current banking challenges, some Shari'ah experts suggested that BNM along with IBs establish more strict and systematic operational parameters and *tawarruq* contract procedures (Mahyudin and Seman, 2018; Alkhan and Hassan, 2019). Moreover, IBs should reduce their reliance on *tawarruq* contracts for their product offerings (Ali and Hassan, 2020). This is critical in order to ensure that Islamic banking operations

comply with Shari'ah principles, as this contract is subject to major Shari'ah risks and has been widely criticised by Shari'ah experts (Alkhamees, 2017; Fa-Yusuf and Ndiaye, 2017).

Salam contract as an alternative

Meanwhile, there have been recommendations for the *salam* contract to replace the *tawarruq* contract in Islamic banking product offerings (Mahaini, 2016; Dchieche and Aboulaich, 2016; Putri *et al.*, 2019). The *salam* contract is a sale and purchase contract whereby the asset price is paid in advance for future delivery of a defined asset. Farmers utilise the *salam* contract to get financing for their agricultural activities (Mahadik, 2013).

The *salam* contract provides several advantages over the *tawarruq* contract. To begin with, usage of the *salam* contract is more in accordance with economically-friendly transactions (Mahadik, 2013) as it is utilised to finance agricultural and manufacturing operations (Saleem *et al.*, 2014; Obaidullah, 2015; Putri *et al.*, 2019; Ahmad *et al.*, 2020). Furthermore, *salam* contracts benefit both sellers and buyers since the former require advanced payments to finance their production operations while the latter benefit from the *salam* commodity price which is lower than the spot selling price.

The use of the *salam* contract in structuring deposit products is known as reverse *salam*. It involves the bank as the seller (the bank represents the party offering the commodity in the future) and the customer as the buyer (the customer provides the cash deposit). It is different from the *salam* contract used by banks in financing products.

Reverse *salam* enables IBs to collect customer deposits at the moment of the *salam* contract inception ($T+0$). By the time the deposit *salam* contract reaches maturity ($T+90$), the IB has to provide depositors with a specific quantity, quality and value of commodities. IBs are free to utilise accumulated deposits between the starting date of the contract and the maturity date. To reduce market risks, Mahaini (2016) recommended that IBs adopt approved hedging tools to lock in the commodity purchase price on the contract maturity date. When the *salam* contract reaches maturity, and the depositor owns the commodity, he may delegate the bank to sell it on the market on his behalf and for the bank to credit the amount to the depositor's account. This amount is referred to as the redemption amount (Saleem *et al.*, 2014).

In Malaysia, Bursa Suq Al-Sila's platform offers deposits based on the *salam* contract. The structure provided by Bursa Malaysia Islamic Services Sdn Bhd (BMIS) has been approved by Bursa Suq Al-Sila's Shariah committee as a Shari'ah-compliant product (Bursa Malaysia, 2019). In the meantime, Koperasi Co-opbank Pertama Malaysia Berhad, a cooperative organisation in Malaysia, is one of the Malaysian Islamic financial institutions that uses the *salam* contract in deposit products (CBP, 2021).

There are, however, constraints in applying the *salam* contract in Islamic banking deposit products. This is so because Islamic banking operations in Malaysia still do not have the best model and practice of the *salam* contract. Meanwhile, the *salam* contract contains risks that need to be managed by IBs, including market risks on fluctuating commodity prices (Saleem *et al.*, 2014) and issues related to hedging against commodity asset prices before contract maturity (Mahaini, 2016). Moreover, due to the reliance of IBs on the *tawarruq* contract, which is easier to use in deposit products since they do not entail market risks, efforts to employ the *salam* contract in deposit products have drawn less attention among Malaysian IBs. The *salam* contract, on the other hand, is more suited to be offered in financing products related to agricultural and industrial operations.

Conclusion

Based on prior discussions, the *tawarruq munazzam* contract that incorporates the concept of *hiyal* has become a subject of controversy among Shari'ah experts, with some allowing it to be used in Islamic banking products in limited situations, while others allowing it with

procedures and operations that need to be tightened and still others advising IBs to shift away from *tawarruq* to other contracts to ensure the Islamic banking sustainability.

The *salam* contract is one of the recommended contracts that is less controversial. In terms of Malaysian Islamic banking product offerings, the *salam* contract is more feasible as a solution for financing products involving agricultural and manufacturing activities. This contract, on the other hand, is less viable in deposit products since no sustainable application model has yet been proposed, and its usage exposes banks to market risks.

However, IBs must consider the long-term implications of excessive *tawarruq* utilisation in product offerings on the Islamic economy and IBs' reputation. IBs must seek to balance their product offerings with the *salam* contract and other Shari'ah-compliant and economy-friendly contracts, and they must develop a clear roadmap for shifting away from *tawarruq* contracts. Simultaneously, the regulator and IBs must ramp up efforts to raise customer awareness of Shari'ah contracts that underlie various products as well as encourage them to choose Shari'ah-compliant and economically sustainable products.

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