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MUDARABAH IN ISLAMIC FINANCE: A CRITICAL ANALYSIS OF INTERPRETATION & IMPLICATIONS

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ABSTRACT

Mudarabah is one of the important methods of Islamic financing broadly used in different fields including Islamic banking. It is normally considered as lawful and arguments from Quran & Hadith and other sources are given for its justification. But the real fact is that, its legitimacy cannot be proved from any source. The verses of Quran which are presented in favour of it, do not have any relationship with this typical type of partnership. Same as any proof from the books of Hadith cannot be presented in this regard. On the same line, arguments other than Quran and Hadith are also unable to provide any reason for its validity.

Keywords: Mudarabah, Quran, Hadith, Justification, Arguments.

INTRODUCTION

By nature *Mudarabah* is a special type of Partnership between at least two types of partners one partner provides the capital who is or as *rabb-ul-maal* or the investor and the second is term as *amil* or *Mudarib* who is responsible for the working and management of business (Saleh, 1986). According to the conditions imposed by Muslims scholars former's role is restricted to provide finance in the business and he cannot take part in the business even his agent also cannot participate in the business (Gazi, 1993). The worker or *amil* is completely responsible for all the affairs of the business (Chapra, 2005). Whereas the distribution of profit – loss is concern in case of profit it will be distributed in a pre-decided ratio and in case of loss only *rabb-ul- maal* bear it (Siddiqui, 1969). The reason is that since *amil* has not invested in the business hence is loss will be in that form of

labour which he has lost. But if this loss is due to the negligence of worker then he will also responsible for that. In this type of partnership in case of liquidation the liability of *rabb-ul-maal* is limited to his investment unless he has permitted the *mudarib* to incur debts on his behalf. In this case all assets which are purchased by *mudarib* are solely owned by *rabb-ul- maal* and *mudarib* can earn his share in the profit only and cannot claim his share in the ownership of assets. (www.islamicbanker.com/mudarabah-introduction).

JUSTIFICATION OF MUDARABAH

From Islamic point of view it is an important method of financing and provides a sound base of working for Interest Free Banking, which is largely dependent on it (Rammal and Zurbuegg, 2007). Whereas the legal base or justification of this method is concern three types of arguments are given in this regards. These sources are Quran, Hadith and some analogous arguments. These reasons and their critical analysis is as follows.

Quranic Arguments in Favour of Mudarabah

Three different verses of Quran are presented to justify this act. These verses are as follows.

Translation: While others travel in the land in search of Allah's bounty (Chapter 73, Verse 20).

It is claimed that, justification of *Mudarabah* can be proved from the initial four words. *Mudarabah* is derived from the word *Zerab* which is used in the Arabic language in the meaning of "to beat", "to hurt", and "to Struggle". On this basis these words have the meaning of struggle or walk on the earth. Since in the case of *Mudarabah*, partners do the struggle for the bounty of Allah, hence these words justified the act of *Mudarabah* (Taseen, 2002).

In this context second and third verses are as follows.

Translation: And when the prayer in ended, then disperse in the land and seek of Allah's bounty (Chapter 62, Verse 10).

فَإِذَا قُضِيَتِ الصَّلَاةُ فَانْتَشِرُوا فِي الْأَرْضِ وَابْتَغُوا مِنْ فَضْلِ اللَّهِ وَاذْكُرُوا اللَّهَ كَثِيرًا لَعَلَّكُمْ تُفْلِحُونَ ﴿١٠﴾

Translation: It is no sin for you that you seek the bounty of Allah (by trading) (Chapter 2, Verse 198).

لَيْسَ عَلَيْكُمْ جُنَاحٌ أَنْ تَبْتَغُوا فَضْلًا مِنْ رَبِّكُمْ

It is

reason

that since in these words order is given to Muslims for the struggle of bounty of Allah and in case of *Mudarabah* partners struggle for the same, hence these words also prove the legality of this act.

Rebuttal of Arguments Given From Quran

In- fact all conclusion which are drawn from the first verse are completely out of context, it can be cleared from the following facts.

Whereas the words of first words are concern in these words a general order is given to all Muslims for the struggle of bounty of Allah. These efforts may be in unlimited forms and Quran has not emphasized on a particular form like *mudarabah* or any other condition. Hence it is impossible to draw a conclusion about any specific form of business from these words.

The words which are used in these verses are also repeated at some other places e.g. In the verse 94 of Chapter 4 these are used for any struggle in the way of Allah. In the same line verse 101 of same Chapter these are used just in the meaning of travelling. Hence it is impossible to draw the sense of any specific meaning for these words.

As far as the last two verses are concern which are given in this regards, in both of these verses again a general order is given to all Muslims to struggle for the *fadal* of Allah. *Fadal* is another Quranic term which has the meaning of excess wealth, power, courtesy of Allah, increase in honour, respect etc (Siddiqui, 1996). Again it is a general order given to all Muslims and a conclusion about any specific form of business cannot be drawn from them.

On the basis of above arguments it can be said that justification of *Mudarabah* from Quran is not possible, because all verses which are presented in this regards do not have any direct or indirect link with this special type of partnership. It is interesting to note that validity of *Mudarabah* cannot be proved from Quran in-fact Quran openly deny its base. As a matter of fact Quran did not recognize the reward of any capital in any form (Aziz *et al.*, 2011). On this basis *Mudarabah* is completely against the teaching of Quran. The reason is that in such type of partnership the financier (*Rab-ul-mal*) takes the rewards of his capital which is strictly prohibited by Quran in Chapter 2 verses 275-179. Hence, this method is against the basic teaching of Quran.

Hadith as a Reason of Mudarabah

From this source five different types of arguments are given in this regards which are as follows:

It is claim that some companions of Prophet Muhammad (P.B.U.H) has done this types of partnership. The Prophet Muhammad (P.B.U.H) did not stop them but allowed them to do the same. In this regards the names of some prominent *sahabah-e-kram* e.g. Umar Farooq, Utman (second and third caliphs), Abu Musa Ashari & Abbas are given and it is claimed that these personalities were involved in this types of business (Qasim, 2003).

Some impressions of companions of Prophet are also coated in this context regarding the very nice behavior of Prophet Muhammad (P.B.U.H) as a businessman or as a partner in the business.

One incidence from the life of Prophet Muhammad (P.B.U.H) is quoted in this context. According to this event Prophet Muhammad (P.B.U.H) has given one *denarto* a *sahabi*Urvab. AbiJa'ad Al-barti to purchase a goat for the purpose of *quarbani*(slaughtered animal in the way of *Allah*). He has purchased two goats from this amount and sold one of them against one *denar*, and presented the goat and one *denarto* prophet Muhammad (P.B.U.H) and described all details of the event. Prophet was happy and gave him blessings and donated that, particular *denar*, (Abu-Daud et al., 1950). Supporters of *mudarabah*claim that, it is an example of this type of agreement. Hence on this basis *mudarabah*is lawful.

Another event which is reported in the *Sanun-al-Kubra Al-Bay, bahaki* also presented as a proof of *mudarabah*. According to the text, two sons of second caliph Ummer Farooq were included in an army mission which was sent to Iraq. This army has stayed at Basara Province. The governor of Basra has given warm welcome to the sons of caliph and when this mission was returning to Madina City he handed over them some *mal* (Cash and merchandise etc.) to deliver it to the caliph. With that he suggested if, they can purchase some commodities form his province with this *mal* and sell them out in Madina. Keeping the profit by themselves and will return the original amount to government exchequer. They have liked this suggestion and followed the same line of action. But when caliph came to know this event he ordered them to return the profit also to government exchequer because it was an open discriminatory action, which has given undue advantage to his sons as compare to the rest of army men. On his order, one of his sons has followed it, but the second raised the point that, they were collateral of that merchandise. If it was lost or damaged in any form then they were responsible for that. But the caliph did not accept this reason and kept his decision intact. At this time one person who was present there during this discussion suggested the caliph to consider this transaction as *mudarabah*. This point has impressed the caliph and he has allowed to keep the profit to his sons (*Al-Bayhaki et al., 458H*). This event is also presented as an example of *mudarabah*. (Ayub, 2010).

The economic transaction between Prophet Muhammad (P.B.U.H) and Hazrat Bibi Khadija before Prophet-hood is also presented as an example of *mudarabah* transaction

REFUTATION OF REASONS DERIVED FROM HADITH

As far as these reasons are concerned none of them fulfill any standard of reasoning. Their critical analysis is as follows:

Whereas the first argument is concerned it cannot be acceptable, because any detail of such type of agreements is not available in which it is described that, what was the nature of agreement? With

what terms and conditions it was applicable? etc. definitely it is not enough just to say that any particular *sahabi* has done the same until its detail is not found. Hence this claim cannot be a base of justification of *mudarabah*.

The situation is quite same in the case of second reason, any detail of any partnership deed is not available on which it can be said that, Prophet Muhammad (P.B.U.H) has ever done any such type of agreement. Hence this claim also cannot be accepted.

As far as that event is concerned in which as *Sahabi* has purchased a goat under the order of Prophet Muhammad (P.B.U.H), this event cannot be treated as a *mudarabah* agreement on the following grounds:

According to the conditions of *mudarabah* it should be a business agreement. But in this case it was not so. Prophet has given the order to purchase the goat just for the purpose of *sadaqa* (donation in the way of Allah) not for any business deal. Hence it cannot be treated as *mudarabah*. In *mudarabah* agreement profit / loss should be decided at the start of the business in this transaction this condition is not fulfilled.

Another condition of *mudarabah* is also absent in this case under which partnership should be based on a agreement between finance and worker for a particular business. In this event prophet did not give the permission to do any business to the sahib. It was his personal decision. Hence any condition of *mudarabah* is not applicable here.

It is important to note that, Prophet Muhammad (P.B.U.H) has donated that particular *denar* which was saved by that *Sahabi*, this action of the Prophet clearly shows that he was not ready to keep that income which was not the result of his dint of labour. This fact also proves that it was not a agreement of *mudarabah*. The event which is related to the sons of second caliph ummer is also failed to qualify as *mudarabah* agreement due to the following reasons.

The amount which was given to them was a debt, whereas in case of *mudarabah* the amount given by the financier to worker is treated as a charge or deposit. In this case both brothers were guarantors of that merchandiser. Hence it cannot be seen us any *mudarabah* agreement. In case of *mudarabah* it is necessary that profit / loss ratio should be decided at the start of the business. This basic condition is also violated in this agreement. Hence again it cannot treated as any *mudarabah* agreement. In the event which is related to the sons of caliph, it is interested that, both Sons were not aware of the fact that they were doing an agreement of *mudarabah*, It was just a suggestion given by that person which was present at time. It was not a predicated matter neither profit I loss ratio was decided. Moreover the role of governor of Basra cannot be treated as financier. Hence from any angle this event cannot be treated as *mudarabah*.

On the same line the economic transaction between Prophet Muhammad (PBUH) and *HazratBibi* Khadija cannot be and base of *mudarabah* because all books in which this event is reported categorically admit that, it was not the case of profit sharing, because the remuneration of Prophet in each visit was pre-decided. Moreover two other factors also prove that it was not the case of *mudarabah*. First one slave of *HazratBibi* Khadija Maysara was with the Prophet in both visits. It is an open violation of this type of agreement, according to which financier or his agent cannot take part in business in any way. Second Prophet Muhammad (P.B.U.H) has sold the merchandise of *HazratBibi* Khadija in Syria and purchased some other commodities for *HazratBibi* Khadija and delivered them to her, which she personally sold. This act is another violation of this type of agreement according to which there is no role of financier in the business. Hence it is concluded that, this transaction cannot be treated as *mudarabah* from any angle.

SOME ANALOGOUS ARGUMENTS

Following presumptive reasons in favour of this act are also given:

It is said that, this agreement has a deep resemblance with *Ijara* (rent) and *mazara* (share cropping). Since both of these are considered as lawful hence on this basis *mudarabah* should also be treated as lawful. another reason is that, since in the eyes of *shariah* the income which is subject to risk is considered as lawful. Hence on this basis income of this agreement should also be considered as valid.

It is claimed that in this case worker and financier got the reward of their labour and capital respectively which is according to the law and justice. Hence no objection can be raised in this context on the validity of this agreement.

Last reason in this context is that *mudarabah* is a good method both for financier or worker. In case financier do not has skill and worker does not has finance. Then through this method both of them can utilize their resources and got profit from the business.

NEGATION OF ANALYSIS ARGUMENTS

All arguments which are given under this title are completely baseless. Their critical analysis is as follows:

It is claimed that *mudarabah* should be considered as valid because it is quite similar to *mazara* (share cropping) and *ijara* (rent). Since both of these are recognized hence it should be considered as lawful. In this regard whereas the concept of *mazara* is concerned, it cannot be said that it is a well recognized concept. There are a lot of conflicts between Muslim thinkers in its validity. Hence on the basis of a quite controversial concept how another concept can be recognized? Moreover

since Quran did not recognize the concept of Private ownership of land (Aziz and Naveed-ur-Rehman, 2012), hence on this basis concept of *mazara* automatically vanished out whereas *ijara* (rent) is concerned not doubt it is well accepted by Muslim thinkers but the matter of fact is that it is openly against of Quranic teachings and all agreements which are given in this regard are completely base less (Aziz and Farooq, 2004). Hence *Ijara* cannot be treated as base for the validity of *mudarabah*.

As far as the validity of that income is concerned which is considered as lawful on the basis of risk, it can be proved in any way. The simple proof in this regard is that, Quran has strictly prohibited any gambling transaction (Chapter 5, verse 90) in which the highest degree of risk is involved. Hence on this basis it can be claimed that risk in any case cannot be the base of legal income. Hence from this agreement also validity of *mudarabah* cannot be proved.

CONCLUSION

On the basis of this discussion it can be concluded that, all arguments which are given to prove the validity of *mudarabah* from Quran, *Hadith* and in the form of analogous arguments are unable to provide any solid reason to justify the *mudarabah* agreement. Conclusions which are drawn from first two sources do not have any relationship with this particular type of agreement. The last types of arguments are against the basic teachings of Quran. Hence *mudarabah* is a completely unlawful agreement and do not has any legitimate base.

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