THE CONVERSATION

Academic rigour, journalistic flair

Image of a abandoned property project at Bukit Beruntung Malaysia. Provided by author, CC BY

Justice, trust and Sharia: why Malaysia must reform its Isla home financing

Published: December 6, 2025 10.02am GMT

Nuarrual Hilal Md Dahlan

School of Law, Universiti Utara Malaysia

Languages

Bahasa Indonesia

English

DOI

https://doi.org/10.64628/AAN.jrqt9cc9g

https://theconversation.com/justice-trust-and-sharia-why-malaysia-must-reform-its-islamic-home-financing-268366

Islamic home finance in Malaysia was introduced in the 1980s with high expectations. It promised to create a system free from *riba* (usury), *gharar* (harmful uncertainty), and *ẓulm* (injustice) for 20.6 million Malaysian Muslims.

Four decades on, the original vision of Islamic home finance as an ethical, risk-sharing alternative compliant to Islamic law Sharia is now being put to the test.

Ironically, Sharia-compliant home financing has been implicated in the government's recent findings, which identified 15,553 homebuyers affected by 107 abandoned housing projects comprising 29,587 units as of 30 September this year.

17 projek perumahan terbengkalai di Kelantan dengan lebih 1,00...

Some Shariah-labelled home financing products closely resemble conventional loans, highlighting the need for clearer and more substantive differentiation to better guide and protect consumers — a concern that has already prompted calls for reform.

Consequently, many families continue to make monthly payments for homes that remain unfinished, are delivered long past their promised dates, or — in some cases — never materialise at all.

These perceptions have eroded public trust and confidence in Islamic home-financing instruments.

Reforms aim at enhancing fairness, transparency, and shared responsibility are gaining momentum.

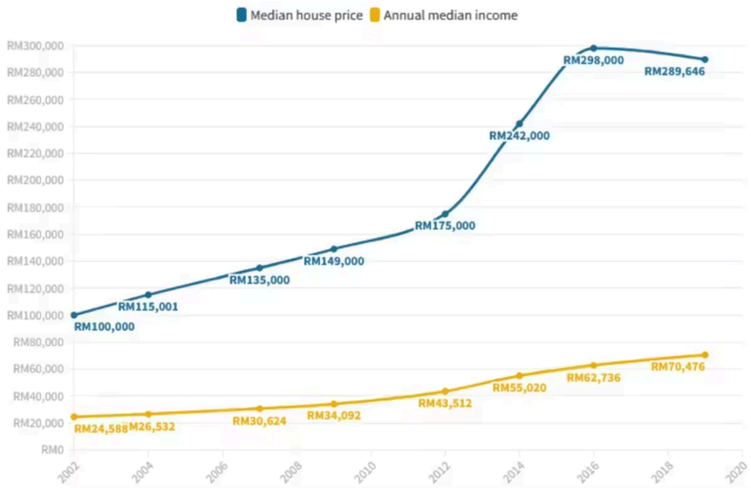
Read more: ***The government wants more of us living in high rises. Here's why Australians don't want to***

Form over substance: The problem with contentious contracts

The most common Islamic home financing structures in Malaysia are *Bayʿ Bithaman al-Ājil* (BBA, or deferred payment sale) and *tawarruq* (a deferred purchase followed by a quick resale for cash).

Both are designed to avoid the direct payment of interest. Yet, their financial outcomes often resemble those of conventional loans.

In a typical BBA arrangement, for instance, the bank purchases the property and resells it to the buyer at a marked-up price to be paid in instalments.



Soaring demand and scarce affordable supply continue to leave many Malaysians without accessible housing. Source: marketresearchmalaysia.

While this structure formally avoids charging interest, its economics are almost identical. Banks lock in fixed returns, while buyers bear the risks of non-delivery, delays, or even project abandonment.

This goes against the principle of *al-ghunm bi al-ghurm* — that profit should come hand in hand with risk.

Prominent scholars, including Justice Taqi Usmani, have warned that such contractual manoeuvres risk undermining the ethical foundations of Islamic finance.

Many homebuyers continue to service loans for projects that are severely delayed, partially abandoned, or unlikely to be completed.

Such financial and emotional burdens run counter to the *maqāṣid al-sharīʿah* — the higher objectives of Shariah, which uphold justice, welfare, and the protection of wealth.

Read more:* *Turning houses into homes: Community land trusts offer a fix to Canada's housing crisis

---

Pressures from the Basel Accord and investor expectations

Islamic banks are under growing pressure from global regulations and investor expectations. The Basel Accord enforces stringent capital, liquidity, and risk-weight requirements to maintain financial stability.

These regulations, however, make debt-based contracts such as *bayʿ bithaman al-ājil* (BBA), *murābaḥah* (a cost-plus resale on deferred payment), and *tawarruq* more capital-efficient — and therefore more appealing to banks.

By contrast, genuine risk-sharing models such as *mushārakah mutanāqiṣah* (diminishing partnership) and *ijārah* (Islamic leasing contract) typically demand more capital and appear less profitable on paper.

This dynamic forces banks to prioritise balance-sheet "safety," often shifting delivery risks onto homebuyers. In doing so, Basel inadvertently reinforces the "form over substance" dilemma that continues to shadow Islamic finance.

At the national level, neither the Shariah Advisory Council of Bank Negara Malaysia (SAC) nor the Shariah Committees (SCs) of individual Islamic banks are legally required to include consumer representatives.

To enhance fairness, Malaysia's Islamic finance sector should ensure that Shariah Committees are appointed and remunerated independently — a move that would reduce potential conflicts of interest and strengthen public trust.

As a result, borrowers' hardships — such as paying instalments for homes that are delayed or abandoned — often go unheard. Dispute mechanisms, meanwhile, tend to favour financiers, leaving affected families with little meaningful recourse.

Lessons from the Gulf

The Gulf Cooperation Council (GCC) countries face similar challenges — and have taken steps to guard against them.

Dubai, United Arab Emirates (UAE): A 2007 law mandates all buyer payments be placed in regulated escrow accounts to safeguard funds and ensure transparency.

Funds can only be released in line with verified construction progress. If a project stalls, the Dubai Land Department or a special tribunal may order refunds or transfer the project to another developer.

Bahrain: Established under a 2014 decree, the Stalled Property Committee is empowered to replace failing developers, merge projects, or liquidate assets to protect homebuyers.

Saudi Arabia: The Wafi off-plan sales programme and SAMA's escrow regulations ensure that buyer payments are ring-fenced, with any liquidation handled through the Infath Centre.

Malaysia’s Islamic financial system is among the largest and most comprehensive in the world. Uwe Aranas/ Shutterstock.com

Nonetheless, property development oversight and consumer protection in these GCC countries still require stronger safeguards and more consistent enforcement.

Read more: ***The hidden costs of building a home: what every family should know***

Pathways to reform

To restore public trust and uphold Shariah principles, Malaysia’s Islamic home financing should prioritise the Build-Then-Sell model — offering financing only for completed homes, thereby eliminating abandonment risks and avoiding harmful *gharar* (uncertainty).

Where the Sell-Then-Build model remains in use, developers should be required to provide insurance coverage and a clear rehabilitation plan within financing contracts. Shariah governance should also be strengthened through an independent consumer ombudsperson, third-party Shariah audits, and consumer representation on the country’s Sharia advisory council and committees.


Thousands of consumers have suffered long-term losses as a result of the stalled Forest City project. Sebastian Castelier/Shutterstock

Malaysia should also reform the Housing Development (Control and Licensing) Act 1966 (Act 118) to make financiers partially accountable when projects fail — creating a fairer balance of responsibility among banks, developers, and homebuyers.

To advance Malaysia's goal of fully embedding Islamic principles in banking and finance, the country could expand *sukuk*-funded housing programmes and create a dedicated rehabilitation fund to revive distressed or abandoned projects.

Read more: To end chronic homelessness, we must stop evictions

---

A National Islamic Housing Fund could adopt the Build-Then-Sell model and the profit-and-risk-sharing principle of *al-ghunm bi al-ghurm*, offering stronger protection for homebuyers.

Capital could be drawn from Khazanah Nasional Berhad, the Employees Provident Fund (EPF), the Retirement Fund (KWAP), Permodalan Nasional Berhad (PNB), and Tabung Haji. This could be reinforced through government guarantees, *musharakah*-based *sukuk*, and targeted contributions from *waqf* (Islamic endowments), *zakat* (mandatory almsgiving), and corporate social responsibility programmes.

If Malaysia and the GCC fail to reform Islamic home financing to make it more equitable and aligned with the principles of *maqāṣid al-sharīʿah*, the consequences could be severe.

Real estate properties in Selangor, Malaysia. Wisnu Gareng/ Shutterstock.com

Public trust in Islamic finance may likely to keep eroding without concrete action. Malaysia's goal of addressing its one-million-home deficit by 2026 — through a mix of financing instruments including Islamic options — could also be at risk.