

Definition of Mudarabah:

"Mudarabah" is a special kind of partnership where one partner gives money to another for investing it in a commercial enterprise. The investment comes from the first partner who is called "rabb-ul-mal", while the management and work is an exclusive responsibility of the other, who is called "mudarib."

Its Authenticity in Islam

Hazrat Khadijah gave capital for business and our Holy prophet Muhammad (salAllahu alaihe wassalam) did business from her capital.

Overview:

The rabb-ul-mal may specify a particular business for the mudarib, in which case he shall invest the money in that particular business only. This is called al-mudarabah al-muqayyadah (restricted mudarabah). But if he has left it open for the mudarib to undertake whatever business he wishes, the mudarib shall be authorized to invest the money in any business he deems fit. This type of mudarabah is called 'al-mudarabah al-mutlaqah' (unrestricted mudarabah)

A rabbul-mal can contract mudarabah with more than one person through a single transaction. It means that he can offer his money to A and B both, so that each one of them can act for him as mudarib and the capital of the mudarabah shall be utilized by both of them jointly, and the share of the mudarib shall be distributed between them according to the agreed proportion. In this case both the mudâribs shall run the business as if they were partners inter se.

The mudarib or mudâribs, as the case may be, are authorized to do anything which is normally done in the course of business. However, if they want to do an extraordinary work, which is beyond the normal routine of the traders, they cannot do so without express permission from the rabb-ul-mal.

Rules of Profit & Loss in Mudarabah

- Profit may be distributed at any agreed ratio.
- In case of loss, all loss will be borne by the "Rabb-ul-Mal". Mudarib's share of profit will not be given to Rabb-ul-Mal.

Different Capacities of Mudarib

Ameen (Trustee): The capital of Mudarabah is an Amanah in the hand of Mudarib, therefore if any loss incurs to business without negligence of Mudarib, Mudarib will not be liable for that loss.

Wakeel (Agent): When Mudarib starts the business, he becomes an Agent of Rabb-ul-Mal. Therefore, all the business activities will be carried out on behalf of the principal. And if principal (Rabb-ul-Mal) gives any instructions, Mudarib is bound to comply with these instructions.

Shareek (Partner): In case of profit, Mudarib is partner in that business to the extent of his profit share.

Dhamin (Liable): If Mudarib disobeys the instructions of Rabb-ul-Mal, he is liable for loss.

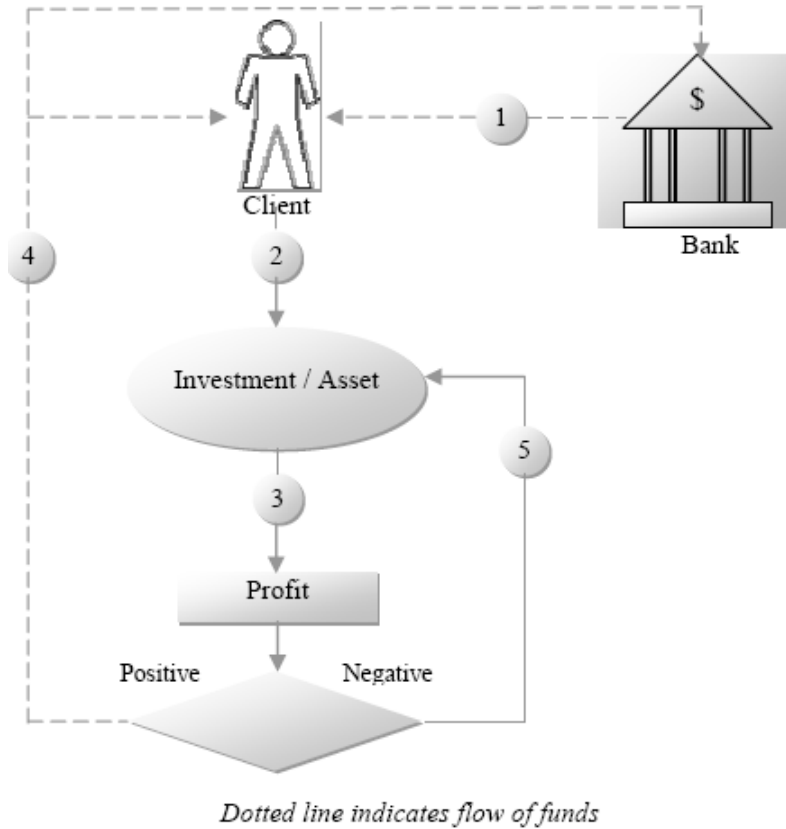
Ajeer (Employee): If Mudarabah becomes void due to any reason, then Mudarib is Ajeer. He is entitled to get normal salary (Ujrat-e-Misl).

Rules for Termination of Mudarabah Contract

- Each partner can terminate Mudarabah at any time.
- If a time period is fixed in Mudarabah, then all partners will be responsible for the completion of this period.
- Physical liquidation is not necessary, constructive liquidation can also be performed.
- After liquidation all business expenses will be deducted from the capital.
- Mudarib will bear all those expenses which are normally considered the responsibility of Mudarib. Although, the expenses which are not considered the responsibility of Mudarib will be deducted from the entire capital.
- Capital of investor will be returned to him. Remaining amount will be the profit and distributed according to agreed ratio.

Mechanism:

A simple Mudaraba financing structure is presented below:



Activity:

- 1: Bank and Client discuss business plan; Bank provides funds to client towards capital investment;
2. Client sets up the business and manages its operations;
3. Business generates positive or negative profits;
4. Profits if positive are shared between Client and Bank as per a pre-agreed ratio;
5. Profits if negative are absorbed by Bank; effectively bringing down the value of the asset created with its investments

Differences between Musharakah (Shirkah) & Mudarabah

In Musharakah	In Mudarabah
Investment from each partner	Investment from one partner while working from other partner
Every partner can be a working partner	Investor cannot be a working partner
Every partner bears loss according to ratio of his Investment	Only Rabb-ul-Mal suffers loss
Every partner's liability is unlimited	Investor is liable up to the amount of investment
If both the partners give investment in joint pool and an asset is purchased from that investment, all partners will be co-owners of that asset, so if value of that asset is increased, all will get benefit	Asset purchased from investment of investor, remains in the ownership of investor before sale. Therefore, if it is terminated at this stage, Mudarib is not entitled to share in the exceeding price of that asset