

## **The Development of Partnership Based Structure In Comparison To the Concept of Mushārah (Sharikah) with Special Reference to Malaysia.**

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### **Abstract**

In Malaysia, most of the businesses are micro, small and medium. According to the SME Annual Report 2010/2011, the latest statistics indicate that SMEs constitute 99.2% of the total business establishments and contribute about 32% of GDP and 59% of total employment. In carrying out the SMEs, the option of business vehicles which are available in Malaysia is only the conventional business structure, namely, sole proprietorships, partnerships and company. For the micro, small and medium businesses, the company structure is observed not to be appropriate due to its formal and highly regulated business structure. As such, most of the SMEs are carried out in the form of sole proprietorships and partnerships. This can be seen from the statistics published by Companies Commission of Malaysia which provides that there are 4,660,067 sole proprietorships and partnerships registered compared to only 970,396 of companies being registered. The tax scheme is also another discouraging factor which makes the partnership as a better option for SMEs. In certain sectors, particularly the professionals, for example, lawyers and accountants, the business can only be carried out in the form of sole proprietorships or partnerships. This article intends to highlight the development of partnership based structure in Malaysia and compare it with Islamic version of partnerships structure (Sharikah).

### **Abstrak**

Di Malaysia, kebanyakan perniagaan adalah mikro, kecil dan sederhana. Menurut laporan tahunan PKS 2010/2011, statistik terkini menunjukkan bahawa PKS membentuk 99.2% daripada jumlah seluruh pertubuhan perniagaan dan menyumbang kira-kira 32% kepada KDNK dan 59% daripada seluruh jumlah pekerjaan. Dalam menjalankan PKS, pilihan jenis perniagaan yang terdapat di Malaysia hanyalah struktur perniagaan konvensional, iaitu milikan tunggal, perkongsian dan syarikat. Bagi perniagaan mikro, kecil dan sederhana, struktur syarikat didapati tidak sesuai kerana struktur perniagaannya adalah formal dan sangat terkawal. Sehubungan itu, kebanyakan PKS dijalankan dalam bentuk milikan tunggal dan perkongsian. Ini dapat dilihat dari statistik yang diterbitkan oleh Suruhanjaya Syarikat Malaysia (SSM) yang memperuntukkan bahawa terdapat 4,660,067 milikan tunggal dan perkongsian yang didaftarkan berbanding dengan hanya 970,396 syarikat yang didaftarkan. Skim cukai juga adalah satu faktor yang tidak digalakkan yang menjadikan perkongsian itu pilihan yang lebih baik untuk PKS. Dalam sektor-sektor tertentu, terutamanya golongan profesional, contohnya seperti peguam atau akauntan, perniagaan itu hanya boleh

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dijalankan dalam bentuk milikan tunggal atau perkongsian. Artikel ini bertujuan untuk menonjolkan pembangunan struktur berasaskan perkongsian di Malaysia dan membandingkannya dengan versi struktur perkongsian Islam (Sharikah)

### **Introduction**

Partnerships structure has long been accepted as one of the major venture capital vehicles. It is generally opted by small and medium businesses and by the professionals who are not allowed by their respective regulatory bodies to incorporate. With the development of the economy, the general partnership structure was found to be no longer suitable for some of the businesses, particularly the professionals. The rising cost in trade and litigation has forced partners to take precaution in regard to liabilities in the business. These lead to development in partnerships structure to limited partnership (LP) and limited liability partnerships (LLP). In the United States of America, the partnership structure has undergone more rapid evolution to include master limited partnership and family limited partnership. In Singapore, LP and LLP had also been introduced. In Malaysia, the Companies Commission of Malaysia (CCM) had published two consultation documents on Limited Liability Partnerships (LLP) in 2003 and in 2008 respectively. The draft LLP Act has also been tabled in the 2011 Parliamentary session and expected to be enforced in 2012. The CCM initiatives marked a major step towards development in Malaysian business laws after 54 years of independence. In Labuan, the Malaysian offshore, there is also a development in business laws when the Labuan Limited and Limited Liability Partnerships Act 2010 was passed to enable LP and LLP to be registered in Labuan. This article intends to highlight the development of partnership based structure in Malaysia and compare it with Islamic version of partnerships structure (Sharikah).

### **Partnership as a Business Structure**

A partnership structure is a business owned by two or more people.<sup>1</sup> It is basically a business arrangement between two or more persons to carry out similar nature of business with the agreement that the net profits shall be shared among them.<sup>2</sup> A partnership is not a legal

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<sup>1</sup> For trading partnership the maximum number of partners which is allowed by the law is 20 person; section 47(2) of Partnerships (Malaysia) Act 1961

<sup>2</sup> Section 3(1) Partnerships (Malaysia) Act 1961,

entity.<sup>3</sup> As such, the partners and the business are not distinct from one another. In fact, the firm actually represents all partners collectively.<sup>4</sup> Any action against or by the firm constitutes as action of all the partners.<sup>5</sup> Partners in a partnership are jointly liable for debts of the business mainly because they are not separated from the firm. Debts incurred by the firm in the due course of business are treated as debts of all partners and their extent of liabilities in the firm are extended to their personal assets. Creditors or third parties dealing with the firm could claim their debts against the personal property of the partners in the event that the partnership assets are not sufficient to settle all debts.<sup>6</sup>

A partnership is not a tax entity under the Income Tax Act 1967 and as such no tax is imposed on the firm.<sup>7</sup> Each partner is treated as if he was a sole proprietor and assessed in accordance with his share of the partnership income.<sup>8</sup>

### **The Development of Partnership Based Business Vehicles**

It is observed that the development of partnership based business vehicles mainly concentrates on the aspect of limited liability amidst the criticism of the unlimited and joint liability principle.<sup>9</sup> From merely the traditional form (general partnerships), the structure has been expanded to include limited partnerships and limited liability partnerships (LLP).

A limited partnership differs from a general partnership in the role and responsibilities of the partners. Limited partnerships comprise the

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<sup>3</sup> Although in some countries, partnerships are regarded as a legal entity, for example, in Scotland. See section 4(2) of Partnerships Act (UK) 1890. See David Bennett, *An Introduction to the Law of Partnership in Scotland*, Sweet & Maxwell, Edinburgh, 1995

<sup>4</sup> Section 6 of Partnerships (Malaysia) Act 1961.

<sup>5</sup> Section 7 and 11 of Partnerships (Malaysia) Act 1961.

<sup>6</sup> (Reference missing)

<sup>7</sup> Goh Chen Chuan, *Guide to Malaysian Business Taxation*, Leeds Publication, Kuala Lumpur, 1996 at 43.

<sup>8</sup> Income Tax Act 1967; section 55(1)

<sup>9</sup> See URN 94/529 Diana Faber (1997), *The Law Commission Review Of the Law of Partnership*, *Butterworths Journal of International Banking and Financial Law*, June, p 242 and Joanna Gray (1997), *DTI Consults On Limited Liability Partnerships*, *The Company Lawyer*, *Butterworths Journal of International Banking and Financial Law*, June, p. 242.

general and limited partner.<sup>10</sup> The general partner controls the limited partnership's day-to-day operations and is personally liable for business debts.<sup>11</sup> Limited partners on the other hand, have minimal control over daily business decisions or operations and in return, they are not personally liable for business debts or claims.<sup>12</sup>

Another fascinating structure which is said to be an extension of partnership structure is limited liability partnerships (LLP).<sup>13</sup> However, LLP is not a very accurate partnership structure, as it is actually a hybrid creature of a company and a partnership. It has a separate legal entity and therefore enjoys most of the attributes of a company such as limited liability, right to own property and right to take legal action. The external obligations of LLP are also similar to requirements applicable to companies such as audit and disclosure requirements. However, as regards its internal regulation, LLP has the flexibility of a partnership, as the members are given the right to decide through the members' agreement.

Despite the similarities in the external and internal regulations, there are three types of LLP. The first type of LLP has the status of a partnership such as the United States of America LLP.<sup>14</sup> The second type is the LLP which is a legal entity but not a body corporate such as the Jersey LLPs.<sup>15</sup> Whereas the third type of LLP has the status of a body corporate such as the Singapore LLP<sup>16</sup> and the UK LLP<sup>17</sup>.

From the aspect of taxation, both limited partnership and most LLPs work like a general partnership in that it is a pass through operation with profits passing through to the partners or members who then include their allocated income on their personal tax returns.

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<sup>10</sup> Terence Prime and Gary Scanlan. (1995). *The Law of Partnership*. Butterworths. London, p 342..

<sup>11</sup> For example under the Limited Partnership Act (UK) 1907; s4 (2), Labuan Offshore Limited Partnerships Act 1977; s 9(1).

<sup>12</sup> Limited Partnership Act (UK) 1907; s 6(1). In Labuan Offshore Limited Partnerships Act 1977; s 11 provides the rights which limited partners have which did not include right in management.

<sup>13</sup> For UK LLP, see <http://www.companieshouse.gov.uk/infoAndGuide/llp.shtml> for detail information on LLP.

<sup>14</sup> See Chapter 614 Uniform Partnership Act; Limited Liability Partnerships.

<sup>15</sup> Article 2(4) Jersey Limited Liability Partnerships Law 1997 (Rev 2008)

<sup>16</sup> Section 4(1) of Limited Liability Partnerships (Singapore) Act 2005

<sup>17</sup> Section 1(3) of Limited Liability Partnerships Act (UK) 2000.

### **The Development of Partnership Related Business Vehicles in Malaysia.**

In Malaysia the initiative to expand the option of business entities was made by the Companies Commission of Malaysia (CCM) under its Corporate Law Reform Program. To ensure that the reform program will be conducted effectively and objectively, CCM has established a committee called the Corporate Law Reform Committee (CLRC) pursuant to sections 17 and 19 of the Companies Commission of Malaysia Act 2001.<sup>18</sup> One of the terms of reference of the CLRC is to consider whether the existing legal forms of business vehicles i.e. the partnership and the corporate forms are able to provide alternative and adequate choice of establishing legal forms of business entities. This objective was executed by the CLRC by establishing Working Group A.<sup>19</sup> One of the outcomes of the CLRC's efforts is the 2003 consultative document (CD) for an alternative business vehicle for small businesses and venture capital arrangements.<sup>20</sup> The second consultative document was issued in April 2008.<sup>21</sup> The main objective of both consultative documents is to gather responses from the public, business community, financial institutions, academicians, and practitioners, as regards the proposed structure of Malaysia's own limited liability partnerships. Pursuant to the feedback received from public consultations in 2003 and 2008, CCM published the discussion draft bill of LLP in March 2009. The draft LLP Act now waits for its reading at the Senate which is scheduled for the 2011 Parliamentary session.<sup>22</sup>

#### **Limited Partnerships (LP) in Malaysia**

In Malaysia, LP is only available in Labuan. Under the Labuan Limited Partnerships and Limited Liability Partnerships Act 2010 (LLP and LLPA 2010), a limited partnership must be formally registered with Labuan Financial Services Authority (LFSA).<sup>23</sup> LFSA shall not register

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<sup>18</sup> Retrieved from <http://www.ssm.com.my/clrc/clrc.html> on 2 August 2011.

<sup>19</sup> Ibid.

<sup>20</sup> SSM Consultative Document on Limited Liability Partnerships, April 2008 at p 6

<sup>21</sup> Ibid.

<sup>22</sup> Retrieved from Official Website of the Parliament of Malaysia at <http://www.parlimen.gov.my/index.php?modload=document&uweb=dr&doc=bills&lang=en> on 2 August 2011.

<sup>23</sup> LLP and LLPA 2010; s 5(1)

an offshore limited partnership unless a partnership agreement which is duly executed has been submitted to the authority.<sup>24</sup>

Similar to the English LP, the Labuan LP requires a composition of two types of partners, i.e. general partners and limited partners.<sup>25</sup> A general partner essentially has all the rights and powers and shall be subject to all the restrictions and liabilities similar to a partner in general partnerships<sup>26</sup> but despite the vast authority given to them, general partners cannot act without the written consent or ratification by all limited partners, in certain matters.<sup>27</sup> As for the limited partners, the Act clearly stated that they have no management rights and if they participated in the management of the firm, limited partners will lose their status as limited partners and become general partners.<sup>28</sup> Nonetheless, the limited partners have all the rights in the partnerships books and true account of the business affairs.<sup>29</sup> Limited partners also can lend or borrow money from the firm and enter into transactions with the firm.<sup>30</sup> In such cases, except where the limited partner is also a general partner, the limited partners claim against the assets of the offshore limited partnership shall rank them as creditors of the firm.<sup>31</sup>

In the Labuan LP, the general partners have unlimited liability towards the business debts similar to partners in general partnerships. On the other hand the limited partners shall not be liable for the debts or obligations of the offshore limited partnership<sup>32</sup> provided that they have fully paid their contribution as specified in the partnerships agreement.<sup>33</sup>

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<sup>24</sup> LLP and LLPA 2010; s 5(2)(a)-(f)

<sup>25</sup> LLP and LLPA; section 4(2)

<sup>26</sup> LLP and LLPA; section 11(1)

<sup>27</sup> LLP and LLPA; section 11(1)

<sup>28</sup> LLP and LLPA; section 19(3)

<sup>29</sup> LLP and LLPA; section 13(1):A limited partner has the same right as a general partner-

(a) during business hours, to inspect and make copies of or take extracts from the offshore limited partnership books, documents and records; and

(b) to be given, on demand, true and full information of all things affecting the offshore limited partnership and to be given a formal account of partnership affairs whenever circumstances render it just and reasonable.

<sup>30</sup> LLP and LLPA; section 15(1)

<sup>31</sup> LLP and LLPA 2010; section 15(2)

<sup>32</sup> LLP and LLPA 2010; section 19(1)

<sup>33</sup> LLP and LLPA 2010; section 18: A limited partner shall be liable to the offshore limited partnership for the difference, if any, between the value of money or other property contributed by him to the offshore limited

The Act also clearly provides that if limited partners participate in the management of the firm, they will lose their limited liability shield and become liable as general partners.<sup>34</sup>

The internal regulation of limited partnerships is generally similar to general partnerships except for the composition of partners. As the general partners in LP have similar rights and terms as partners in the general partnerships, the LLP and LLPA 2010 does not specify any provision to regulate internal relations between the general partners.<sup>35</sup> On the other hand, the Act clearly provides for relation between the limited partners inter-se.<sup>36</sup>

In 2002, when the Labuan Offshore Business Activities Tax Act (LOBATA) 1990 was amended, the Labuan limited partnerships was included in the definition of offshore companies and as such has a tax status as company.<sup>37</sup> However, with the amendment of Labuan Business Activities Tax Act 1990 in 2010, Labuan limited partnerships is

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partnership or the statutory value and the value of money or other property specified in the records kept under subsection 9(5) to be contributed by him to the offshore limited partnership.

<sup>34</sup> LLP and LLPA 2010; section 19(2); A limited partner shall not be liable as a general partner unless the limited partner participates in the management of the offshore limited partnership.(3) Subject to subsection (4), if a limited partner participates in the management of the offshore limited partnership in its dealings with persons who are not partners, that limited partner shall be liable in the event of the insolvency of the offshore limited partnership for all debts and obligations of the offshore limited partnership incurred during the period that the limited partner participated in the management of the offshore limited partnership as though the limited partner were for that period a general partner.

(4) A limited partner shall be liable under subsection (3) only to a person who transacted partnership with actual knowledge of the participation of the limited partner in the management of the offshore limited partnership and who then reasonably believed the limited partner to be a general partner.

<sup>35</sup> In absence of specific statute on Labuan Partnerships Act, reference on relation between general partners

Inter-se should be made to the Partnership Act (Malaysia) 1961.

<sup>36</sup> LLP and LLPA 2010; section 16(1) Subject to subsection (2), limited partners, in relation to one another, shall rank - (a) *pari passu* in respect of the return of their contributions; and (b) *pro rata* to those contributions in respect of profits.(2) Where there is more than one limited partner, the partnership agreement may provide that one or more of the limited partners is to have greater rights than the other limited partners as to -(a) the return of contributions;(b) profits; or (c) any other matter.

<sup>37</sup> Retrieved from <http://www.lofsa.gov.my/lofsa5/PubAnnSpe/ar/ar2002.pdf> on 25 January 2007.

categorized as Labuan entity<sup>38</sup> and therefore shall be the person assessable and chargeable to tax under the Act.<sup>39</sup> In Labuan, tax shall be charged at the rate of three per cent for a year of assessment upon the chargeable profits of a Labuan entity carrying on a trading activity for the basis period for that year of assessment<sup>40</sup> whilst a Labuan entity carrying on non-trading activity for the basis period for a year of assessment shall not be charged to tax for that year of assessment<sup>41</sup>.

### **Limited Liability Partnerships (LLP)**

LLP is a business structure that combines the best features of partnerships and company. It enjoys all the attributes of a body corporate, namely, separate legal entity, limited liability, perpetual succession and legal entity but at the same time retaining the internal flexibility of a partnership.

There are three types of LLPs: the first one is LLP with the status of a legal person but not a body corporate; the second one is LLP with the status of a body corporate: and the third one is LLP with the status of a partnership.

### **The Jersey LLPs.**

The Limited Liability Partnerships (Jersey) Law was enacted in 1997 and revised in 2008. The Jersey LLP has a separate legal entity, distinct from its partners although it is not a body corporate.<sup>42</sup> Due to its separate legal entity, Jersey LLPs shall be liable for any debt or loss of the business.<sup>43</sup> A partner or former partner in a limited liability partnership shall not be liable for any debt or loss of the business.<sup>44</sup> Any

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<sup>38</sup> Labuan Business Activities Tax Act (LBATA)1990; Schedule Section 2B. Under section 11 of LBATA 1990, **11.** A Labuan entity shall (a) at the time of filing of the statutory declaration and return of its profits for a year of assessment under section 5, make full payment on account of (i) tax to be charged for that year of assessment; or (ii) tax to be charged for that year of assessment after reduction of rebate under section 8A; or (b) at the time of filing of the statutory declaration under section 7 or 8, make full payment of (i) the tax charged for that year of assessment; or (ii) the tax charged for that year of assessment after reduction of rebate under section 8A.

<sup>39</sup> LBATA 1990; section 15

<sup>40</sup> LBATA 1990; section 4(1)

<sup>41</sup> LBATA 1990; section 9

<sup>42</sup> Article 2(4) of the Limited Liability Partnership (Jersey) Law 1997 (rev 2008)

<sup>43</sup> Article 4(1) of Limited Liability Partnership (Jersey) Law 1997 (rev 2008)

<sup>44</sup> Article 5(1) ) of Limited Liability Partnership (Jersey) Law 1997(rev 2008)



change due to admission, retirement or death of a partner does not affect the existence, rights or liabilities of the LLP.<sup>45</sup> Despite its legal entity, the internal regulations of Jersey LLPS Act are determined by the partnership agreement.<sup>46</sup> However, different from general partnerships, partners in the LLPs are agent to the LLP<sup>47</sup> and not to other partners.<sup>48</sup>

### **The Body Corporate LLP**

The second type of LLP is the LLP with a body corporate status. Examples of this LLP are the UK and Singapore's LLPs. An interesting feature of the second LLP is that although it has the status of a body corporate<sup>49</sup>; its internal regulation is via partners' agreement, which is akin to a partnership agreement.<sup>50</sup> This means partners of LLP may adopt any forms of internal arrangement, which they prefer. Nonetheless, when it comes to external obligations, LLP is subjected to similar requirements applicable to companies such as reporting and disclosure requirements.<sup>51</sup>

One important principle to be highlighted is that despite adopting the internal regulation, which is similar to a partnership, the UK LLP Act 2000 and the Singapore LLP Act 2005 clearly provides that the partnership law is not applicable to the LLP<sup>52</sup> whilst the company law is expressly (unless otherwise provided) applicable to the LLP.<sup>53</sup>

Another interesting feature of the incorporated LLP is its tax status. Although it has the status of a body corporate and subjected to the company law, the LLP is treated as a partnership for tax purposes.<sup>54</sup>

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<sup>45</sup> Article 2(4)(b) of Limited Liability Partnership (Jersey) Law 1997(rev 2008)

<sup>46</sup> Article 11(1) of Limited Liability Partnership (Jersey) Law 1997(rev 2008)

<sup>47</sup> Article 15(2) of Limited Liability Partnership (Jersey) Law 1997(rev 2008)

<sup>48</sup> Article 15(1) of Limited Liability Partnership (Jersey) Law 1997(rev 2008)

<sup>49</sup> Limited Liability Partnerships (UK) Act 2000; section 1(3) and Limited Liability Partnerships (Singapore) Act 2005; section 4(1).

<sup>50</sup> Limited Liability Partnerships (UK) Act 2000; section 6 and Limited Liability Partnerships (Singapore) Act 2005; section 10(1) and (2).

<sup>51</sup> Limited Liability Partnerships (UK) Act 2000; In Singapore, the LLPs are only required to submit annual insolvency/solvency report but there is no obligation to lodge the audited account report to the Registrar; Limited Liability Partnerships (Singapore) Act 2005; section 24 and section 25.

<sup>52</sup> Limited Liability Partnerships (UK) Act 2000; section 1(5) and Limited Liability Partnerships (Singapore) Act 2004; section 6.

<sup>53</sup> Limited Liability Partnerships (UK) Act 2000; section 1(3) and Limited Liability Partnerships (Singapore) Act 2004; section 8.

<sup>54</sup> Limited Liability Partnerships (UK) Act 2000; section 10(1) and Income and Corporation Taxes Act 1988; section 118ZA. See also Linda L.Ng, Singapore LLP: A

### **LLP with Partnership Status**

This type of LLP is available in the United States of America. The LLP is clearly treated as partnership as regards to its legal status and tax status. However, despite its status as partnership, the law recognized the LLP as a legal entity. This enabled the LLP to limit the liability of its partners and lives independently from its partners.

### **5.0 Differences between LLP and a Partnership**

The main difference between the LLP and a partnership is that in both types of LLP, the members or partners are not personally liable for the business debts and liabilities. Creditors of the LLP cannot go after the members' or partners' personal assets to pay off the LLP's debts. In a partnership structure, all partners have unlimited liability for the business debts to the extent that their personal assets could be claimed by the creditors if the business assets are not sufficient to pay the creditors.

It is also important to highlight that in a partnership, all partners are liable, jointly with all the other partners and also for all acts of the firm done while he is a partner. But in a LLP, liabilities of the partners or members are limited to his agreed contribution. In addition, due to its legal entity, partners or members of LLP are only agent to the LLP and not to one another. As such they are not liable on account of the independent or un-authorized acts of other partners, thus allowing individual partners to be shielded from joint liability created by another partner's wrongful acts or misconduct.

Despite having different liability regime, LLP and partnerships are almost identical when it comes to internal regulation and taxation. In both types of business entities, the internal affairs are regulated via an

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Smart, Flexible Hybrid Vehicle. Tax Notes International, February 23, 2009, p. 697. Singapore Income Tax Act, section 36A; IRAS circular, "Income Tax Treatment of Limited Liability Partnerships (LLPs)," first published on July 15, 2004, and revised on July 16, 2004, paragraph 5 (IRAS circular on LLPs), *available at* [http://www.iras.gov.sg/irasHome/uploadedFiles/Quick\\_Links/e-tax\\_Guides/Individuals\\_and\\_employees/2004it6.pdf](http://www.iras.gov.sg/irasHome/uploadedFiles/Quick_Links/e-tax_Guides/Individuals_and_employees/2004it6.pdf); Singapore budget speech 2009, paragraph E29, *available at*: [http://www.singaporebudget.gov.sg/speech\\_toc/downloads/index.html](http://www.singaporebudget.gov.sg/speech_toc/downloads/index.html).

agreement between the partners or members. There is no formal constitution such as the Memorandum and Articles of Association which determined how the internal relationships should be governed. Members and partners in LLP enjoy the internal flexibility similar to partners in a partnership. In relation to taxation, both partners and members of LLP and partnerships report business income or losses on their personal tax returns; the business itself does not pay tax on the income.

### **LLPs in Malaysia**

#### **(i) Labuan LLP**

At present, LLPs are only offered in Labuan. Under the LP and LLPA 2010, any two or more persons may form a Labuan limited partnership for any lawful purpose.<sup>55</sup> An individual or a corporation may be a partner in a Labuan limited liability partnership.<sup>56</sup> To register a Labuan limited liability partnership, the designated partner shall submit all relevant documents to the Authority and accompanied by the prescribed fee as may be specified by the Authority.<sup>57</sup> The name of a Labuan limited liability partnership shall end with the words “Labuan Limited Liability Partnership” in full or the abbreviation “(Labuan) L.L.P.” or “(Labuan) LLP” or any other form of abbreviation in romanised character or words in the national language of a country which connotes a limited liability partnership or any abbreviation thereof as may be approved by the Authority.<sup>58</sup>

A Labuan LP may convert to a Labuan LLP provided that the partners are all existing partners of the LP and consists of no new partner.<sup>59</sup> A Labuan company may convert to a Labuan LLP provided that there is no security interest in its assets subsisting or in force at the time of application and the partners of the Labuan limited liability partnership to which it is to be converted comprises all the shareholders of the Labuan company and consists of no new shareholders.<sup>60</sup>

Upon registration, the Labuan limited liability partnership shall be a body corporate and has legal personality separate from that of its

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<sup>55</sup> LLP and LLPA 2010; section 29(1).

<sup>56</sup> LLP and LLPA 2010; section 29(2).

<sup>57</sup> LLP and LLPA 2010; section 30(1).

<sup>58</sup> LLP and LLPA 2010; section 32(1).

<sup>59</sup> LLP and LLPA 2010; section 34(1).

<sup>60</sup> LLP and LLPA 2010; section 35(1)(a) and (b).

partners.<sup>61</sup> It shall also enjoys perpetual succession<sup>62</sup> have all the powers of a natural person.<sup>63</sup>

As a legal entity, Labuan LLP shall be liable for its own debts arising in contract, tort or otherwise.<sup>64</sup> The liabilities of the Labuan limited liability partnership shall be met out of the property of the Labuan limited liability partnership.<sup>65</sup> A partner is not personally liable, directly or indirectly solely by reason of being a partner of the Labuan LLP.<sup>66</sup> However, the protection of limited liability shall not be applicable for personal liability of a partner in tort for his own wrongful act or omission.<sup>67</sup> In such as case, the LLP is liable to the same extent as the defaulted partner.<sup>68</sup> This means the third party can make a claim against the defaulted partner and the LLP.

In the Labuan LLP, every partner is the agent of the LLP and accordingly, the acts of a partner in the partner's capacity as a partner shall bind it.<sup>69</sup> However, the LLP shall not be bound by any act of a partner with the third party if the partner has in fact no authority to act for the LLP<sup>70</sup> and the person knows that the partner has no authority or does not know or believe that partner to be a partner LLP<sup>71</sup>.

The mutual rights and duties of the partners inter se and between the LLP with its partners are mainly govern by the partnership agreement.<sup>72</sup> Only in the absence of an agreement that such matter shall be referred to the Labuan LP and LLP Act 2010.<sup>73</sup>

In the Labuan LLP there must be at least one designated partner.<sup>74</sup> A partner may become or ceased to be a designated partner by and in accordance with an agreement with the other partners.<sup>75</sup> A designated

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<sup>61</sup> LLP and LLPA 2010; section 55(1)

<sup>62</sup> LLP and LLPA 2010; section 55(2)

<sup>63</sup> LLP and LLPA 2010; section 55(3)

<sup>64</sup> LLP and LLPA 2010; section 56(1)

<sup>65</sup> LLP and LLPA 2010; section 56(5)

<sup>66</sup> LLP and LLPA 2010; section 56(2)

<sup>67</sup> LLP and LLPA 2010; section 56(3). The other partner shall not be personally liable for the wrongful act or omission of any other partner of the LLP.

<sup>68</sup> LLP and LLPA 2010; section 56(4)

<sup>69</sup> LLP and LLPA 2010; section 57(1).

<sup>70</sup> LLP and LLPA 2010; section 57(2)(a)

<sup>71</sup> LLP and LLPA 2010; section 57(2)(b)

<sup>72</sup> LLP and LLPA 2010; section 58(1)

<sup>73</sup> LLP and LLPA 2010; section 58(2)(a)-(j)

<sup>74</sup> LLP and LLPA 2010; section 64(3)

<sup>75</sup> LLP and LLPA 2010; section 64(2)

partner shall be responsible for all acts required to be done by him under the Act<sup>76</sup> and shall be personally liable to all penalties imposed on the LLP for any contravention of Parts IV and V of the Act unless the court decided that he should not be liable<sup>77</sup>.

As regards tax regime, Labuan LLP is categorized as Labuan entity<sup>78</sup> and therefore shall be the person assessable and chargeable to tax under the Act.<sup>79</sup> In Labuan, tax shall be charged at the rate of three per cent for a year of assessment upon the chargeable profits of a Labuan entity carrying on a trading activity for the basis period for that year of assessment<sup>80</sup> whilst a Labuan entity carrying on non-trading activity for the basis period for a year of assessment shall not be charged to tax for that year of assessment<sup>81</sup>.

### **Proposed Malaysian LLP**

Different from the UK LLP, which was introduced to resolve the problem of increasing insurance claims for professional negligence of accounting firms,<sup>82</sup> the proposed Malaysian LLP is meant to stimulate growth of the SMEs and to enhance the domestic business activities.<sup>83</sup> It is also aimed to prepare the local market for the international business environment.<sup>84</sup>

Referring to draft LLP Act, the Malaysian proposed LLP is akin to the incorporated LLP, whereby the LLP shall have a status of body corporate.<sup>85</sup> The draft LLP Act also highlighted similar features of a company that the LLP shall have, i.e. limited liability for all members<sup>86</sup> and perpetual succession.<sup>87</sup>

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<sup>76</sup> LLP and LLPA 2010; section 65(a)

<sup>77</sup> LLP and LLPA 2010; section 65(b)

<sup>78</sup> Labuan Business Activities Tax Act (LBATA)1990; Schedule Section 2B. Under section 11 of LBATA 1990, **11.** A Labuan entity shall (a) at the time of filing of the statutory declaration and return of its profits for a year of assessment under section 5, make full payment on account of (i) tax to be charged for that year of assessment; or (ii) tax to be charged for that year of assessment after reduction of rebate under section 8A; or (b) at the time of filing of the statutory declaration under section 7 or 8, make full payment of (i) the tax charged for that year of assessment; or (ii) the tax charged for that year of assessment after reduction of rebate under section 8A.

<sup>79</sup> LBATA 1990; section 15

<sup>80</sup> LBATA 1990; section 4(1)

<sup>81</sup> LBATA 1990; section 9

<sup>82</sup> Diana Faber, *The Law Commission Review of the Law of Partnership*, Butterworths Journal of International Banking and Financial Law, 1997 at 242..

<sup>83</sup> Consultative Document on Limited Liability Partnerships, April 2008 at p 8

<sup>84</sup> Ibid.

<sup>85</sup> Draft LLP Bill; section 3(1)

<sup>86</sup> Draft LLP Bill; section 21,

Despite the provision on limited liability, it is also expressly stated that a partner shall be personally and jointly liable with the LLP for his own wrongful act or omission.<sup>88</sup>

Other than the attributes, it is important to highlight that LLP is governed by an agreement which is akin to a partnership agreement.<sup>89</sup> However, default rules as provided under Schedule 2 of the LLP Act shall be applicable in the absence of the agreement.<sup>90</sup>

As for the number of members, draft Bill provides that any two or more persons, consisting of, wholly or partly, individuals or bodies corporate, associated for carrying on any lawful business with a view to profit may form a LLP.<sup>91</sup> It is also stated that in the case that the number of partner falls below two, the LLP can still continue its business for a period not exceeding six months or a longer period as may be determined by the Registrar upon the application from the remaining partner, provided that the period does not exceed one year.<sup>92</sup>

Professionals may also set up a LLP for the purpose of carrying on a professional practice. However, such LLP must consist of natural persons who are practicing the same professional practice.<sup>93</sup> Other than this requirement the LLP Act also provides other additional requirements for professionals LLP.<sup>94</sup>

The draft LLP Bill also requires the LLP to appoint at least one compliance officer from amongst its partners or persons qualified to act as secretaries under the Companies Act 1965.<sup>95</sup>

Pertaining to relation with the third parties, partners of the proposed LLP shall only be agents to the LLP and not to one another.<sup>96</sup>

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<sup>87</sup> Draft LLP Bill; section 3(2).

<sup>88</sup> Draft LLP Bill; section 21(3) and (4)

<sup>89</sup> Draft LLP Bill; section 9 (1) (a).

<sup>90</sup> Draft LLP Bill; section 9 (1)(b)

<sup>91</sup> Draft LLP Bill; section 6.

<sup>92</sup> Draft LLP Bill; section 7(1).

<sup>93</sup> Draft LLP Bill; section 8(a).

<sup>94</sup> Draft Bill; section 8(b): have in force professional indemnity insurance cover for an amount of not less than the amount (i) approved by the Registrar; or (ii) in the case where the professional practice is governed by a governing body as specified under the third column of the First Schedule, approved by the Registrar after consultation with the governing body.

<sup>95</sup> Draft LLP Bill; section 27(1). The compliance officer must be (a) is a citizen or permanent resident of Malaysia; and  
(b) ordinarily resides in Malaysia.

<sup>96</sup> Draft LLP Bill; section 23(1).

However, the LLP shall not be liable if the partner is acting without authority and the person with whom the partner is dealing either knows that the partner has no authority or does not know that he is a partner of the LLP.<sup>97</sup>

### Definitions and Concepts of *Sharikah*

The Islamic law recognizes a wide range of business structures for the purpose of trading, investment and profit-making. One of the structures recognized is the structure known as *sharikah/shirkali* or *musharakah*. This structure has been frequently construed as similar, or at least equivalent, to what is contemporarily termed as partnership. Nonetheless, the term *sharikah* or *musharakah* actually connotes a wider meaning than normal partnership. The term may include not only the modern partnership structure, but also any other structure that involves capital contribution and the subsequent profit and loss-sharing, including that of shareholding in modern companies, and even, certain parts of financing arrangement in a joint venture.<sup>98</sup>

The literal meaning of *sharikah* is ‘intermingle’, implying the intermingling of properties that form the capital whereby one cannot be differentiated from the other.<sup>99</sup> The term has later been used to connote the modern-day contract of partnership. A study of the classical definitions of *sharikah* reveals a variety of legal meanings given to the term. For example, the Malikites define *sharikah* as a permission to transact (*tasarruf*), where each of the partners permits the other to transact with the partnership property while at the same time retaining his right to transact with the said property also. The Hanbalites define *sharikah* as the amalgamation of rights or freedom to transact (*tassaruf*). The Shafi‘ites define *sharikah* as the confirmation of the rights of two persons or more over a common property. The Hanafites define *sharikah* as a contract between two parties in relation to capital and profit.<sup>100</sup>

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<sup>97</sup> Draft LLP Bill; section 23(2)(a) and (b).

<sup>98</sup> See for example, the discussion by Al Khayyat, Abd al Aziz (1994), *Al sharikat fi al shariah al islamiyyah wa al qanun al wad ‘i*, Muassasah al Risalah, Beirut, 4 Edition, vol.2, at p.p. 14-16.

<sup>99</sup> Al Zuhaili, Wahbah (1989), *Al-Fiqh al-Islamiyy wa adillatuhu*, Dar al-Fil, Syria, 3rd Edition, vol.5, p.792; Sabiq, Sayyid (1987), *Fiqh a- sunnah*, Dar al-Kitab al-‘Arabiyy, vol.3, p.287.

<sup>100</sup> Ibid. Al Zuhaili prefers the Hanafite definition since it incorporates the essence of *sharikah*, i.e., it being a contract, whilst the other definitions explain more on the objectives and legal implications of *sharikah*.

These various definitions refer to three dimensions. First, *sharikah* is essentially a contract between two or more parties. Second, the focus of *sharikah* is on authorization to transact with the capital or partnership property. Third, the Hanafites' definition adds another dimension to the focus of *sharikah* contract, i.e., the profit-sharing element. These three definitional characteristics of *sharikah* are also manifested in the juristic discussions on the essential elements (*arkan*) of the *sharikah* contract. Majority of the jurists<sup>101</sup> agree that there are three essential elements for the contract of *sharikah*, namely:

- Offer and acceptance, since *sharikah* is essentially a contract
- The two parties to the contract who have full legal competency to contract<sup>102</sup>
- The subject matter of *sharikah*, which can be in the form of monetary/proprietary capital, and labour capital.<sup>103</sup>

A comparison of these three definitional characteristics of *sharikah* with that of modern partnership shows some similarities. The English as well as Malaysian law definition of partnership is a "relation which subsists between persons carrying on business in common with a view of profit".<sup>104</sup> This definition is apparently implying some similar characteristics, i.e.: the contractual relation between the persons; carrying on business in common, partly implying the authorization to transact with a common property; and the profit-sharing element. Yet, some noticeable difference in focus between the definition of *sharikah* and modern partnership can also be traced. *Sharikah* focuses more on the authorization by partners to transact with the capital. Modern partnership focuses more on the commonality of actions by the partners for the purpose of business or profit.

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<sup>101</sup> Except for the Hanafites who consider offer and acceptance as the only essential element for all contracts, including that of *sharikah*. Actually, the difference between the Hanafites and the majority is purely academic because the Hanafites consider the contracting parties and subject matter as automatically covered by the requirement for offer and acceptance

<sup>102</sup> The jurists discuss the contractual competency in *sharikah* especially in relation to capacity to appoint and be appointed as agents (*wakil*), because the main underlying legal relation between the partners in *sharikah* is that of agency (*wakalah*).

<sup>103</sup> Monetary/proprietary capital is allowed by all jurists, whilst labour capital is allowed by majority of jurists except the Shafi'ites.

<sup>104</sup> Section 3(1) of the Malaysian Partnership Act 1961 (revised 1974).



Applying the definitions of *sharikah* to modern companies, it appears that the shareholders may be construed to be the ‘partners’ who contribute to the capital of the company, and thus, are entitled to certain rights (e.g. to profits/dividends, and management through general meetings) and liabilities (to contribute to the debts and losses incurred by the company). In fact, according to the Islamic law, shareholding implies a contribution to the capital of the company whereby the shareholder has a general/common proprietary right in the assets of the company including real properties, usufructs, rights, money and debts.<sup>105</sup> Thus, according to Islamic law, the legal principles governing partnerships and companies are basically similar. This concept is different from the common law approach which clearly distinguishes partnerships from companies, both in definitions or concepts, as well as the governing legal principles.

In terms of the legal effects of the contract of *sharikah*, majority of the Muslim jurists agree that it is not a binding contract (*‘aqd ghayr lazim*), which means that the partners can terminate the contract at anytime they wish to. This may be quite similar to the concept of partnership under English and Malaysian law. Another important legal effect of a contract of *sharikah* is the fiduciary position (*amanah*) that the partners hold in relation to the partnership property and capital, whereby the exercise of necessary prudence and avoidance or harm (*darar*) is the overriding principle.<sup>106</sup> This may be analogous to the common law concept of good faith and fiduciary duties of partners to each other.

The legal effect of the contract of *sharikah* on the liability of the partners will be discussed separately in the paper due to its complexity and importance to the main theme of the paper.

### Types of Sharikah

There are many ways of categorizing *sharikah*. The classical categorization of *sharikah* is based on a variety of factors. If origin of the partnership becomes the determining factor, *sharikah* can be divided

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<sup>105</sup> Hussain Hamid Hassan, *93Mukawwinat al ashum wa atharuha 91ala tadawuliha wa dawabit al qurud wa al fawa ‘id fi mua’malatiha*”, in Al Baraka Symposium for Islamic Economy, 25-27 June 2001, Kuala Lumpur, p.6.

<sup>106</sup> See Al Zuhaili, op. cit. vol.4, at p.p. 827-828.

into two broad categories, namely, *sharikah al mulk* (proprietary partnership) and *sharikah al 'aqd* (contractual partnership).

For *sharikah al mulk* (proprietary partnership), the origin of the partnership is the joint ownership of property. Joint ownership is its only qualification, and no joint exploitation of property is necessary. It occurs when two or more people are partners in the possession of property. The rule governing this type of *sharikah* is that any increase in the property shall be shared by the co-owners in proportion with the extent of their ownership. Each of them is in the category of a stranger in regard to any action on the part owned by his colleague. In other words, it is not lawful for either partner to perform any act with respect to the other's share except with the latter's express permission.<sup>107</sup> Thus, in terms of liability of the partners, they are quite independent of each other, except for actions based on express authorization by any of the partners. Their partnership is only in terms of ownership and potential sharing of any profit or increase in the co-owned property, not in term of sharing the liabilities arising from the partners' actions. This type of *sharikah* may not be known in the common law or Malaysian law. In fact mere joint-ownership is generally insufficient to constitute a partnership in common and Malaysian law.<sup>108</sup>

For *sharikah al-'aqd* (contractual partnership), the origin of the partnership is the contract between the parties. The structure of this type of *sharikah* may have more similarities to the normal partnership in common law and Malaysian law. For *sharikah al-'aqd*, joint ownership is not an element necessary for the establishment of the partnership. The emphasis is rather on the joint exploitation of capital and the joint participation in profits and losses,<sup>109</sup> based on the terms of the partnership contract. Joint ownership is one possible consequence, and not a prerequisite for the formation of *sharikah al-'aqd*.<sup>110</sup>

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<sup>107</sup> Al Qusi, Abdul Mun'irn (1982), *Riba, Islamic Law and Interest*, unpublished Ph.D dissertation, Temple University, at p.p. 205-206.

<sup>108</sup> See section 4 (a) of the Malaysian Partnership Act 1961

<sup>109</sup> This is analogous to the concept of 91 carrying on business in common with a view of profit<sup>92</sup> in normal partnership.

<sup>110</sup> Al Qusi, op. cit.

The jurists further sub-divide *sharikah al-'aqd* into various other categories. The subdivisions depend on a number of factors. If the underlying factor is the subject matter of capital contribution, *sharikah al-'aqd* can be sub-divided into three main categories, namely, *sharikah al-amwāl*, *sharikah al-a'māl* and *sharikah al-wujūh*. When the subject matter of the capital is money, it becomes *sharikah al-amwāl* (monetary partnership). If the capital is in the form of labour, it becomes *sharikah al-a'māl* (labour partnership). If the capital is in the form of reputation or creditworthiness, it becomes *sharikah al-wujūh* (reputation partnership).

The jurists also make further sub-divisions to *sharikah al-'aqd* based on the terms of the contract, i.e., whether the partners are required to contribute equally to the capital and enjoy full equality in exploiting the capital and sharing the profit or not. Based on this consideration, *sharikah* can be divided into two types, *sharikah al-mufāwahdah* and *sharikah al-'inān*.

Basically, *sharikah al-mufāwahdah* means an unlimited investment partnership, whereby each partner must contribute equally to the capital, and enjoys full and equal authority to transact with the partnership capital or property. The Hanafites consider each partner as an agent (*wakīl*) for the partnership business and stands as surety (*kafīl*) for the other partners. Thus, the partners can be made jointly and severally responsible for the liabilities of their partnership business provided that such liabilities have been incurred in the ordinary course of business.<sup>111</sup> This type of *sharikah* clearly implies unlimited liability on the part of partners since they are both agents and guarantors of each other.

On the other hand, *sharikah al-'inān* can be loosely defined as a limited investment partnership whereby each partner may only transact with the partnership capital according to the terms of the partnership agreement and to the extent of the joint capital. Hence, their liability towards third parties is several but not joint.<sup>112</sup> In other words, the liability of partners in *sharikah al-'inān* resembles that of modern-day limited liability partnerships.

Both *sharikah al-mufāwahdah* and *sharikah al-'inān* can occur in all the three earlier types of *sharikah*, i.e., *sharikah al-amwāl* (monetary

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<sup>111</sup> Umar Chapra, Towards a just inonetaly system, at p. 253.

<sup>112</sup> Ibid.

partnership), *sharikah al-a'māl* (labour partnership) and *sharikah al-wujūh* (reputation partnership).

The jurists differ with regard to a special type of commercial dealing, i.e. *mudarabah* (profit-sharing)<sup>113</sup>, whether it is a kind of *sharikah* or not. The Malikites and Hanbalites regard it as a form of *sharikah*, while the Hanafites and Shafi'ites categorize it as a separate kind.

*Mudarabah* is basically a form of commercial arrangement where one of the contracting parties act as the provider of capital (*rabb al-māl*), while the other party acts as the entrepreneur (*mudārib*). The essential difference between *mudarabah* and other forms of *sharikah* is whether or not all the partners make a contribution towards the capital as well as management of the partnership, or only one of these. In *mudarabah*, one party provides capital whilst the other provides management skill. In *sharikah*, all partners contribute to both capital and management of the partnership.

In *mudarabah*, the *rabb al-māl* is the dormant partner, while the *mudārib* is the active partner who provides the entrepreneurship and management for carrying any venture, trade or industry with the objective of generating profits. Any accruing profit shall be shared between the *rabb al-māl* and *mudārib* according to a pre-fixed ratio. In the event of loss, the *rabb al-māl* bears the financial losses to the extent of his contribution to the capital, while the *mudārib* suffers the frustration of a fruitless effort. Again, in the *mudarabah* arrangement a limited liability regime is created. However, the regime is quite different from modern limited liability. On the one hand, in *mudarabah*, it is the active partner who is exempted from financial liability (except if proven negligent or fraudulent). On the other hand, the passive partner, though bears the bulk of financial liability also enjoys limited liability because his financial liability is just to the extent of his capital contribution.

From the many types of *sharikah*, the one mainly used in contemporary Islamic banking and finance is that of *sharika al-'inan* in the category of *sharikah al-amwāl*. *Sharikah al mufāwahdah* is rarely

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<sup>113</sup> Also known as qirad or muqaradah. It has been said to be the possible origin for the commenda of medieval Europe, see for example, Hillman, R.W., "Limited liability in historical perspective", 54 Wash. & Lee Law Review, 1997, at p.p. 621-622.

opted for due to the higher degree of responsibility and the practical difficulty to achieve full equality between the partners in all aspects of the partnership. Another commonly utilised contract is that of *mudārabah*, which, some jurists consider distinct from the other forms of *sharikah*. Actually, *mudārabah* can be construed as a *sharikah* with monetary capital on the one part and labour on the other part.

In *sharikah* and *mudārabah* contracts can and have been utilized across the board, regardless of the formal business structures, i.e., whether they are partnerships or companies. For example, if the parties opted for the partnership structure, under Islamic principles, the contract will still be that of *sharikah* or *mudārabah*. The liabilities of partners are still limited up to their capital contribution, unless if they opt for *sharikah al-mufāwāḍah*, which is very rare. Similarly, even if the parties choose the company structure, the contract will still be that of *sharikah* or *mudārabah*. It follows that the extent of partners' liabilities remains the same under Islamic law, i.e., up to the amount of their capital contribution. There are no separate contracts on the basis of pure business structures - partnerships or companies. Thus, the paramount consideration in determining liability in Islamic law is not the business structure, but the actual *sharikah* contracts between the parties. If the parties want limited liability, they can choose *sharikah al-'inan* or *mudārabah*. If they want unlimited liability, they can choose *sharikah al mufāwāḍah*. Thus, from the foregoing discussions we can see that the origin of limited liability regime in *sharikah* is the contract between the parties, and not the business structure opted for.

It is also noteworthy in Islamic law that liabilities in *sharikah* normally refer to contractual obligations. Discussion on liabilities of partners in *sharikah* in the event of liabilities exceeding the assets has not been elaborately made in the classical Islamic law literature. What has been mentioned is just the general principle that liabilities follow the amount of capital contribution. This lack of elaborate discussion is understandable because the way Islamic economics and business works, ensures a built in mechanism against excessive mismatch in asset and liability ratio. As pointed out by Chapra,<sup>114</sup> in an Islamic economy, since all financial participation in business would be essentially in the form of equity, the only exceptions being suppliers' credits and *qurūd ḥasanah* (beneficial loans), the liability of the partners would in reality be limited

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<sup>114</sup> Umar Chapra, op. cit., p. 253.

to their capital contributions. Prudence would induce the suppliers to keep an eye on total equity, movement of sales and cash flows of the business concerned, while *qurūd ḥasanah* would tend to be limited. All other participants in the business (whether by way of loan or equity) would be treated as equity holders and would share in the risks of business. Since interest bearing loans are not allowed, the total obligations of the business could not be out-of-step with the total assets, and any erosion in their value may not exceed the total equity. Hence, in the ultimate analysis liability would essentially be limited to the extent of the total capital (including ploughed-back profits) invested in the partnership business.<sup>115</sup>

### CONCLUSION

It is observed that under the Civil law, the partnership based structures expanded in the line of legal entity and limited liability. For example, for the LP, the notion of limited liability is introduced but only for limited partners whilst in LLP which is actually a hybrid structure which is only similar to partnerships as regards its internal arrangement; both the legal status and limited liability are introduced. Different from the Civil law where partnerships are formed as a business structure, the concept of *Sharikah* on the other hand is confined more to the contractual relationships rather than as a business structure or a business vehicle.

The main alteration imposed to new partnership based structure is the legal status or legal entity. This is mainly obvious in LLP whereby the structure is recognized as a legal entity distinct from the partners. Such recognition as a legal person enable the LLP to embrace similar attributes of companies, namely perpetual succession, rights to enter into contract and legal proceedings under its own name and rights to own property. For the *Sharikah*, such attribute is not an issue as the partnerships between partners is merely arrangements or contracts which the parties agreed to adopt and do not exist as a business structure or entity which could be recognized by the law. The parties may agree to

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<sup>115</sup> Ibid. For a variant view see S.M. Hasanuzzaman, 93The liability of partners in an Islamic Shirkah<sup>94</sup>, Journal of Islamic Studies, Islamic Research Institute of Pakistan, 1971, at p. 332, whereby, he said that the liability of partners in a sharikah is unlimited and joint, and Al Qusi, op. cit. p. 213.

take legal action, enter into contract or limit liabilities of some partners but all these shall exist via the contract of *Sharikah* and in the form of business entity. No *Sharikah* can exist independently from the partners. As regards to limited liability, the Islamic law approach is quite distinct if compared with the civil law approach. The civil law approaches limited liability from the perspective of the actual business structure, whereby it is clear limited liability is available to companies but not to partnerships. However, under the Islamic law, the determining factor for limitation of liability is the actual contract between the parties, not the formal business structure. If the actual contract gives full equality and authority to the partners, thus, making the partner agent and guarantor of the other partners (*sharikah al mufāwah*), there will be unlimited liability. But, anything short of that makes the *sharikah* contract limited and liability will also be limited. In addition to that, if the parties choose the special arrangement of *mudarabah*, a unique situation exist, whereby the active partner is prima facie exempted from financial liability, while at the same time, the passive partner enjoys limited liability. Despite the different approach, it is apparent that the principle of limited liability is viable and acceptable under the Islamic law. In Malaysia the partnership structure had been expanded to include the LP and the LLP. It is obvious that the pattern of development of the partnership based structure in Malaysia is in accord to the Civil Law, whereby as the partnership based structure is developed, some attributes of the partnerships are changed. Under the Islamic law, the concept of partnership or *Sharikah* is not changeable though modifiable in accordance with the agreement of the partners.