Understanding 'Al-Hiyal': The Clever and Controversial Tool of Islamic Banking Products Creation

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ABSTRACT

This article investigates al-hiyal (legal stratagems) as the device through which Islamic banks meet modern financing needs while observing the Shariah prohibition of interest (riba). Grounded in classical jurisprudence, including al-Khassaf's definition and the Prophet Muhammad's guidance to Bilal on exchanging dates, it separates permissible al-hiyal (al-hiyal al-masyru'ah), which reach lawful ends by lawful means, from forbidden al-hiyal (al-hiyal al-mamnu'ah), which dress an unlawful substance in a lawful contractual form. It then dissects two flagship products, Tawarruq (commodity Murabahah) and Bay' Bithaman Ajil (BBA) with Bay' al-'Inah, showing how each rebuilds the cash flows of a conventional loan through a chain of sales. The article compares the positions of the four Sunni schools and of institutions, setting the pragmatic stance of Bank Negara Malaysia's Shariah Advisory Council against the stricter rulings of the OIC Fiqh Academy and Middle Eastern scholars, and reviews market data showing that fixed-return contracts far outweigh profit-and-loss sharing. Weighing contractual form against economic substance, it argues that heavy dependence on al-hiyal strains the Maqasid al-Shariah (justice, fairness and social welfare) and risks leaving Islamic finance a relabelled copy of conventional banking. It does not call for abolition. It proposes instead a gradual portfolio shift towards asset-backed and partnership structures, such as Musharakah Mutanaqisah, ijarah, purpose-linked financing and risk-controlled Musharakah and Mudarabah, supported by product-mix disclosure and outcome-based regulation such as Value-Based Intermediation. It concludes that the continuing form-versus-substance debate is a constructive discipline pushing the industry towards more authentic, ethically grounded innovation.

Keywords: al-Hiyal in Islamic finance, Shariah compliance, Tawarruq, Bay' al-'Inah, Maqasid al-Shariah

INTRODUCTION

Islamic finance began in the mid-twentieth century as a small ethical-banking movement and now manages assets worth trillions of dollars across retail banking, capital markets and insurance (takaful), in Muslim-majority countries and Western financial centres alike (Saleem et al., 2023). One question has shadowed this growth from the start: how can institutions offer products that meet the needs of an economy organised around interest while staying true to the Shariah ban on riba (usury or interest)? The answer decides whether Islamic finance is seen as a distinct ethical alternative to conventional banking or as the same system under a different name. (Ibrahim, A.R et.al., 2026)

The main tool used to resolve this tension is al-hiyal, or legal stratagems: contractual arrangements that structure a transaction so that it complies with Islamic law on its face. Al-Khassaf defined it as a legitimate route from the forbidden (haram) to the permissible (halal), and its precedent is often traced to the Prophet Muhammad (PBUH), who, faced with an unequal exchange of dates amounting to riba, advised a two-step sale and repurchase instead (Sokris, F.M et.al, 2024). The lesson still underlies Islamic finance: the form of a transaction matters, and careful restructuring can reach a desired economic result without breaching the letter of the law.

The same ingenuity has produced the industry's most persistent controversy. As al-hiyal-based structures grew more elaborate, they became embedded in mainstream products such as Tawarruq (commodity Murabahah)

for cash financing and Bay' Bithaman Ajil (BBA) with Bay' al-'Inah for home and asset financing (Ahmad, 2020). Murabahah-based contracts, including Tawarruq, far outweigh equity-based modes such as Mudarabah and Musharakah (International Monetary Fund, 2015; Saleem et al., 2023), so critics ask whether these instruments simply reproduce an interest-bearing loan in the vocabulary of Shariah-compliant trade, a back door to interest (International Monetary Fund, 2015; Usmani, 2007, as cited in Saleem et al., 2023). This is the form versus substance debate: a transaction can satisfy every technical requirement of Islamic contract law and still deliver a fixed, predetermined return on money advanced over time.

No single authority settles the matter. The four Sunni schools (Hanafi, Shafi'i, Maliki and Hanbali) differ on whether al-hiyal is permissible, from the relatively pragmatic Hanafi view to the more cautious Maliki and Hanbali positions (Sokris F.M,et.al., 2024). National bodies such as Bank Negara Malaysia's Shariah Advisory Council tend to be permissive so that domestic Islamic banks can compete within dual banking systems (Ismon, N. Y. B. (2012), whereas transnational bodies such as the OIC International Islamic Fiqh Academy, and many Middle Eastern scholars, have restricted or prohibited practices like organised Tawarruq as deceptive stratagems that circumvent the ban on riba (International Islamic Fiqh Academy, 2009).

Understanding al-hiyal therefore requires examining how it works in real banking products, the classical reasoning that both allows and limits it, and whether reliance on it undermines the Maqasid al-Shariah, the higher objectives of justice, fairness and social welfare. The article sets out the jurisprudential basis of al-hiyal, shows how it operates in two widely used products, places the tension within the scholarly and regulatory debate, and then criticises heavy reliance on it, outlining alternatives such as diminishing partnership and asset-based leasing (Abdul Rahman et al., 2020; Subky, 2017).

The Core Puzzle of Islamic Finance

The central question is how a bank can supply financing that works like a loan without charging interest, which Islamic law forbids as riba. Islamic institutions operate inside a global financial system built almost entirely on interest, so scholars and practitioners have needed products that are commercially competitive yet doctrinally defensible: customers should be able to use them as they would a conventional loan, and Shariah scholars should be able to certify them as compliant (Ahmad, 2020; International Monetary Fund, 2015).

The main answer is al-hiyal: deliberately structured contracts that let Islamic banks turn ordinary needs, such as raising cash, buying a home or funding working capital, into chains of permissible sale and trade contracts. Instead of banning interest and leaving demand unmet, al-hiyal recasts conventional financing objectives as transactions built from Murabahah (cost-plus sale), bay' (sale) and other contract types recognised in classical fiqh (Satti, W. M., & Riaz, M. 2025; Sokris, F. M., et.al 2024). Seen this way, al-hiyal is less a loophole devised to defeat the law than a juristic technique developed within it.

The puzzle also has a history. Modern Islamic banking is commonly traced to the Mit Ghamr Savings Bank, founded in Egypt in 1963 around profit-sharing investment by local depositors (MEED, 2008), and the sector has since grown into a multi-trillion-dollar industry (Saleem et al., 2023). Growth pushed Islamic banks to match conventional finance on pricing and liquidity, and al-hiyal-based structures largely eased that pressure, so murabahah-based contracts now clearly outweigh equity-based modes (International Monetary Fund, 2015; Saleem et al., 2023).

The same success is the source of the industry's most lasting controversy. The ingenuity that lets al-hiyal solve the interest problem also permits structures whose economic substance may closely resemble the interest-based products they were meant to avoid, even while their contractual form stays compliant (Hamour et al., 2019). The tension therefore bears on whether Islamic finance is an ethically distinct system or only a relabelled version of conventional banking.

Describing al-hiyal merely as a "workaround" understates its jurisprudential depth and risks reducing a centuries-old legal tradition to a marketing euphemism. It is better read as double-edged: a historically sanctioned means of reaching lawful ends by lawful methods, which can be misused when the drive to compete

with conventional finance outweighs commitment to the Maqasid al-Shariah (Satti, W. M., & Riaz, M. 2025; Sokris, F. M., et.al., 2024).

What Exactly is Al-Hiyal? More Than Just A "Workaround"

The Arabic root of al-hiyal (singular: al-hilah) carries an everyday sense of skill, resourcefulness and the ability to reshape the outward form of an act to reach a particular aim. Classical jurists sharpened this into precise legal content. Al-Khassaf, among the earliest jurists to treat the subject systematically, described al-hiyal as a device for freeing a person from something sinful and forbidden by directing them toward what is permissible instead (al-Khassaf, 1314H, as cited in Sokris F.M.et.al, 2024).

In its original conception, then, al-hiyal was never a means of evasion but a tool of legal craftsmanship that leaves the underlying prohibition intact while offering a lawful route around a practical obstacle. Even so, Shariah does not treat all al-hiyal alike: classical scholars separated them by the intention behind a stratagem and its outcome, as the table below sets out (Sokris F.M.et.al., 2024).

Permissible al-Hiyal (hiyal masyru'ah)	**Forbidden al-Hiyal (hiyal mamnu'ah)**
The "Clever Solution"	**The "Legal Loophole"**
A stratagem used to achieve a permissible (halal) outcome or to avoid something forbidden (haram).	A stratagem used to make a forbidden (haram) act appear permissible on the surface.
Its objective is to find a Shariah-compliant pathway to a legitimate goal.	It uses the form of a lawful contract to achieve an unlawful substance (e.g., circumventing the prohibition of riba).

The line between the two categories is not always obvious from a contract's structure alone; it often turns on the purpose the parties intend. Ibn Taimiyyah captured this when he taught that a stratagem is good or evil according to the goal it serves, placing intention rather than form at the centre of the assessment (Ibn Taimiyyah, 1987, as cited in Sokris F.M.et.al., 2024). This standard is doctrinally sound, but it is also what makes hiyal hard to regulate: intention is subjective and largely unobservable to a regulator or auditor, who can judge only the objective steps of a transaction.

Conventional legal and tax systems face the same difficulty through substance-over-form doctrines and general anti-avoidance rules aimed at transactions that are lawful in structure yet designed to defeat the purpose of the rule behind them (Hamour et al., 2019). The al-hiyal debate is thus a theologically grounded version of a broader dilemma: how any rule-based system tells lawful creativity from rule-defeating manipulation.

The Foundational Precedent: The Case of Bilal and the Dates

The most authoritative illustration of a permissible al-hilah comes directly from the Sunnah. A companion, Bilal, once brought Prophet Muhammad (PBUH) high-quality dates. Asked how he had obtained them, Bilal explained that he had traded two units (sa's) of his own inferior dates for one unit of the superior kind. The Prophet's response was immediate: this was riba, and Bilal was told not to do it again (Sahih al-Bukhari, 2003., Hadith 2312).

The Prophet did not stop at prohibition, however. He set out an alternative process that reached the very same practical result: sell the inferior dates for money first, then use that money to buy the superior dates (Sahih al-Bukhari, 2003., Hadith 2312). This two-step transaction is the paradigmatic al-hilah: a restructuring that removes the impermissible element, the unequal and uncertain exchange of like-for-like goods, while preserving the customer's legitimate goal of upgrading the dates owned.

Modern literature often treats this hadith as an origin story for al-hiyal, and with good reason: it shows that Islamic law does not merely prohibit but offers constructive alternatives. Yet the precedent should not be stretched indefinitely. Bilal's transaction was two straightforward, sequential sales with one identifiable purpose, carried out openly between known parties, whereas modern al-hiyal-based products often involve multiple intermediaries, offshore commodity exchanges and simultaneous transactions with terms fixed in advance. The precedent establishes that process and form matter, but it does not settle how much complexity or predetermination a modern hilah can tolerate before it drifts from al-hilah al-mashru'ah toward al-hilah al-mamnu'ah.

From Classical Precedent to Modern Practice

This principle, that a lawful process can be engineered to reach a lawful outcome, is what modern Islamic banks rely on. Where the Prophetic precedent addressed a single barter, today's banks apply the same logic at institutional scale, in standardised, repeatable contract structures that serve thousands of customers and meet regulatory and accounting requirements. (Sokris F.M.et.al., 2024)

How Al-Hiyal is Used Today: A Look at Real Banking Products

Hiyal is the operational engine behind many products of Islamic banks worldwide. Two illustrate this especially clearly: Tawarruq (commodity Murabahah), used mainly for cash financing, and Bay' Bithaman Ajil (BBA) combined with Bay' al-'Inah, used for major assets such as homes. Side by side, they show both the technical sophistication of al-hiyal-based engineering and the recurring points where critics argue that form has outpaced substance (International Monetary Fund, 2015; Saleem et al., 2023).

These are not marginal products. Tawarruq underpins a substantial share of personal financing and interbank liquidity management, particularly in the GCC states and Malaysia, while BBA-style home financing has long been among the most common retail products in Malaysia's dual banking system (International Monetary Fund, 2015; Saleem et al., 2023). Their scale makes the form-versus-substance debate a matter of systemic importance.

Tawarruq (Commodity Murabahah): Creating Cash from Commodities

Customer Need: To obtain cash liquidity—for personal use or working capital—without resorting to an interest-based loan.

The Tawarruq transaction uses a coordinated sequence of commodity trades as a al-hiyal to convert a deferred-payment sale into immediate cash. The process typically unfolds as follows:

- **The Need for Cash:** A customer approaches the bank seeking financing.
- **Commodity Purchase 1:** Acting as the customer's agent (wakalah), the bank purchases a real, tradeable commodity—such as palm oil or metal—from a broker, often via an organized exchange like Malaysia's Bursa Suq al-Sila' or the London Metal Exchange.
- **Commodity Sale:** The bank immediately sells that same commodity to the customer on a deferred basis at a marked-up price (cost plus an agreed profit margin), payable in installments. At this point, the customer legally owns the commodity but owes the bank the marked-up sum.
- **Commodity Purchase 2:** The customer, now holding a commodity they never actually wanted, immediately sells it to a third party in the open market for cash. This must be a different party from the original seller, in order to avoid constituting a prohibited Bay' al-'Inah (a sale and buy-back with the same original party).

In practice, the entire sequence is often executed within minutes, sometimes through a single electronic platform designed to facilitate organized Tawarruq (Tawarruq Munazzam). Some scholars distinguish this

sharply from "classical" Tawarruq, where a customer independently sources and sells the commodity on their own initiative and timeline. Classical Tawarruq more closely resembles a genuine trade with real commercial risk, whereas organized Tawarruq, pre-arranged, near-instantaneous and often facilitated entirely by the bank, more closely resembles a synthetic mechanism for generating cash, with the commodity a mere legal formality.

Here the form-versus-substance debate is at its clearest. The customer never intends to use, store or profit from the palm oil or metal; the commodity is a legal vehicle rather than an economic asset. The transaction satisfies the classical requirements of a valid sale (transfer of ownership, an identifiable asset and an agreed price), yet its economic effect is indistinguishable from a cash loan repaid with a markup functioning as interest. This gap is why the OIC Fiqh Academy characterizes organized Tawarruq as impermissible, even while national regulators such as Malaysia's Bank Negara sanction it as a tool for liquidity management within a competitive dual-banking system.

Bay' Bithaman Ajil (BBA) and Bay' al-'Inah: Financing Major Purchases

Customer Need: To finance a major asset, such as a house, without relying on a conventional, interest-bearing mortgage.

Bay' Bithaman Ajil (BBA) is a deferred-payment sale contract. In Malaysia, its application to home financing became especially controversial because it frequently incorporated a second al-hiyal, known as Bay' al-'Inah (a sale-and-buyback arrangement), to generate the initial liquidity for the purchase.

The Bay' al-'Inah mechanism operates in two steps:

- **Step 1 (Sale):** The bank sells an asset to the customer on a deferred-payment basis at a higher price (for example, RM100,000 payable over ten years).
- **Step 2 (Buy-Back):** The bank then immediately repurchases that same asset from the customer for a lower cash price (for example, RM80,000).

In effect, to generate the upfront cash needed for the home purchase, the bank and customer execute a Bay' al-'Inah transaction on a separate asset, creating the liquidity that the BBA contract then finances over an extended term. The net economic result is that the customer receives RM80,000 in cash while being contractually obligated to repay RM100,000. Although structured as two legally distinct sales, critics argue that its economic substance is identical to an RM80,000 loan carrying RM20,000 in interest.

The controversy is compounded by a further wrinkle: unlike Tawarruq, which typically involves a genuine third party to break the circularity of ownership, Bay' al-'Inah is transacted directly between the same two parties, the bank and the customer, with no external commodity or intermediary. This is why the Maliki and Hanbali schools regard it as unambiguously impermissible: without a real third-party transfer, the transaction lacks the commercial risk and genuine change of ownership that classical sales embody, leaving what critics describe as two paper transactions wrapped around a single cash-for-more-cash exchange. The Shafi'i school occupies a middle position, permitting the contract in principle while scrutinizing intention, whereas the pragmatic Hanafi stance provided the opening that allowed Malaysian regulators to sanction its use in retail home financing for several decades before reforms began phasing it out in favor of alternatives such as Musharakah Mutanaqisah (diminishing partnership).

Tawarruq, BBA and /Bay' al-'Inah show that the form-versus-substance tension is a recurring structural feature of al-hiyal-based design. In both, a genuine trade or sale contract is scaffolding to reconstruct the cash-flow profile of a conventional loan: principal disbursed today, a larger fixed sum repaid over time. What separates them, and drives much of the divergent scholarly opinion, is the presence or absence of an independent third party and genuine market risk: Tawarruq at least routes the transaction through an external market and a separate buyer, while classical Bay' al-'Inah does not. The debate can therefore be assessed against a concrete criterion: the degree of real economic risk and independent market participation embedded in the stratagem.

The Heart of the Debate: Form Vs. Substance

Having seen how al-hiyal operates in two flagship products, we reach the question they illuminate: is a transaction Shariah-compliant simply because it follows the form of recognised Islamic contracts, even when its economic effect replicates the substance of an interest-bearing product? This is the central fault line in contemporary Islamic finance: whether the industry is judged by its contractual architecture or by its economic outcomes.

The debate draws on centuries of divergence among the classical schools of law (madhahib), inherited and sometimes sharpened by modern regulators shaped by local economic realities and competitive pressures. Regulators in dual banking systems, such as Malaysia's, tend to favour a pragmatic reading that lets Islamic banks compete, whereas scholars and standard-setting bodies outside that pressure may feel freer to insist on the underlying spirit of the law (Laldin & Furqani, 2016, as cited in Sokris, F. M., et.al 2024).

Group	General Stance on al-Hiyal	Primary Rationale (The 'Why')
Hanafi School	More open and pragmatic.	Permits legal stratagems as long as they do not explicitly violate the letter of Shariah law.
Shafi'i School	More conservative.	Scrutinizes al-hiyal carefully to ensure it does not undermine the spirit and ethical goals of Shariah.
Maliki & Hanbali Schools	More conservative and critical.	Emphasize that al-hiyal must not be used to manipulate Islamic law or achieve outcomes that are otherwise prohibited.
Malaysia (Bank Negara's SAC)	Permissive (e.g., allows Tawarruq and Bay' al-'Inah).	Takes a pragmatic approach to enable Islamic banks to compete and provide necessary financial solutions in a dual-banking system.
OIC Fiqh Academy & Middle East Scholars	Largely impermissible (especially for organized Tawarruq).	Contend that these structures are stratagems (al-hilah) designed to secure quick additional cash while carrying an element of riba, thereby circumventing its prohibition (International Islamic Fiqh Academy, 2009).

This fragmentation has real-world consequences. A Tawarruq-based product approved by Malaysia's Shariah Advisory Council may be rejected by a Shariah board in the Gulf, creating friction for cross-border institutions, complicating AAOIFI's standardisation efforts, and sometimes requiring multinational Islamic banks to run different structures in different jurisdictions (International Monetary Fund, 2015).

Critics argue that unchecked expansion of al-hiyal risks undermining the Maqasid al-Shariah, which cover justice, fairness and social welfare, not merely the avoidance of specific prohibited terms. Prioritising letter-of-the-law compliance over these ethical goals risks reducing Islamic finance to a replica of conventional banking distinguished only by Arabic contract labels (Hamour et al., 2019). Many scholars regard this tension as the greatest challenge to the industry's long-term legitimacy.

Beyond Doctrine: The Regulatory and Reputational Stakes

The tension carries direct commercial and reputational consequences. AAOIFI has progressively tightened its standards on organized Tawarruq and similar structures to protect the industry's credibility, while national regulators must weigh credibility against the risk that restrictive standards shrink the range of compliant products and push customers back to conventional financing. Tightening too far protects doctrinal purity at the cost of competitiveness; permitting too much protects market share at the cost of ethical identity.

What emerges is not a simple split between "permissive" and "strict" camps but a spectrum of interpretive positions, each coherent within its own jurisprudential and economic logic. Hanafi-influenced pragmatism in Malaysian practice is not a doctrinal shortcut but a historically grounded tradition that gives greater latitude to contractual form. The OIC Fiqh Academy's restrictive position is not reflexive conservatism but a considered application of Maqasid-based reasoning that treats economic substance as the test of compliance. This plurality is better read as a living legal tradition working out how far commercial pragmatism can extend before it compromises the law's ethical core than as a weakness to be resolved by forced consensus.

Conclusion: The Ongoing Challenge for Islamic Finance

For any serious student or practitioner of Islamic finance, understanding hiyal is indispensable, because it lays bare both the ingenuity of the field and its most profound unresolved tensions. Having traced hiyal from its classical origins, through real banking products, to the divergent positions it has generated, three conclusions emerge.

- **A Necessary Tool.** Hiyal is a practical instrument that has enabled Islamic banks to function, compete and offer viable financing within a global economy built around interest. Without it, the industry would have struggled to provide even basic products such as cash financing, home ownership and working capital.

- **An Enduring Controversy.** The use of al-hiyal embodies Islamic finance's central unresolved debate: adhering to the letter of the law (the form of contracts) versus fulfilling its spirit (the ethical substance and higher objectives, or Maqasid al-Shariah). As Tawarruq and Bay' al-'Inah show, this is embedded in products used by millions of customers worldwide.

- **The Drive for Authenticity.** Far from being merely destructive, this debate is healthy and constructive. It is an internal accountability mechanism, pushing the industry to resist becoming a "mere replication of conventional banking" under different labels and to pursue innovation that is authentically distinct: technically compliant and also ethically meaningful in its economic effect.

These conclusions should be set against the industry's likely trajectory. As Islamic finance expands into new markets and digital platforms, pressure to standardize hiyal-based products will intensify. Standardization led by bodies such as AAOIFI could entrench the most permissive, form-focused interpretations for the sake of interoperability, or become the route by which stricter, more Maqasid-oriented standards are adopted. The shift from Bay' al-'Inah toward Musharakah Mutanaqisah in home financing suggests that part of the industry is moving in the latter direction, driven as much by market and reputational pressure as by scholarly consensus.

The scale of this imbalance is visible in market data. Tawarruq was reported as the second most widely used financing product globally at nearly 22% (IFSB, 2017, as cited in Ahmad, 2020); in Malaysia, Murabahah-based financing, which includes Tawarruq, exceeds 57% of Islamic financing (Bank Negara Malaysia, 2018, as cited in Ahmad, 2020); and in the GCC, Tawarruq has been estimated at roughly 80% of financing products in Saudi Arabia and 50% in the UAE (Al-Jarhi, 2013, as cited in Ahmad, 2020). Equity-based modes remain marginal: profit-and-loss-sharing contracts contribute roughly 10–15% of Islamic financing in Malaysia (Saleem et al., 2023), and a study of two Pakistani Islamic banks found Mudarabah averaging about 5% and Musharakah under 3% of financing, against Murabahah above 54% ("Comparison of Theory and Practice of Murabahah Financing in Islamic Banking," 2025). The IMF notes that Murabahah accounts for 70–80% of Islamic financing (International Monetary Fund, 2015). Although these figures come from different years and jurisdictions and cannot be aggregated into a global market share, they consistently indicate that al-hiyal-based, fixed-return structures dominate while risk-sharing structures remain a small minority.

Implications for Practice, Regulation, and Future Research

This ongoing negotiation has distinct implications. **Practitioners and Shariah advisory boards** should look beyond checklist compliance and assess the economic substance of products against the Maqasid al-Shariah. **Regulators**, particularly in dual-banking jurisdictions, must balance competitiveness against the sector's

ethical identity through sustained engagement with international scholarly opinion. **Researchers** can move the debate beyond doctrine with empirical studies of the economic effects of al-hiyal-based products on customers compared with conventional equivalents.

Critique: When al-Hiyal Replicates the Conventional Loan

The analysis above supports a sharper critique than the form-versus-substance debate usually receives. Where al-hiyal is used at scale, the product typically delivers the cash-flow profile of a conventional loan: funds advanced at the outset, a larger fixed sum repaid over a set tenor, and the customer rather than the financier absorbing the risk of the underlying transaction. In organised Tawarruq the commodity is a conduit never wanted for its own use, so no real asset justifies the return. Three consequences follow. First, risk is not shared: entitlement to a return in exchange for bearing asset or business risk, the feature that distinguishes permissible profit from interest, is largely engineered out, which is why fixed-return, non-profit-and-loss-sharing financing has been described as a back door to interest-based debt (Usmani, 2007, as cited in Saleem et al., 2023). Second, dependence concentrates risk and weakens the industry's claim to distinctiveness: a study of two Malaysian Islamic banks found extensive use of Tawarruq in personal financing and identified overreliance on a single contract as a challenge (Abdullah, M. M. I et.al., 2025). Third, reform can be cosmetic: Bay' al-'Inah and BBA products in Malaysia were largely replaced by Tawarruq or Musharakah Mutanaqisah once regulators required removal of mandatory buy-back provisions, and some banks have since moved legacy home-financing customers from BBA to Murabahah via Tawarruq (Islamic Bankers Resource Centre, 2019). Swapping one hiyal-based structure for another changes the paperwork but not the substance.

This critique should be stated with care. Hiyal-based contracts are not all equivalent, since classical Tawarruq involves more genuine commercial risk than organised Tawarruq, and regulators in dual-banking systems reasoned from real constraints: competitive pressure and the lack of infrastructure for risk-sharing. The argument is therefore not that these instruments must be abolished, but that heavy dependence on them is neither necessary nor consistent with the Maqasid al-Shariah.

Alternative Structures That Meet Market Demand with Less Reliance on al-Hiyal

A credible response must show that Islamic banks can serve mainstream demand (home purchase, personal liquidity, business working capital, project funding and start-up capital) through structures in which the bank holds real asset or business exposure. The table below outlines such alternatives by market need.

Market need	al-Hiyal-dependent incumbent	Viable alternative structure	How it differs, and what it takes
Home and property financing	Bay' Bithaman Ajil with Bay' al-'Inah; Murabahah via Tawarruq	Musharakah Mutanaqisah (diminishing partnership, with the bank's share leased through Ijarah) or Ijarah Muntahia Bittamlik (lease ending in ownership)	The bank co-owns the property and bears ownership risk, and its return follows rental value rather than a fixed marked-up debt. Malaysia's Shariah Advisory Council accepted the structure in 2006, when Kuwait Finance House Malaysia launched the first equity-based home financing (Subky, 2017). Constraints: higher documentation cost and bank risk (Subky, 2017); almost half of the Malaysian banks offering it had stopped by a 2010 review ("Musharakah Mutanaqisah Home Financing," 2010).
Vehicles, equipment	Organised Tawarruq; Murabahah	Ijarah / Ijarah Muntahia Bittamlik, or Murabahah for a genuine asset bought and	The bank owns the asset during the lease and bears its usage and ownership risks (typically covered by takaful), so the

and durable goods	with pre-arranged resale	delivered with payment made directly to the seller	return is tied to a real asset. Requires asset-management capacity on the bank's balance sheet.
Personal financing and consumer liquidity	Organised Tawarruq, the largest single al-hiyal exposure in the market data above	Purpose-linked financing (Murabahah, Ijarah or Istisna' for identifiable goods and services such as education, medical care and renovation, paid to the vendor); Ujrah (fee-for-service); Qard al-Hasan funded from social funds for small hardship needs	Finances the underlying need instead of cash-through-commodities. Some pure cash needs cannot be tied to an asset, so Tawarruq would remain a narrow fallback with safeguards: real commodity ownership and delivery risk, and no mandatory buy-back or inter-conditionality. Practitioners also cite Ujrah as a replacement for Bay' al-'Inah in cash and working-capital products (Islamic Bankers Resource Centre, 2019).
SME working capital and trade	Tawarruq or Bay' al-'Inah credit lines	Musharakah and Mudarabah with risk controls (staged disbursement, performance-linked profit ratios, guarantees); Salam and Istisna' for agriculture and manufacturing; supply-chain Murabahah tied to actual goods	The bank shares business risk and returns vary with performance. Banks avoid risk-sharing lending because of moral hazard and information problems (Saleem et al., 2023), consistent with its 10-15% share of Malaysian Islamic financing. Needs monitoring capacity, guarantee support and good data.
Corporate, infrastructure and project finance	Commodity Murabahah term facilities; sukuk with repayment promised at face value	Ijarah, Musharakah, Mudarabah and Wakalah sukuk backed by real assets and loss-bearing; diminishing Musharakah for projects	Returns depend on asset or project performance. Sukuk that guarantee repayment at par regardless of performance replicate debt, so the test is whether investors truly bear asset risk. Requires disclosure and investor education.
Start-ups and innovation finance	Little Islamic supply; conventional debt or Tawarruq	Musharakah-based venture capital, Islamic equity crowdfunding and peer-to-peer platforms	Direct equity exposure aligned with entrepreneurial risk; Abdul Rahman et al. (2020) examine venture capital strategies for musharakah financing. Constraints: small scale, valuation, exit routes and platform regulation.
Interbank liquidity management	Commodity Murabahah placements	Wakalah-based placements, Islamic collateralised funding and Islamic overnight benchmark rates	Requires a deeper Islamic money market and more eligible assets; Bank Negara Malaysia (2026) reports progress on the Malaysia Islamic Overnight Rate (MYOR-i) and Islamic collateralised funding.

Across these alternatives the common test is that the bank's return should depend on the performance of a real asset or business, and that the bank should bear the associated risk. Contracts that fail this test are al-hiyal in the forbidden sense, whatever their label. The alternatives are not costless: they demand valuation, monitoring and asset-management capability, legal and tax settings that do not penalise multi-step ownership transfers, and customer education about variable returns, which helps explain why Musharakah Mutanaqisah take-up

stalled in Malaysia. A realistic path is therefore a shift in the portfolio rather than wholesale replacement: narrow Tawarruq to a safeguarded fallback for genuine cash-liquidity needs, expand asset-backed and partnership structures wherever the need is tied to an asset or business, and track the change through published product-mix data.

For regulators, an existing lever is Value-Based Intermediation, introduced by Bank Negara Malaysia in 2017 to move Islamic banks from formal compliance toward the intended outcomes of Shariah (International Federation of Accountants, 2022). Its financing and investment impact assessment framework offers a tool for assessing products by outcomes (Bank Negara Malaysia, 2020). Building on it, regulators could require disclosure of the share of Tawarruq, asset-backed and partnership financing in each bank's book, consider capital, guarantee or tax treatment that lowers the cost of risk-sharing structures, and work with AAOIFI and the Islamic Financial Services Board to narrow cross-border divergence on organised Tawarruq. For researchers, the priorities are comparative studies of customer cost, default and satisfaction under Musharakah Mutanaqisah versus Tawarruq-based products, and a standardised cross-country dataset of financing by contract type.

Ultimately, the story of al-hiyal is not one of an industry quietly resolving a technical problem, but of Islamic finance continuously renegotiating its own identity. Its long-term credibility and public trust will be defined not by which side of the form-versus-substance debate "wins" but by its willingness to keep asking the question honestly as it scales. A sector that stops interrogating its al-hiyal-based structures risks becoming the conventional banking system relabeled in Arabic terms that its critics fear; one that treats the tension as a permanent, generative discipline is better placed to deliver finance that is not merely technically lawful, but genuinely, substantively just.

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