100103 - He is investing someone else’s wealth and will bear half of the losses

the question

A man is investing someone else’s wealth. If he makes money, is it permissible for him to give the investors 80% of the profit and keep the rest as a fee, but in the event of a loss, 50% will be borne by each party? If it is not permissible, what is the shar’i way of doing it?.

Detailed answer

Praise be to Allah.

Firstly:

The one who invests the wealth of others either takes part by means of his work only, so that the money belongs entirely to someone else, or he takes part by means of his work and his wealth. The former is called a mudaarabah transaction, in which the profits are shared according to whatever he has agreed upon with the owners of the money. It may be 20% or more or less, but the rate must be stipulated in the mudaarabah contract.

As for losses, he does not bear any of them; the losses are borne entirely by the owner of the capital, and the worker loses his work and effort, unless the loss is due to some shortcoming or transgression on the part of the worker, in which case he has to bear the loss.

If it is stipulated in the mudaarabah contract that any loss or part of it – such as 50% - is to be borne by the worker, then this condition is invalid and there is a difference of scholarly opinion as to whether the contract itself is valid or invalid.

Secondly:

If you are contributing both your wealth and your work, then the profits are to be shared according to the agreement, as stated above.

As for losses, they are to be borne according to the capital invested. If you put in one-tenth of the capital, for example, then you must bear one-tenth of the loss; if you put in one half of the capital, then you must bear one half of the loss, and so on.

Among the comments of the scholars about the worker in a mudaarabah contract not having to bear any financial loss, and the partners bearing losses according to their shares are the following:

Ibn Qudaamah (may Allaah have mercy on him) said in al-Mughni (5/22): The loss is to be borne by each partner according to his share of the wealth; if the shares (of two partners) were equal then they each bear half of the loss. If there were three shares then they each bear one third of the loss. We do not know of any difference of scholarly opinion concerning this matter, and it is the view of Abu Haneefah, al-Shaafa'i and others.

The loss in a mudaarabah contract affects the (invested) money only, and the worker does not bear any loss, because the loss affects the capital, which has to do with the owner of that capital, and the worker has nothing to do with it, so the loss affects the investor's wealth only; but they share any growth that takes place. End quote.

He also said: If it is stipulated that the worker is liable for the money or for part of any loss, this condition is invalid, and we do not know of any dissenting opinion, but the contract is still valid. This was stated by Ahmad and it was the view of Abu Haneefah and Maalik.

It was narrated from Ahmad that the contract is invalidated thereby, and this was narrated from al-Shaafa'i, because it is an invalid condition which invalidates the mudaarabah contract. But the former view is more correct.

End quote from al-Mughni (5/40).

And Allaah knows best.