

MUDARABA

ISLAMIC FINANCE

Definition

- ✉ Contract between two parties..
- ✉ Based on profit sharing.
- ✉ One party provides Capital-***Rabulmal.***
- ✉ The other Manages the venture- ***Mudarib.***



Elements of Mudaraba!

 Contracting Parties.

 Wording.

 Capital.

 Work.

 Profit/Loss rules.

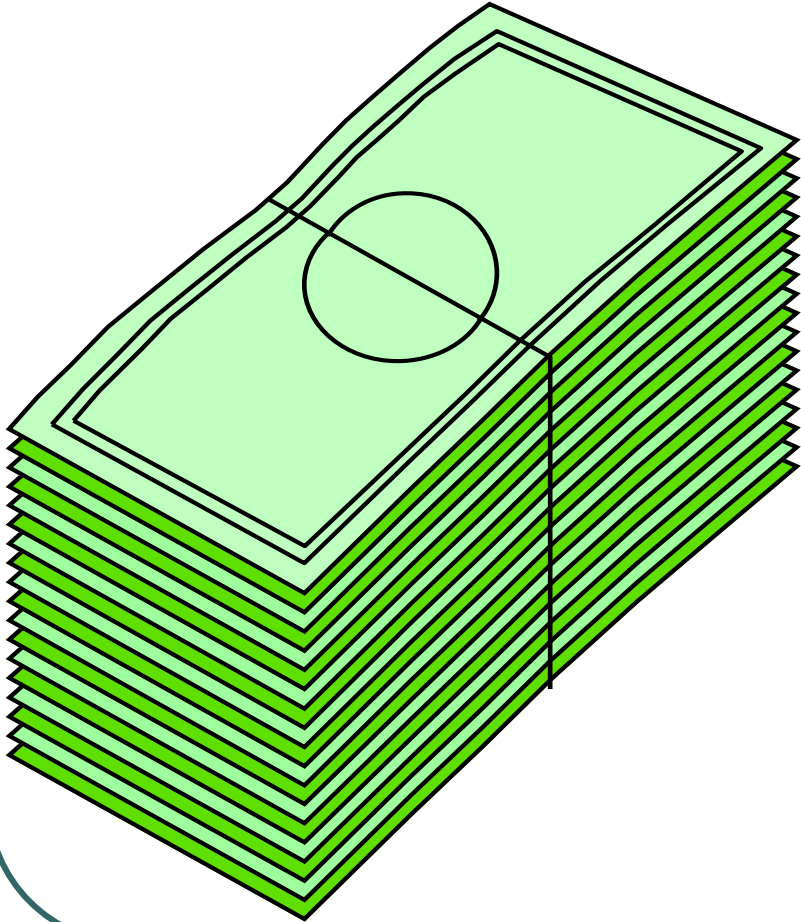
General Rules

- Contract can be for specific time period or open-ended.
- Can be in any type of lawful business. But Shafis limit it to trade.
- Capital should not be guaranteed by Mudarib.

General Rules....Cont.

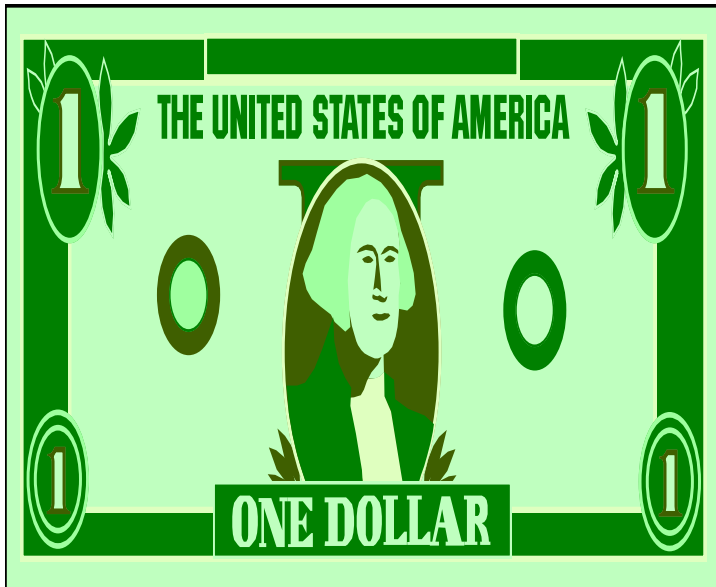
- Contract can be ***contingent*** on a condition to happen.
- Contract can be ***delayed***.
- Contract can be ***Restricted*** or ***Unrestricted***.

Juristic Rules of Capital!



- Should be know to Amount & Type.
- Should be in Cash. But Hanbali approved Trading and/or productive Assets as capital.

Capital.....Cont.!



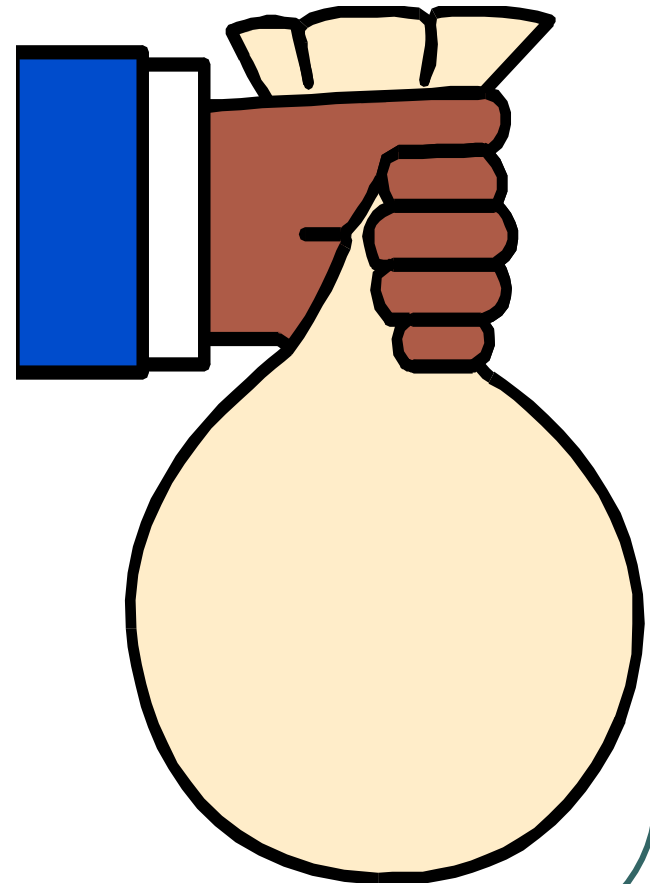
- ❏ Can not be debt with Mudarib or third party. However, Hanafis & Hanbalis approved third party debt.
- ❏ Mudarib Should have right to utilize capital.
- ☞ Commingling with other funds.

Third party debt as Capital!

- 📷 Approved by Hanafi & Hanbali because capital will be an asset as soon as collected.
- 📷 Maliki don't approve it because of extra burden on Mudarib.
- 📷 Shafis don't approve it because Mudaraba becomes Contingent & delayed, both unacceptable in their jurisprudence.

Delivery of Capital!

- ▶ Hanafi, Maliki & Shafi: Require actual delivery of capital. Not enough availing Mudarib to use of capital.
- ▶ Hanbali: Enough to make capital available to Mudarib.



Guarantee of Capital?

- ⌚ Unanimously not allowed to ask Mudarib for guarantee of capital to cover market risk.
- ⌚ Unanimously not allowed for Mudarib to offer voluntary Guarantee as part of contract to cover market or credit risk.

- ⌚ However, Rabulmal can ask for guarantee to protect him in case of negligence and/or misconduct of Musarib.
- ⌚ A few Maliki scholars allow a voluntary guarantee if offered after contract.

Third Party Guarantee

- Unanimously not allowed as part of contract.
- Allowed if independent of contract.

Rules Governing Management

- ❏ Exclusive right of Mudarib. No interference by Rabulmal as long as no violation of Shariah or terms of contract.
- ❏ Scholars rule that Mudaraba is invalid if Rabulmal places restrictions on Mudarib hindering his job.
- ❏ However they differed over types of restrictions.



Rules Governing Management?


- Majority of scholars don't approve Rabulmal participation in the management.
- Such condition invalidates contract. Management is Mudarib role.
- However, Hanbali scholars allow Rabulmal participation. They argue Rabulmal can participate in the management and is entitled to the same rights as the Mudarib.

Management rules!

- Majority of Scholars approve Rabulmal participation in management if:

-  Unconditional.

-  Under Mudarib mgt.

-  For no extra share of profit or Wage.



Rules Governing Management!

- scholars also differed over the extent of delegation to the Mudarib that is not possessed by virtue of contract.

Rights of Mudarib!

- By virtue of contract(unanimously agreed):



Buy/sell in Cash.



Recruit people to work in Mudaraba venture.

Hanafi & Shafi scholars –by specific permit- add:



Buy/sell on credit.



Transfer & receipt of goods.






Giving & taking Guarantee.



Appointing agents.

Rights of Mudarib cont.!

- By General delegation, Hanbali & Hanafi scholars, Rule that Mudarib can take the following decisions:
 -  Invest Mudaraba capital in another Mudaraba.
 -  Invest Mudaraba capital in Musharaka.
 -  Commingle Mudaraba capital with other funds.
- Maliki & Shafi scholars require specific permit from Rabulmal for this list of decisions.

Rights of Mudarib!

- ◆ Unanimously agreed that Mudarib needs specific permit to:
 - 👉 Exceed Mudaraba Capital i.e volume of business more than capital
 - 👉 Lend/donate all or part of Mudaraba capital.

Profit/Loss Rules!

- ☺ Profit is amount earned in excess of capital.
- ☺ Profit sharing should be pre-set and inserted in contract .
- ☺ Profit sharing can be reviewed bilaterally if contracting parties wish. However new arrangements apply to future profits.

Profit/loss rules!

- ☺ Rabulmal bears all losses.
- ☺ Can profit be designated to one Party?
- ☺ NO. Hanafi, Hanbali & Shafi scholars do not approve this. Contract changes to the status of loan if Rabulmal donate his share.
- ☺ Maliki scholars approve it as it takes form of donation by one party to another


Profit/loss rules:


- ☺ Who should bear Mudarib expenses?
- ☺ Hanbali scholars Opinion: To be charged to Mudaraba if contract stipulates. Otherwise chargeable to Mudarib share of profits.
- ☺ Hanafi & Maliki scholars Opinion: Chargeable to Mudaraba if Mudarib travels away to trade. Chargeable to Mudarib if he trades at home.
- Shafi scholars Opinion:
 - Chargeable to Mudarib share of profits in any case.

Profit/loss rules: Profit Allocation!


😊 Unanimous Agreement that:

 Profits to be shared as agreed.

 Profits are protection of capital.

 Profits are distributed by permission of Rabulmal.

😊 Conflicting Views about:

 Profit distribution before liquidation.

 Mudarib permanent entitlement to profits.

General Rules!

- ***Unrestricted Mudaraba:***

- ↑ General-in any business.

- ↑ With general delegation.

- ↑ No specific delegation.

- ***Restricted Mudaraba:
As to:***

- 📷 Type & place of work.

- 📷 Duration.

- 📷 Customers/clients to deal with.

- 📷 Area of business

General Rules: Status of Mudaraba!

➡ Effective.

➡ Temporary.


➡ Contingent.


➡ Delayed.

Status of Mudaraba!


- ***Effective:***


 Starts immediately after signing.


 Capital immediately delivered.

 Work immediately begins.

- ***Fixed term:***


 Term is fixed in contract.


 To be liquidated when period has elapsed.

 If renewed, then that is a different contract.

Status of Mudaraba!

- ***Contingent:***

 Depends on something to happen e.g raising certain amount of funds.

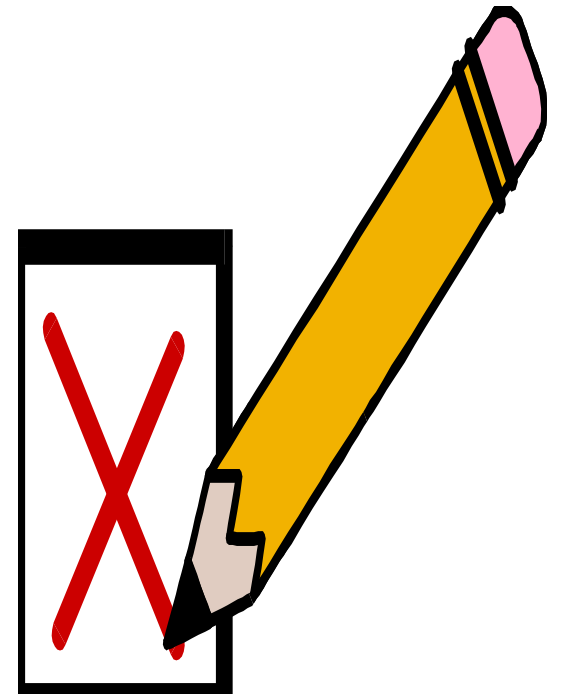
 If it didn't happen, no contract.

- ***Delayed:***

- Tied to a condition delaying its execution to a future date.
- Hanafis & Hanbalis scholars approved all four statuses. Maliki & Shafi scholars approve the first one only.

Violation Of Contract!

- If Mudarib violates any of the terms of the contract then:
 - ⌚ He is guilty of misconduct.
 - ⌚ His status changes from that of Mudarib to guarantor.
 - ⌚ Funds become debts payable by him.



Revocation of Mudaraba!

- ❏ Mudaraba is revoked due to non-fulfillment of any of its terms.
- ❏ If so partner is no longer Mudarib but employee of Rabulmal.
- ❏ He works for salary not profit sharing.
- ❏ Funds remain with him as trust not Mudaraba capital.
- ❏ Realized profit go to Rabulmal.


Status of Mudarib!


- ✉ As trustee.
- ✉ As Partner.
- ✉ As Agent.
- ✉ As Hired Worker.
- ✉ As Confiscator.

Status of Mudarib!

- ***As Trustee:***


Before Starting Work
Mudarib is a trustee:

 Money with him is deposit.

 Not responsible for its loss except in case of negligence and/or misconduct.

- ***As Partner:***

As soon as profit are realized:

 Mudarib becomes partner in this profit.

Status of Mudarib:

- ***As Agent:***

After starting work:

- ✉ Mudarib becomes agent of Rabulmal.

- ✉ He acts on his behalf.

- ***As hired Worker:***

If contract is revoked:

- ✉ Mudarib Status changes to that of a hired worker.

- ✉ He works for salary, not a share in profits.

Status of Mudarib:

- ***As Confiscator:***

On violation of any terms of contract by Mudarib:

 His status changes to that of confiscator.

 He guarantees repayment of capital.


 Has no wage or share in profits.


Five Forms of Mudaraba:

- ☺ **Form 1:** One Mudarib & one Rabulmal.
- ☺ **Form 2:** One Mudarib Providing some capital & the Work, and one Rabulmal providing some capital too.
- ☺ **Form 3:** One Mudarib & one rabulmal who provides capital and participates in the work.
- ☺ **Form 4:** one Mudarib & more than one Rabulmal.
- ☺ **Form 5:** More than one Mudarib & one Rabulmal.


Termination of Mudaraba Contract


- ***Normal Reasons:***

 Hanafi, Hanbali & Shafi scholars: Any party can terminate Mudaraba contract anytime.

 Maliki: Mudaraba Contract can not be terminated if Mudarib started working. Because Capital is not liquid.

- ***Force Majoure Reasons:***

 Hanafi, Hanbali & Shafi: Contract is terminated for the death of any party.

 Maliki: Death of any party doesn't terminate Mudaraba. It can be inherited.