150113 - Guidelines on dealing with a diminishing-share partnership

the question

I am building one house and an attached flat right now.
I am looking at doing a partnership where I get someone to help me cover the cost of the flat and we split the rental income according to what each person owns as a percentage. We will share all costs/profit/losses during the term of the partnership.
The amount the flat will cost is 70 000. I am after a contribution of 50 000 from my partner.
I want to also pay them each month to buy a greater share of the flat until I own all of it. They will continue to receive rent based on their percentage of ownership until I have purchased all of their share and they no longer own any share on do not receive any income.
The agreement will be written down and witnessed according to the sharia.
I dont have enough money to finish this project and do not want to go to the islamic bank because the sheiks in Australia differ on whether they are halal.
Please help because I want to avoid the haram.

Detailed answer

Praise be to Allah.

There is nothing wrong with the transaction mentioned, which is called a diminishing-share partnership. The guidelines thereon are as follows:

~1~

That you agree with a partner to put your shares of the funds into building the flat, and the profit – namely the returns from rent – should be shared out in accordance with whatever you have agreed upon, and any loss should be proportionate to the amount of money invested by each partner. So if construction will cost 70,000, it is permissible to agree that he will pay 50,000 and you will pay 20,000; then the distribution of the profits (rent) will be according to whatever you

have agreed upon, whether it is equal shares or less or more. But any loss – if it occurs – should be proportionate to the amount of money that each of you put in.

~2~

That you agree that when construction is completed, you will buy his share of the flat in portions, such as if you divide his share into five portions for example, and you buy one portion each month, and his share of the rent diminishes accordingly. So when you have bought the first portion, his share of the rent will decrease by one fifth, then when you have bought the second portion, his share of the rent will decrease by two fifths. It is also permissible to leave his share of the rent as it is, as was mentioned in al-Ma‘aayeer ash-Shar‘iyyah (p. 207)

~3~

That there should be a binding promise from one of you in which he pledges to buy or sell the portions of his partner gradually, and the other party will have the option of accepting or rejecting that. It is not permissible for this promise to be binding on both parties, because it comes under the rulings on transactions (buying and selling), and it is not permissible to engage in a transaction (sale) that is to happen in the future, just as it is not permissible to stipulate the condition of sale at the time of drawing up the partnership contract.

~4~

The new sale contract should be drawn up at the time of the sale of each portion. If the contract is verbal only, the purchaser must express his wish to buy (the proposal) and the seller responds by agreeing (acceptance).

~5~

That selling should be done on the basis of the market price at the time of the sale, not on the basis of the value of the apartment at the time of drawing up the partnership contract. This means that if a loss is incurred and the price of the flat drops, both parties bear the loss according to their shares. It is not permissible to make a promise to buy the shares based on their value at the

beginning of the project, because that is like offering a guarantee for the share of the partner, which is not allowed.

It says in a statement of the International Fiqh Council, which was issued during its fifteenth session in Muscat (Sultanate of Oman) 14-19 Muharram 1425 AH/6-11 March 2004 CE, with regard to diminishing-share partnerships and the shar'i guidelines thereon:

~1~

The diminishing-share partnership is a new type of transaction. What it involves is a partnership between two parties in a project that brings an income, in which one party pledges to buy the share of the other party gradually, whether the purchase is done with income acquired by the purchaser from this project or from any other source.

~2~

The basis of the diminishing-share partnership is the contract that is drawn up by the two parties, in which each of them contributes a portion of the capital of the partnership, whether his contribution is in the form of cash or materials, after evaluation of the materials, with a stipulation of how the profits are to be shared, on condition that both parties will bear losses – if incurred – each according to his share in the partnership.

~3~

What makes the diminishing-share partnership different is the promise clause, which is a binding promise from one partner only to buy the share of the other, provided that the other party has the choice. That is done by making a new transaction contract every time the purchaser wants to buy a portion of the other party's share, even if that is done verbally by means of proposal and acceptance.

~4~

It is permissible for one of the two parties to rent the share of the other party, according to set

fees and for a specific period. Both parties remain responsible for basic maintenance, commensurate with each party’s share.

~5~

The diminishing-share partnership is Islamically acceptable if it is done within the general guidelines on partnerships and if the following guidelines are adhered to:

a.Neither party should be committed to buying the share of the other party on the basis of the value of the shares at the time of forming the partnership, because that comes under the heading of one partner guaranteeing the share of the other partner. Rather the price of selling the shares should be decided by the market value at the time of the transaction, or on the basis of what they agreed at the time of the transaction.

b.There should be no stipulation that one party will be responsible for insurance, maintenance and other expenses; rather these expenses are to be covered by the partnership, each according to his shares.

c.The profit share of each party is to be defined in terms of a percentage. It is not permissible to stipulate a specific sum from the profits or a percentage of the money invested.

d.The partnership contract is to be kept separate from financial commitments connected to the partnership.

e.It is not allowed to state that one of the two parties has the right to withdraw what he offered of finance.

End quote from Qaraaraat wa Tawsiyaat Majma‘ al-Fiqh al-Islami

In al-Ma‘aayeer ash-Shar‘iyyah (p. 206) it says:

It is essential that the partnership contract should not stipulate any condition of buying or selling. Rather the partner may give a separate promise to that effect, that is not part of the partnership contract. Similarly, buying and selling should be done on the basis of a separate contract that is

not connected to the partnership contract. It is not permissible to include one of these contracts in the other. End quote.

If these guidelines are followed, then there is nothing wrong with this transaction.

And Allah knows best.