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Legal Application of Musharakah Mode of Finance in Islamic Banking

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Introduction

MUSHARAKAH IS A MODE OF FINANCE IN ISLAMIC BANKING, albeit one of the many Islamic banking products.[2] It is an arrangement whereby the bank and its client come together under a partnership or joint venture arrangement, both parties pulling in their capital contributions to engage in a business venture[3] with a view to sharing the profits accruing there from as well as the losses thereof according to an agreed ratio.

The participation of the bank in such business arrangement is based on the principle of Islamic finance which encourages earnings through participation in business activities involving sharing of risks and profits[4] but discourages activities involving interest and speculative trading.[5]

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2 Other Islamic banking products are *mudarabah*, *murabahah*, *salam*, *ijarah*, *bai bithaman ajil* (BBA—a deferred payment sale contract), *musharakah mutanaqisah* (MMQ—diminishing partnership), *istisna*, and *bai inah*, the last three being essentially Islamic modes of home financing.

3 See Salahudeen Ahmed, *Islamic Banking Finance and Insurance: A Global Overview*, Kuala Lumpur, A.S. Noordeen, 2nd edition, 2009, 27.

4 Sharia prohibits usury (*riba*) or interest but permits trade by the provision in Quran 2:275 thus: "The non-believers say that sale is very similar to *riba*, Allah has permitted trade and prohibited *riba*." With this provision, trade is encouraged, with the profits therefrom shared as predetermined by the parties to a partnership transaction. Prof. M. N. Siddiqui (2004) has clarified that failure to see the difference between sale (trade) and interest is a product of a flawed mentality. See as cited in Hifzur Rab, *Economic Justice in Islam: Monetary Justice and the Way Out of Interest(Riba)*, Kualar Lumpur, A.S. Noordeen, 2006, 90.

5 See Quran 2:274–281; 3:130; 4:161; and 30:39. Jabir said that Allah's Messenger cursed the acceptor of interest and its payer and the one who records it and the two witnesses, and he said: "They are all equal." Sahih Muslim, Hadith 3880 and 3881.

Being one of the many and perhaps one of the best modes of Islamic finance, this work seeks to examine the nature of *musharakah* and the various forms of use it can be put into in Islamic financing. The work chronicles the various rules guiding *musharakah* arrangement ranging from rules on securitization to rules on liquidity of capital contribution as well as the rules on mixing of capital. Various misgivings about *musharakah* financing are also carefully analyzed as well as the manner(s) in which such contracts can be invalidated by the element of *gharrar* (uncertainty).

Musharakah has its root in the Arabic word *shirkah*, meaning "being a partner." Therefore *musharakah* can be said to mean a joint venture into a business in which both parties make capital contributions and are also both involved in the management of the enterprise with profits and losses accruing shared in accordance with agreed predetermined ratio[6].

Shirkah, which is the root of *musharakah*, is in two major types. One of the two types, *shirkatul-aqd*, partnership by contract,[7] is more relevant to the subject of this research work. *Shirkatul-aqd* can be of three major types, namely: *shirkatul amwal* (partnership in capital), *shirkatul aamal* (partnership in service) and *shirkatul wujooh* (partnership in goodwill).[8] The first type, *shurkatul amwal* (partnership in capital) is the focus of this work and shall interchangeably be used with the term *musharakah* throughout the research work. *Musharakah* can be used to finance a plethora of modern banking products of Islamic banks.[9] In term of Asset financing, *musharakah* can be used for project financing, short-/medium-/long-term financing, import financing, small and medium enterprises setup financing, large enterprise financing, road and bridge construction financing, import bill drawn under import letters of credit, inland bills drawn under inland letters of credit, letter of credit with margin (for *musharakah*)[10]; export financing (pre-shipment financing), running accounts financing/short term financing; working capital financing.[11]

In terms of liability financing, *musharakah* can be used[12] for inter-bank lending/borrowing; for current/saving/investment accounts (deposit giving, profit based on *musharakah* with predetermined ratio)[13]; treasury bill and federal investment bonds/debenture; securitization for large projects (based on *musharakah*); term finance cer-

6 Several authors have made attempts at defining the concept. Akran Khan defines *musharakah* or partnership as a contract between two persons who launch a business of financial enterprise to make profit. See Akhram Khan, *Glossary of Islamic Finance*, Mansel, London, 1990, 100. Ibn Arfa also defines it as "An agreement between two or more persons to carry out a particular business with the view of sharing profits by joint investment." See Ibn Arfa, "*Mukhtesan* of Sidi Khalil," cited in Abbdur Rahman Doi, *Sharia: The Islamic Law*, A.S. Noordeen, Kuala Lumpur, 1984.

7 The other type of *shirkah* is *Shirkat-ul Milk* (partnership by joint ownership) which may also either be the optional type (*ikhtian*), where parties voluntarily purchase property together or the compulsory type (*ghair ikhtian*), where parties, for example, inherit a property together.

8 The three forms of *shirkatul aqd* are each divisible into *shirkat al-mufawada* (where capital and labor and profit are equal) and *shirkat ul-ainan* (where capital may be equal but profits are not equal, and vice versa). See Dr. Muhammad Imran Ashraf Usmani, *Meezan Bank's Guide to Islamic Banking*, Karachi, Darul Ishaat, 1st ed., 2002, 89. See also generally, Muhammad Taqi Usmani, *An Introduction to Islamic Finance*, New Delhi, Idara Isha'at-E-Diniyat(P)Ltd., 2008, 31.

9 Imran Ashraf Usmani, 103.

10 Letter of credit (LC) without margin is taken care of by *mudarabah*.

11 The list is not exhaustive, however.

12 Muhammed Imran Ashraf Usmani, 103.

13 This arrangement can also be on *mudarabah*.

tificates and certificate of investment; Islamic *musharakah* bonds (based on projects requiring large amounts-profit based on the return from the project.

Generally, in shareholder/banker/customer relationship, *musharakah* transaction may play out in several ways. It is the appropriate contract between bank and shareholders where the shareholders constitute management of the bank and the members of management are shareholders.[14] *Musharakah* is also the suitable contract between the bank which advances money for a business (where it also participates in management of the business) and the entrepreneur to whom money is advanced if such entrepreneur has his own contribution to the capital either through deposit account or by other legally acceptable means.

Basic Rules of *Musharakah*

Since *musharakah* is a kind of joint commerce, which comes into existence by contract, then all the required elements of a valid contract must be present. These include the existence of partners (*muta'aqideen*), presence of capacity[15] on the part of the partners to enter into contract, presence of consensus ad idem,[16] and there must be presence of commodity or service which is the subject matter of transaction.

Apart from the foregoing, there are other rules which may not be applicable to other forms of contract but are peculiar to *musharakah*. One of such rules is that in *musharakah*, both parties must take part in capital contribution and both parties have the right to take part in the management of the business[17]. Other rules have to do with controversies surrounding the issue of capital contribution by parties; and the issue of sharing of profit and loss both of which will be addressed herein.

Capital Contribution by Parties

While sharia jurists agree on the requirement of involvement of both parties in the capital contribution to *musharakah* business,[18] there is difference of opinion regarding the nature of such capital. Some jurists hold that the sharia allows that a party's contribution may be in money while the other party's capital contribution is in material form or any other lawful asset. According to Imam Abu Hanifah,[19] capital contribution in any other form other than money is not allowed. His view is promised on the reason that if it is allowed, then capital of the partners become distinguishable and therefore no part-

14 This is because, in *musharakah* both parties must have capital contribution and both must be accorded the right of participation in the management of the business. Nonetheless, the parties to *musharakah* may agree that one partner becomes active while the other is a sleeping partner. Where this happens, the sleeping partner cannot, even by agreement, have ratio of profit exceeding the ratio of his investment. See Muhammed Imran, 92.

15 Parties must be legal persons and must not be minors and must be sane.

16 Consent must be freely given and not obtained by duress, undue influence or misrepresentation. See, generally, Yahya Bambale, *Islamic Law of Commercial and Industrial Transactions*, Zaria, Malthouse Press Limited, 1st edition, 2007, 22–59.

17 However, the parties may also agree on who should be in charge of the management. The Bank Negara Malaysia (BNM), in its set sharia parameters for *musharakah* contract, suggests that *musharakah* venture may be managed in the following manner: i.) management by all partners, or ii.) management by certain partners or single partner; iii.) management by a third party. See Noraziah Che Arsad and Abdul Ghafar Ismail, "Sharia Parameters for Musharakah Contract: A comment," *International Journal of Business and Social Science*, Vol. 1 No 1, 2010, 152.

18 *Ibid.*, 149.

19 Imam Ahmad Hambali holds the same view as Imam Abu Hanifah.

nership can take place if the property contributed by each partner is distinguishable from that of the other.[20] In the view of Imam Al-Shafii, capital contribution in commodities (i.e., other than in money) will be allowed if the commodity contributed falls in the category of *dhawat-ul amthal* (i.e., commodities which if destroy) can be compensated by similar commodity of same quality and quantity); but not allowed if it falls in the category of *dhawat-ul-qeemah* (i.e., commodities or properties which cannot be easily compensated by the similar commodities or properties).[21] On the part of Imam Malik, however, liquidity of capital contribution is not a requirement for Musharakah to be valid. Consequently, this school of law holds that the illiquid capital contribution can be evaluated according to the market price as at the date of the Musharakah contract.[22] The view of Imam Malik appears to be capable of accommodating the realities of the modern day businesses. This position validates a Musharakah arrangement between a bank and its clients who has only landed property to place as his capital contribution.[23]

Mixing of Capital

Another controversy is whether mixing of capital is required where illiquid assets are being used as share capital or part thereof. On this Shafii school of thought holds that for partnership to be possible, investment must be mixed before any business is conducted. The reasoning in this school of thought is that if the share capital ie not mixed, the investment will remain under the ownership of the contributor of the identified capital only and any profit or loss will be attributable to such original investor only. The trio of Hanafi, Malik and Hambali hold that mixing of capital is not important for the validity of *musharakah*.[24]

This issue of mixing of capital may arise in modern day import and export businesses, as exemplified by Dr. Muhammad's scenario[25]—

> If some companies or trading houses enter into partnership for setting up an industry to conduct businesses, they need to open LC (letter of credit) for importing the machinery. This LC reaches the importer through his bank. Now when machinery reaches the port and the importing companies need to pay for taking possession, the later need to show those receipts (evidence of the opened LC) in order to take possession of the goods. Under Shafii school of thought the imported goods cannot become the capital of investment but will remain in the ownership of the person opening the LC because at the time of opening the LC the capital has not been mixed[26] and without mixing capital, *musharakah* cannot come into existence.
>
> Under this situation, if the goods are lost during shipment, the burden of loss

20 See ibn Qudamah, *Al Mugni*, Muwaffaq al Din, Cairo, 1367H, V.5, 124 and 125, cited in M. Muslehuddin, *Banking & Islamic Law*, New Delhi, Adam Publishers & Distributors, 2007.

21 Muhammad Taqi Usmani, 40.

22 Muhammed Imran Ashraf Usmani, 99.

23 This position is particularly relevant in the use of diminishing *musharakah* by modern Islamic banks to finance housing projects.

24 Muhammed Imran Ashraf Usmani, 100.

25 *Ibid.*, 101.

26 Since the ordered machinery had not come yet in order to be part of the business.

> will fall upon the opener of the LC even though the goods were being imported for the entire industry. This is because even though a group of companies had asked for the machinery or imported goods the importers had not mixed their capital at the time of investment.

Going by the view of Hanafi, Maliki and Hambali schools, partnership (*musharakah*) comes into existence at the time of agreement and not upon mixing of capital. Consequently, in their view, *musharakah* transaction is valid even in the foregoing scenario. Therefore if the machinery had been destroyed in transit, the loss would be borne by both parties. This position is more practicable in dealing with modern day business complexity. If a contrary position is taken, it implies that the liquid capital contributed by the other partner must be tied down pending the arrival of the machinery in order to get mixed with it but this does not make business sense because any capital tied down may result into outright loss or in the loss of profit that would have accrued if the capital had been utilized.

Sharing of Profit and Loss

Although in *musharakah* financing, (like other Islamic finance modes) parties to the transaction both share in the profit or loss resulting therefrom, in the case of profit sharing, contract of *musharakah* is invalid if a lump sum profit is fixed for any of the parties to the transaction.[27] Similarly the rate of profit cannot be in proportion to the capital contributed for investment but is rather based on the actual profit.[28] In Islamic law, it is required that the ratio of profit for each of the parties (the bank and the client) must be agreed upon by the parties at the time of contract and not at the time of conclusion of the business, otherwise, contract of *musharakah* is not valid.

There is unanimity of opinion of scholars on the foregoing but what generates difference of opinion is whether the ratio of profit must be proportionate to the ratio of capital contributed. For example if a depositor partners a bank in *musharakah* and contributes 30% of the *musharakah* fund, must he be entitled to only 30 percent of the profit of the business and nothing more?

The opinion of Shafii and Maliki schools of thought on the foregoing scenario is that each party shares in the profit in the proportion of his capital contribution. However, in the opinion of Hambali[29] and Hanafi[30] schools, the ratio of profit may be different from the ratio of capital invested by each party as long as it is mutually agreed by the parties. The implication of this is that a depositor partner in *musharakah* who contributed only 30 per cent of capital may end up getting 60 percent of profit if it is agreed be-

27 Muhammad Taqi Usmani, 92.

28 The only exception being when a lump sum is agreed by parties as an initial disbursement to any party. In such a situation, it must be clearly stated in the agreement that it is subject to final settlement at the close of the business, when actual profit would have been known, and the initial on account payment gets adjusted to the actual profit accruing to the party. See Noraziah and Abdul Gafar, 154.

29 Muhammad Taqi Usmani, 37.

30 Abu Hanifah adds that if it is expressly stipulated in *musharakha* that a partner remains a sleeping partner, the share of such a partner cannot exceed the ratio of his capital contribution. For the Hanafi school, an active partner can get more than his capital contribution but a sleeping partner cannot get more than his capital contribution.

tween the parties in order to serve as an incentive to the depositor partner whose active involvement and participation led to the success of the business.

As regards sharing of loss, there is consensus of opinion of the jurists/scholars on the rule that each partner shares in the loss proportionate to the ratio of his capital contribution to investment. Consequently a partner who contributed 30 per cent of the fund suffers only 30 per cent of the loss.[31]

Financing by *Musharakah* instrument

Musharakah can be used to finance a wide range of capital requirements of a business. As mentioned earlier it can be employed for financing imports and exports and while *musharakah* can be used to finance a one off single transaction it can also come handy in financing of a business' working capital which may involve running a *musharakah* account on the daily products basis.

As regards single transaction financing, *musharakah* instrument is suitable for import financing if the letter of credit for such imports is opened with some margin.[32] In order to fulfill the requirements of Islamic finance, ownership of the imported goods must be with financier bank who must also have possession either directly or through its appointed agent.[33]

As regards the employment of the instrument of *musharakah* to finance the working capital of a running business, the legal position taken by Imam Malik on liquid and illiquid capital contribution may be useful as posited earlier.[34] On the basis of this legal position, the value of the business of the person seeking working capital finance constitutes his own capital contribution while the amount given by the financier bank to finance the working capital is the bank's capital contribution. Both parties may agree that the financier is not participating in the business which is agreed to run for a fixed period and they agree on the profit ratio as well which in the case of the financier bank, cannot exceed the percentage of its capital contribution.[35]

A more complicated scenario may play out in the case of *musharakah* finance of running capital for a big company with a large number of fixed assets. At the end of the short or medium term *musharakah*, while determining the profit, all expenses must be deducted. The problem however is in the area of evaluating the machineries' depreciation. The same machineries are used by the company for other concurrent businesses not subject to *musharakah* arrangement or used for businesses postdating the *musharakah* term. In both cases the whole cost of expenses on machineries cannot be attributed to the current *musharakah* transaction. What is done and is acceptable in law is one of two things. The parties may mutually agree that the *musharakah* portfolio will pay an agreed rent to the client company for the use of the Machineries or the parties

31 Muhammed Imran Ashraf Usmani, 94.

32 here the letter of credit has been opened without any margin, mudarabah will be suitable. See *ibid.*

33 This agent may also be the importer client of the bank. The client importer takes over the goods with a view to selling in the market. Where the goods are not sold upon the expiry of the term, the importer client may himself purchase the share of the financier.

34 That non-liquid assets can also form part of the capital on the basis of evaluation.

35 Although in the case of loss, both parties share in exactly the ratio of their investment.

may also agree that the ratio of profit of the client company be increased in order to take care of the depreciation of machineries.[36]

Effect of *Gharar* on *Musharakah*

The terminology *gharar* means to cause uncertainty, to tempt and to cheat. Just as *gharar* is one of the elements that in general terms vitiate an ordinary sale contract, it is equally an element capable of vitiating a *musharakah* contract between a bank and its client. This is to say that when any element of uncertainty occurs in a *musharakah* arrangement, it is invalid. *Gharar* in *musharakah* or *shirkatul amwal* must be examined in terms of capital contribution, duration of *musharakah* and profit accruable to parties. The rule is that to avoid vitiating of *musharakah* contract, parties must avoid uncertainty in the three areas identified above. In order words, there must be certainty of capital, certainty of period of contract and certainty of profit accruing to the parties.

In respect of certainty of capital, it is required that the total amount being invested must be specified. Such money cannot be in form of loan on third parties and *musharakah* parties must be in possession (whether in actual or in constructive form) as at the time of contract. Nevertheless, where capital contribution is a mixture of cash-in-hand assets, commercial goods,[37] as well as loan on others, it is permissible under the Maliki[38] school. The parties only need to assess and ascertain the value of the non-cash elements of the capital.

In respect of certainty of duration requirement, parties are not necessitated to specify in contract a definite time for *musharakah* transaction. This is based on the established principle of permissibility of *musharakah* partnership for an indefinite period of time. This is more appropriate in the case of the relationship between Islamic banks and their clients/depositors which relationship is a continuous one but can be terminated by the depositors at will. [39] Nevertheless, exigencies of modern-day business especially companies which are in law mandated to issue annual report showing detailed accounts and the shares of profits of the shareholders, would require that *musharakah* be terminated constructively at the end of a fiscal year to enable a proper and accurate preparation of such annual reports.

Moreover, it is permissible for the parties to stipulate a maximum period by the end of which the contract of *musharakah* partnership ceases to exist. It is equally permissible to stipulate the minimum time limit before which neither parties is allowed to terminate the contract in order to take care of situations where sudden withdrawal of a party may have dire consequences on the business of the other party(ies).

The third area of assessment of *gharar* in *musharakah* is certainty of profit. For *musharakah* agreement to be valid, the profit accruable to parties must be determined. It is required to be expressed proportionately in term of percentage of total profit at the time of contract. Profit cannot be expressed in lump sum since the actual profit is not

36 Muhammad Taqi Usmani, 68.

37 Maulana Ejaz Ahmad Samadani, *Islamic Banking and Uncertainty*, Karachi, Darul Ishaat, 1st Ed., 2007, 63.

38 Hanafi school permits the mixture of various forms of capital but does not permit using commercial goods as capital.

39 Notice of termination would be expected to be given where sudden termination may result in loss to others. See Maulana Ejaz, quoting Badai al Sanai. 6/77.

yet known at the time of contract. But parties are required to know the percentage of whatever total profits accruing at the end of the fiscal year.

Securitization of *Musharakah*

This is the art of transforming and representing the value of a *musharakah* business in certificates to enable the holder of such certificate enjoy collateral benefits other than the agreed proportion of profit due to the parties running the *musharakah* business. The process is that every subscriber is given a *musharakah* certificate which represents his proportionate ownership in the assets of the *musharakah* partnership. Such *musharakah* certificate can be traded (sold and bought) in the secondary market for any price agreed upon by the trading parties which may be more than the face value of the certificate.[40] *Musharakah* certificate represents the pro rata ownership of the holder in the assets of the *musharakah* business,[41] therefore what is being traded in the certificate is the assets value as represented in the certificate units. This explains why the portfolio of the *musharakah* is expected to be in non liquid form before the certificate can be traded at a profit.

Where there is difference of opinion, however, is what happens when the portfolio of *musharakah* business is composed of both liquid and non liquid assets.[42] Can the *musharakah* certificates of such a business or company be traded at a profit? Imam Shafii posited that such certificate cannot be sold at a profit unless both the liquid and non-liquid assets represented in the certificate units, are separable and can be sold independently. This position with due respect, will serve as a clog in the wheel of progress of most companies today as most modern day companies hold their portfolio in both non liquid assets and cash in hand and at bank. This perhaps accounts for why majority of scholars today relax the rule by holding that it is permissible to trade, if the non-liquid part of the mixed portfolio is more than 50 percent of the total assets of the *musharakah* portfolio.[43]

It is obvious that the so-called modern-day scholars' position also cannot accommodate the operational structures of most businesses. For example, a new Islamic Bank which capitalization requirement is N10 billion. If the value of its initial deposits from customers is N4 billion and the total value of its initial branches, including machineries, is N3 billion. The implication is that such a bank, going by the view of such scholars, cannot float *musharakah* securitization to enable stakeholders profitability deal in its certificates. In dealing with the modern trend, adopting the legal opinion of Hanafi school is highly helpful. The Hanafi school holds that where there is combination of liquid and non-liquid assets, it is permissible to trade in the share certificate of such a company at a profit as the profit accruing therefrom will be deemed as resulting from the non-liquid part of the assets of the business represented in the *musharakah* certifi-

40 The condition, however, is that the certificate can only be sold above the unit value of the *musharakah* certificate (at a profit), if the assets of the *musharakah* partnership is no longer in liquid (cash) form; if it is still in liquid form, trading in its certificates can only be done at par value since buying and selling certificates in that state is tantamount to exchanging money (same currency), and any profit or excess on such trading is tantamount to taking interest (*riba*).

41 See Muhammad Taqi Usmani, 58.

42 Non-liquid assets such as machineries, furniture, buildings, land and raw materials.

43 See Mohammed Taqi Usmani, 61.

cate while the liquid part of the company's asset's value represented in the certificate unit is taken to have been bought and sold at per value or face value of the *musharakah* certificate.

Misgivings about Choice of *Musharakah* Financing

There are a number of misgivings usually expressed by both financiers and the clients sourcing fund for their businesses. These misgivings which border on a number of factors which include trust, risk factor, and confidentiality of business secrecy often time constitute important determinants in the choice or otherwise of *musharakah* as a model of financing projects. Due to the *musharakah* requirement of banks' participation in the client's business, fear is often expressed on the part of the clients that making the financier institution a partner in business exposes them to the risk of disclosure of the secrets of the business to third parties through the financier which gets to know the secrete through participation.

Contrary to this notion, however, the fear of possible breach of confidence is allayed by the fact that *musharakah* rule as stated earlier permits the parties to agree on the extent of participation of the financier in the *musharakah* business. In fact the partners may agree on the condition that the management shall be carried out by one of them and no other partner shall work for the *musharakah*.[44] Even where both parties are participating, a non-disclosure clause may be inserted in the agreement to bind the financier to maintain secrecy over the business secrets of the client and the breach of such agreement will be actionable to the extent of the injury suffered as a result.

Secondly, it has also been mooted that dishonest clients in *musharakah* transaction may fraudulently claim to have suffered a loss or to have made no profit at all. Scholars have suggested that this apprehension can be dispelled if a well designed system of auditing is implemented in a way that the accounts of *musharakah* clients are fully maintained and properly controlled.[45] In addition to this, various checks are usually built into the process depending on the nature of financing for which the *musharakah* instrument is being deployed. In financing export for instance, the client/exporter has an order from abroad. Payments are secured by a letter of credit and are made through the financier bank. This process automatically forestalls any possible concealment of profits made by *musharakah* business.

Thirdly, there is the misconception that the financier banks and the depositors are more prone to the risk of lack of profit or outright loss resulting from the possible failure of *musharakah* business. Really, the issue of loss resulting from a whole *musharakah* merely lies in the realm of hypothetical possibility and conjecture. The reason is that *musharakah* portfolio will scarcely suffer loss for many reasons. First, in going into *musharakah* business, Islamic banks carry out in depth the feasibility study in respect of the proposed businesses for which funds are required. Therefore the potentials of *musharakah* businesses are usually well determined in advance. Moreover, Islamic banks often engage in diversified portfolio of *musharakah* such that any possible loss in

44 *Ibid.*, 42. However, the implication is that the sleeping partner is entitled to the profit only to the extent of the ratio of his investment.

45 *Ibid.*

one *musharakah* is compensated adequately by the profits accruing from other *musharakah* portfolios. It is the idea of separation of financing from trading which engenders the notion that bank after advancing loans are no longer concerned with the results emerging from the business activities.[46]

An Islamic bank being a partner in *musharakah* business is much concerned about the actual result of the trade and industry activities since the bank is sharing from the profit or loss of the business. This position and attitude of the partners often time contribute to the usual success of *musharakah* business.

Conclusion

This work has extensively examined musharakah concept, known as profit and loss sharing partnership, as one of the permissible methods of Islamic financing. Being an instrument of financing where profits and losses are shared by both parties to the business in equitable proportion, it is an ideal alternative to the interest based financing of the conventional financial institutions.

For *musharakah* contract to be valid all elements of a valid contract of ordinary sale must be met in addition to which special conditions peculiar to *musharakah* instrument must also be met. One of the special conditions is that both the financier bank and the trading customer must contribute their own part of the capital for the business; second is that both parties participate in the management of the business, the subject matter of *musharakah* except it is otherwise agreed by both parties; third is that the ratio of the profit accruable to both parties to *musharakah* finance transaction must be determined at the time of contract; fourth is that *musharakah* business must not be tainted by an element of *gharar* (uncertainty) either in term of capital identification, or certainty of proportion of profit or duration of *musharakah*.

A number of issues arising from *musharakah* application are controversial. One of such issues is whether capital contribution can be in forms other than money. This issue seems to have been settled in line with modern day business requirement by the view of Imam Malik which posited that capital contribution can be in illiquid form by way of evaluation of the asset contributed in line with the market price as at the date of the contract. Another controversial issue is what happens if the portfolio of *musharakah* business comprises both liquid and illiquid assets? Can the *musharakah* certificate of such a company be traded at a profit? Hanafi's legal opinion seems to have settled this in favor of modern-day businesses' operational structures by holding it permissible to trade profitably in such a *musharakah* certificate. The profit accruing from such trading in certificate is deemed as resulting from the non-liquid part of the assets of the business represented in the *musharakah* certificate.

There are some misgivings expressed in some quarters which are capable of militating against using *musharakah* instrument as a mode of finance such issues as lack of trust by parties, dishonesty on the part of customer/partner in respect of disclosure of profit and the tendency to pass the risk of loss on the financier bank and the depositors were highlighted in this work for consideration. However, the highlighted misgiv-

46 This is the case with conventional banks and their customers, but the contrary is the case in Islamic banking and finance.

ings were considered misplaced in the sense that a number of safety valves are built into *musharakah* process by the law, as well as practice procedures, as to be capable of allaying the fears of the parties to *musharakah* transaction, which still remains an ideal instrument of Islamic financing by Islamic banks.