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## Limited Liability in Corporate Group: A Critical Examination under Common Law and Shariah in Malaysia

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### Abstract

Limited liability is a default rule in company law that protects shareholders from shifted-business risk in a company to external parties. Its application in the corporate group setting is heavily criticized for causing harm to the subsidiary's creditors particularly. While this rule is proposed to be refined due to its rigidly unreasonable privilege and lack of justice, it becomes more complicated where the Shariah-compliant businesses have adopted this rule as their corporate structure. Despite this, the Malaysian company law recognizes the distinct legal personalities of entities within corporate group regardless their businesses are typically operated as a single entity. Contrastingly, limited liability is not established in Islamic business entities like *sharikah* (partnership) because the latter entails a single entity premised on a sharing-business risk among the partners. The study undertakes doctrinal analysis to examine the application of limited liability in corporate group under the Malaysian company law and compare it with the Shariah principles of *sharikah*. The study relies on the library-based research in collecting and gathering the data to support this methodology. The paper proposes to show whether the conventional rule of limited liability could be directly applied to group of companies operating Shariah-compliant businesses which supposedly comply its corporate structure with *sharikah*. The paper concludes that such direct application is untenable due to different natures and business structures. Examining this comparison is substantial to explore the essential of forming a new business model for Shariah-compliant corporate groups structured based on *sharikah* principles.

**Keywords:** Corporate Group; Limited Liability; *Sharikah*.

### Introduction

Nowadays, many have raised up a need of conducting businesses in more sustainable ways, covering three main aspects namely economy, social and

environment.<sup>1</sup> Such address insists a reform in the corporate law to achieve this sustainable agenda particularly in corporate governance structure, roles of directors etc.<sup>2</sup> In the meantime, addressing the legal hurdles caused by the COVID-19 outbreak has accelerated the movement to support various parties affected from this pandemic such as employees, creditors and others. Other temporary relief measures are given to affected companies to ensure that their businesses are survived and continuously sustained. However, the fundamental legal attributes underpinning the corporate structure become the cornerstone of why the sustainable agenda is not accomplished successfully. In fact, many have overlooked the roles of shareholders, persons behind the company that are supposed to play in addressing this global crisis. The main reason central to this would be the legal privilege bestowed to the shareholders, i.e., limited liability.

Limited liability is a default rule in company law that protects shareholders by transferring the risk of business in a company to external parties dealing with it. Though it carries many economic advantages, its application in the corporate group setting is heavily criticized for causing harm to the subsidiary's creditors that remains contentious until present. While this rule is proposed to be refined due to its rigidity in a sense that it provides an unreasonable privilege that is mostly not open for challenged and its lack of justice, it becomes more complicated where the Shariah-compliant businesses have adopted this rule as part of their corporate structure. This questions as to the status of its Shariah-compliant status. Despite this, according to the Malaysian company law, corporate group entails separate legal entities, each distinct from the others even if their operations are commonly conducted as a unified entity. The metaphor of corporate personality is used to justify these attributes and the limitation of liabilities within the group. However, such principle is not established in Shariah business entities like *sharikah* because

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<sup>1</sup> Colin Myers and Jason J Czarnezki, 'Sustainable Business Law? The Key Role of Corporate Governance and Finance' (2021) 51 Environmental Law.[992-993].

<sup>2</sup> Benedict Sheehy, 'Sustainability, Justice and Corporate Law: Redistributing Corporate Rights and Duties to Meet the Challenge of Sustainability' (2022) 23 European Business Organization Law Review.[276].

under the Shariah, *sharikah* as a single holding entity is premised on a risk sharing business model among the partners in business profits and losses in the *sharikah* collectively. A doctrinal analysis is chosen by this study to examine the application of limited liability in corporate group under Malaysian company law and compare it with the Shariah principles in *sharikah*. A library-based research was adopted to gather significant literatures from both primary and secondary data. The authors gather its primary data for legal aspect from the statute namely the Companies Act 2016 (CA 2016), and cases laws while the primary data for Shariah aspect includes its primary sources namely Al-Qur`an and Hadith. The secondary data for both legal and Shariah aspects are taken from law textbooks, journals, Islamic *fiqh* literatures and the like. The purpose of this paper is to show whether the conventional rule of limited liability bestowed to group of companies in Malaysia, could be directly applied to group of companies which undertake Shariah-compliant businesses which supposedly comply its corporate structure with *sharikah*.

Previous studies were conducted on the same subject matter and its related area. For instance, Rizkiah and Muhammadin have significantly highlighted that the insulation of shareholders from the company's debts due to limited liability regime while enjoying rights to receive its residual profits is hard to justify under the Shariah because the settlement of debts is obligatory from Shariah perspective. However, they further acknowledge that not utilizing this rule may cause devastating economic repercussions.<sup>3</sup> According to Asad et al., invoking limited liability in a company entails the absolution of debt on the part of shareholders which is prohibited under Shariah and contravenes the Shariah principle of *al-kharaj bi al-dhaman* (the revenue is upon assumption of liability).<sup>4</sup> Furthermore, Abd Ghadas & Abd Aziz studied the comparison of limited liability under common law and Shariah. However, the comparison focusses only on a

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<sup>3</sup> Siti Kholifatul Rizkiah and Fajri Matahati Muhammadin, 'A Critical Examination towards the Islamic Discourse on "Limited Liability"' (2020) 11(1) UUM Journal of Legal Studies.[30].

<sup>4</sup> Muhammad Asad, Hafiz Muhammad Usman Nawaz and Barkat Ali, 'Limited Liability of Shareholders: Islamic Perspective (A Critical Appraisal)' (2020) 14 Journal of Managerial Sciences 99.[101].

single company which makes no reference to corporate group.<sup>5</sup> In addition, Ramli et al. highlighted that *sharikah* can be an avenue for corporate legal structure with certain modifications.<sup>6</sup> Yet, such recommendation has not addressed deeply on how it addresses the issue of limited liability in the corporate group setting. In this regard, this paper aims to fill these gaps.

### **Position of Limited Liability of Corporate Group in Malaysian Company Law Corporate Group under CA 2016**

The Malaysian company law is rooted from the common law. The common law principles governing company are mainly codified in the CA 2016. Under the common law, company is a body corporate that is incorporated by the legal statute based on legal fiction. It has distinct legal personhood from its directors and members. This legal principle is consequential from the doctrine of corporate personality which regards the company having an artificial legal personality.<sup>7</sup> The doctrine and this legal principle are affirmed by the House of Lords in *Salomon v A Salomon and Co Ltd* [1897] AC 22 where Mr. Salomon is insulated for the company's debts owed to its unsecured creditors because of such legal principle. Similarly, the case is firmly applied in various Malaysian legal cases which uphold the same principle embedded from the common law. As a result, this bedrock principle not only changes the company as to its legal form, but also its substance that must be respected.<sup>8</sup>

The incorporation of legal personality of company is the basis of why corporate group is possibly formed.<sup>9</sup> Corporate group is defined as “a body of companies

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<sup>5</sup> Zuhairah Ariff Abd Ghadas and Hartinie Abd Aziz, ‘Analysis on The Doctrine of Limited Liability under Company Law and Shariah’ (2019) 24 *Al-Shajarah Journal of Islamic Thought and Civilization of IIUM*. [295].

<sup>6</sup> Nazri Ramli, Zuhairah Ariff Abd Ghadas and Hartinie Abd Aziz, ‘Sustainability of Businesses via Shariah-Compliant Framework: Analysis of Shariah Principles on Corporation’ (2023) 31 *IIUM Law Journal*. [313-314].

<sup>7</sup> Abd Ghadas and Abd Aziz (n 5). [299].

<sup>8</sup> John Quinn, ‘The Corporate Objective: Reinterpreting Directors’ Duties’ (Dublin City University 2016). [36].

<sup>9</sup> Aiman Nariman Mohd Sulaiman and Effendy Othman, *Malaysia Company Law: Principles and Practices* (2nd edn, Wolters Kluwer 2018). [43].

constituted by the parent company and subsidiaries”. Two characteristics that underlie the corporate group are first, the existence of inheritable link between the entity members of the group, and second, while the group has no corporate legal personality, parent and its subsidiaries within the group are distinct legal entities.<sup>10</sup> The definition of corporate group is not provided in the CA 2016. However, Section 4(a) provides the definition of subsidiary and holding company whereby the latter either controls the subsidiary’s composition of its board of directors, more than half of its voting power, or more than half of its issued share capital (50%). In other word, this corporate group structure entails a parent-subsidiary relationship. Other relevant provisions relating to corporate group structure comprise ultimate holding company, wholly owned subsidiary and related company.<sup>11</sup>

### **Limited Liability: History, Advantages and Its Application under the CA 2016 and Legal Cases**

Macey articulated the concept of limited liability as ‘the ceiling on shareholders’ risk of loss associated with their investments is limited to the amount of those investments’.<sup>12</sup> Historically, it was introduced two hundred years ago to enable the large investment projects took place during the Industrial Revolution.<sup>13</sup> From economic parlance, limited liability encourages business risk taking that generate economic growth and employment, particularly for passive investors who have no knowledge of business management.<sup>14</sup> Interestingly, Tepre stated that limited liability was not originally introduced through judicially legal recognition, but by way of legal statute.<sup>15</sup> Among the benefits of limited liability are that it

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<sup>10</sup> Dieudonné Nzafashwanayo, ‘Corporate Groups under the Laws of Rwanda: An Economic Reality without Legal Identity’ (2016) 7 Beijing Law Review.[97].

<sup>11</sup> Loganathan Krishnan, Parimaladevi Rajoo and Anne Chrishanthani Vergis, *Principles of Business and Corporate Law, Malaysia* (4th edn., Commerce Clearing House, Wolters Kluwer 2022).[217].

<sup>12</sup> Jonathan R Macey, ‘The Central Role of Myth in Corporate Law’ (2020).[35].

<sup>13</sup> Abd Ghadas and Abd Aziz (n 5).[295].

<sup>14</sup> Macey (n 12).[35].

<sup>15</sup> Paul Tepre, ‘Liability Deficit Problem of Multinational Corporate Groups: A Proposal for Legislative and Judicial Reform’ (University of British Columbia 2017).[42].

encourages businesses, the establishment of big firms, the division of ownership of shares and control of management, and the growth of liquid capital markets.<sup>16</sup> Despite these various economic advantages of limited liability, Blumberg underlined several theoretical drawbacks such as (a) unfairness and inefficiency for tort and other involuntary creditors, (b) unfairness for labor claimants, (c) encourages more excessive risky investments, (d) impairment of market and (e) leads to misrepresentation. He viewed that limited liability should not apply to corporate group as the latter's operations and structures are identical to individual shareholder who needs protection from the company by way of limited liability.<sup>17</sup> The application of limited liability into corporate law marked a shifting risk and responsibility from shareholders founded on the partnership principle. The irresponsibility is premised in the corporate legal form, making no obligation nor liability toward the company's misfortunes.<sup>18</sup> Tepre significantly raised the legislature's failure to address potential abuses and bad consequences of limited liability as a risk-shifting device.<sup>19</sup>

The legal rules of limited liability is governed under Section 194(a) of the CA 2016 where a member shall not be liable for a company's obligation by reason of being a member. As derived from Salomon, incorporating business into a corporate legal entity insulates the members' personal liabilities from the company.<sup>20</sup> In particular, separate legal entity and limited liability as the two intertwined legal principles are applied together to the effect that since the law recognizes the company's distinct legal personhood from the shareholders, their liabilities that are

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<sup>16</sup> Sharon Belenzon, Honggi Lee and Andrea Pataconni, 'Managing Risk in Corporate Groups: Limited Liability, Asset Partitioning, and Risk Compartmentalization' (2023) 44 *Strategic Management Journal*, Wiley Blackwell 2888.[2893].

<sup>17</sup> Phillip Blumberg, 'Limited Liability and Corporate Groups' (1986) 11 *The Journal of Corporation Law* 573.[624].

<sup>18</sup> Paddy Ireland, 'Limited Liability, Shareholder Rights and The Problem of Corporate Irresponsibility' (2010) 34 *Cambridge Journal of Economics*. [845] See also Paddy Ireland, 'Corporate Schizophrenia: The Corporation as a Separate Legal Person and an Object of Property' [2016] *University of Bristol*. [30].

<sup>19</sup> Tepre (n 15).[42].

<sup>20</sup> Marios Koutsias and Janet Dine, 'The Three Shades of Tax Avoidance of Corporate Groups: Company Law, Ethics and the Multiplicity of Jurisdictions Involved' (2019) 30 *European Business Law Review* 149.[156].

limited to the balance of unpaid investment capital must also be respected.<sup>21</sup> This is expressly recorded by Shankar J in *Aziz Atan & Ors v. Ladang Rengo Malay Estate Sdn. Bhd* (1985) 2 MLJ 165 as follows:

*“It is trite law that an incorporated company is a legal person separate and distinct from the shareholders of the company. The company from the date of incorporation has perpetual succession and the Companies Act provides that the liability on the part of the shareholders to contribute to the assets of the company will be limited in the manner provided by law and its memorandum and articles of association. The whole point of forming a limited company is that the shareholders can have in their hands the management of the business without incurring the risk of being under unlimited liability for the debts of the company”.*

Similarly, limited liability also applies to group of companies regardless of its various ownership structure in Malaysia particularly. Such application arose from a historical accident. When the company is allowed to become the shareholder of other company, the rule of limited liability applied to a parent as the shareholder of its subsidiary is subsequently followed. Hence, it limits the former for the latter’s action.<sup>22</sup> This limitation creates a multi-layer protection for the parent which insulates itself from liability of its subsidiaries.<sup>23</sup> In *Theta Edge Bhd v. Infornential Sdn Bhd & Another Appeal* [2017] 7 CLJ 53, Hasnah Mohammed Hashim, the Court of Appeal Judge (JCA) held as follows:

*“A company is an entity separate from its shareholders and that a subsidiary and its parent or holding company are separate entities having separate existence”.*

## **Limited Liability of Corporate Group from Shariah Perspective**

### ***Sharikah* as a Form of Islamic Business Entities:**

Discussing the issue of limited liability necessitates a brief overview of the

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<sup>21</sup> Carsten Gerner Beuerle and Michael Anderson Schillig, *Comparative Company Law* (Oxford University Press 2019).[32-33, 41].

<sup>22</sup> Koutsias and Dine (n 20).[9].

<sup>23</sup> Blumberg (n 17).outside fairness review, and ex ante shareholder approval is both flawed in its design and based on contestable assumptions on informed voting of institutional investors. In particular, the contemplated exemption for transactions with wholly owned subsidiaries allows controlling shareholders to circumvent the rule extensively. Moreover, vesting voting rights with (institutional[607, 609].

concept of corporate group from Shariah perspective. Ahmed highlighted that corporate law is a new phenomenon that is not clearly discussed in the Islamic heritage. Yet, numerous contemporary Shariah scholars discussed it under the perspective of *sharikah* to ascertain its ruling.<sup>24</sup>

*Sharikah* is defined as a contract between two or more persons to do business with capital and work, or work from one of them or capital from one partner and work from another partner or with their goodwill with a permissible agreement. It is also defined as a contract between two or more persons for the participation in a business capital and its profit, or in a fee of work or participation in goods without capital available for trading purpose.<sup>25</sup> These definitions include among others *sharikah al-`inan* (limited partnership) and *mudharabah* (silent partnership) as types of *sharikah* contracts. The difference between the two is that *sharikah* entails both or more partners to provide the capital and involve in the management business whereas *mudharabah* demonstrates the passing of capital by the *rabbul mal* or owner of capital to the *mudharib* or manager to do the business and they both share in a profit. In brief, it is illustrated the discussions among the classical Muslim scholars on the permissibility of an existing partner to transact in a new *sharikah* or *mudharabah* with a new partner. All of them agreed that such arrangement is valid upon consent from another co-partner. It is this reason that multiple *sharikah* contracts can be entered by the co-partners subjected to their partners' consent or permission.<sup>26</sup>

In parallel, Al-Khalil recorded the contemporary scholars' discussions on the concept of *sharikah al-musahamah* (joint stock company) from Shariah perspective and recognized it under *sharikah al`inan*.<sup>27</sup> In this regard, some scholars such as

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<sup>24</sup> Habib Ahmed, 'Islamic Law, Investors' Rights and Corporate Finance' (2012) 12(2) Journal of Corporate Law Studies.[384].

<sup>25</sup> Muhammad `Abdullah Butaiban, *Ahkam Al-Khasarat Wa Tatbiqatuha Al-Mu`asirah* (1st edn, Dar Sulaiman Al-Maiman lii Al-Nashr wa Al-Tawzi' 2021).[533-534].

<sup>26</sup> Abdul Aziz Muhammad Abdullah Al-Hujailani, *Tasarrufat Al-Amin Fi Al-`Uqud Al-Maliyyah* (1st edn, Vol 1, Majallah Al-Hikmah, Great Britain 2002).[102-104].

<sup>27</sup> Ahmad Muhammad Al-Khalil, *Al-Ashum Wa Al-Sanadat Wa Ahkamuha Fi Al-Fiqh Al-Islami* (1st edn, Dar Ibn Al-Jawzi 2002).[117].



Al-Khayyat<sup>28</sup> further argued that *sharikah al-qabidhah* (holding company) as derived from *sharikah al-musahamah* is also recognized under Shariah, applying the similar concept of *sharikah al-`inan*. The latter is ascertained where the parent company invests the capital into the subsidiary upon the consent granted by other shareholders of the subsidiary.

### **Views of Contemporary Scholars on Limited Liability of Corporate Group under Shariah**

The authors recorded diverging views among the contemporary scholars on the ruling of limited liability into three groups as follows:

#### **First Group: Limited Liability is Permissible**

This group headed by Al-Zuhaili Al-Khayyat, Al-Khafif, and other contemporary scholars argue that limited liability is permissible under Shariah based on several justifications. Firstly, the permissibility of limited liability is based on the Islamic legal maxim “*the original ruling for everything (that is beneficial) is permissibility, until there is evidence of its prohibition*”. This is because there is no harm under Shariah to limit the liability when other parties dealing with this company consent on its limited liability arrangement. Secondly, limited liability is a stipulated condition agreed upon by its members during the company’s incorporation and other parties dealing with it are aware of such condition and therein consent to it. Thus, stipulating such condition that does not contravene with any provision under Shariah is permissible based on the Hadith: “*the Muslims are bound by their (agreed) conditions except the condition that permits what is forbidden or forbids what is permissible*”.<sup>29</sup> Thirdly, limited liability is analogized with *mudharabah* whereby the *rabbul mal* is not liable for losses in the *mudharabah* business except

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<sup>28</sup> Abdul Aziz Al-Khayyat, ‘Al-Sharikat Al-Qabidhah Wa Ahkamuha Al-Syari’yyah’, *Majallat Majma’ Al-Fiqh Al-Islami Li Mu’tamar Majma’ Al-Fiqh Al-Islami* (Vol 2 2004).[362-364].

<sup>29</sup> Wahbah Al-Zuhaili, *Al-Mua’alat Al-Maliyyah Al-Mua’sirah* (Dar Al-Fikr 2002).[129].

for his limited capital contribution.<sup>30</sup> Furthermore, El-Gari also supported this legal feature by making analogy with *al'abd al-ma'dhun* where the slave's owner, who provided the capital to the former in conducting the business is not liable for any losses more than his capital contribution.<sup>31</sup>

It is observed although El-Gari is silent on the ruling of limited liability within corporate group. The above analogy is also applicable to the latter where he expressly articulated that such legal feature makes the corporate group identical to *sharikah* concept. In support of this view, Al-Soifi argued that in *sharikah al-qabidhah* context, there is no impediment under Shariah to incorporate a business with this legal feature as it is known to others. As such, having knowledge of such limited liability denies *gharar* (uncertainty).<sup>32</sup> According to Maddur, *sharikah al-qabidhah* is not liable for its subsidiary's debts but for its limited investment based on two reasons. First, *sharikah al-qabidhah* is viewed as the *rabbul mal* who is not liable more than its investment capital in the subsidiary. Second, from *sharikah al-'inan* perspective, *sharikah al-qabidhah* is not liable for the subsidiary's debts based on the concept of *sharikah al-'inan* founded on *wakalah* contract not *kafalah* (surety).<sup>33</sup>

### Second Group: Limited Liability is Permissible with Restriction

This group argue that although limited liability is permissible under Shariah, its application must be restricted in some circumstances. For instance, Uthmani argued that limited liability shall not be applicable for private companies because Every shareholder and partner has the capacity to readily access information regarding the daily operations of the business and should bear accountability for all

<sup>30</sup> Abdul Aziz Al-Khayyat, *Al-Sharikat Fi Al-Shariah Al-Islamiyyah Wa Al-Qanun Al-Wad'ie* (4th edn, Muassasah Al-Risalah 1994).[167].

<sup>31</sup> Muhammad Ali El-Gari, 'Athar Al-Ikhtilaf Baina Al-Shakhsiyyah Al-Tabi'iyah Wa Al-I'tibariyyah Fi Al-Ahkam Al-Fiqhiyyah Li Mustajiddat Al-Masrafiyyah Al-Islamiyyah', *5th Shura Fiqh Conference 2013* (2013).[282].

<sup>32</sup> Abdullah A'li Al-Soifi, *Al-Sharikat Al-Qobidah Wa Ahkamuha Fi Al-Fiqh Al-Islami* (1st edn, Dar Al-Nafais 2006).[81].

<sup>33</sup> Jamilah Maddur, 'Al-Sharikah Al-Qabidhah Qawa'id Al-Musharakah Wa Dhawabit Al-Munafasah' (Jamiah Al-Haj Likhudr Al-Batinah 1 2019).[214-215].

its obligations. In addition, it should be allowed if it is used paramount to fraud.<sup>34</sup> Al-Haqil also put the same view that such application must be restricted to two conditions; free from any fraud committed by the shareholders to escape liability; or all the shareholders equally bear the losses in the corporation in proportion to their capital contribution.<sup>35</sup> It is also argued that the application of limited liability should only be restricted to *sharikah al-musahamah* having many shareholders (public company) based on *hajah* (necessity). Yet, such application is not extended to other forms of company due its paramount harm than the benefits.<sup>36</sup>

### **Third Group: Limited Liability is Impermissible**

This group headed by Al-Baqmi and others argue that limited liability is not permissible based on several justifications. First, this legal feature contradicts the classical scholars' consensus on a Shariah principle that the losses shall be borne by the partners in respect of their capital proportion. In fact, they do not differentiate the *dhimmah* of *sharikah* and its partners as they belong to the same aggregate and therefore the debts of the business are attached to them. When *sharikah* fails to settle, then the partners need to settle it based on their capital ratio. Second, as *sharikah* is founded on *wakalah*, it cannot apply limited liability as the *sharikah* property is actually owned by the partners as a single entity. Its existence as a legal entity aims only for capability of its operation and incorporation under the law where it represents the partners as the actual owners of the property.<sup>37</sup> Third, invoking limited liability contradicts the Islamic legal maxim "*al-kharaj bi al-dhaman*" in a sense that to legitimize the gaining of profit under Shariah, the partner must assume all liabilities and obligations in the *sharikah* business or otherwise such gaining

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<sup>34</sup> Muhammad Taqi Uthmani, *An Introduction to Islamic Finance* (Idara Isha'at E-Diniyat (P) Ltd 2008).[159-160].

<sup>35</sup> Abdullah Muhammad Al-Haqil, 'Al-Masuliyah Al-Mahdudah Fi Al-Sharikat Dirasah Ta'siliyyah Tatdbiqiyyah' (2019) 25 Majallah Al-'Adl.[355-356].

<sup>36</sup> Ahmad Muhammad Hamd Al-Razin, 'Al-Shakhsiyyah Al-Hukmiyyah Li Al-Sharikah Al-Mu'asirah Dirasah Fiqhiyyah' (Al-Jami'ah Al-Imam Muhammad Sa'ud Al-Islamiyah 2005). [287-288].

<sup>37</sup> Salih Zabin Al-Marzuqi Al-Baqmi, *Sharikat Al-Musahamah Fi Al-Nidzam Al-Saudi Dirasat Muqabalah Bi Al-Fiqh Al-Islami* (1st edn, Obeikan 2019).[209-210].

would render unlawful.<sup>38</sup>

In relation to corporate group, Disomimba argued that the application of limited liability depends on its relationship. If *sharikah al-qabidhah* is based on *sharikah al-`inan*, then its liability toward the subsidiary's debts is limited to the investment capital except that the former administered the latter's affairs that caused for fraud. If the *sharikah al-qabidhah* is based on *sharikah al-mufawadhah* (equal partnership), then the liability should be unlimited as both parties are based on both *wakalah* and *kafalah*.<sup>39</sup> Fahmi articulated that application of limited liability in *sharikah al-qabidhah* causes *darar* (harm) to the subsidiary's creditors.<sup>40</sup>

### Observation and Analysis

The invocation of limited liability within the corporate group under the common law is based on the company's business structure and not a contractual arrangement among the members as it is a creation of legal statute. The purpose of which the company is incorporated is to enjoy limited liability protection. This entails that the legal form and substance of a company is already changed. In this regard, many legal cases show that corporate group applies the default rule of distinct separate legal entity and limited liability that are not founded on partnership or agency unless factually or legally proven otherwise as highlighted in *Pioneer Concrete Services Limited v Yelnah Pty Ltd* (1986) 11 ACLR 108. Having regard to these legal attributes of company, Sheehy argued that corporate law enables the organization of operations, minimizing the potential for liability arising from the decisions made by the board and members. Such setting is not consonant with the effective allocation of risk and reward.<sup>41</sup>

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<sup>38</sup> Imran Ahsan Khan Nyazee, *Islamic Law of Business Organization: Corporations* (Adam Publishers & Distributors 2010).[168].

<sup>39</sup> Abd Al-Salam Wari Disomimba, 'Ahkam Al-Sharikah Al-Qabidhah Wa Al-Tabi`ah Fi Al-Fiqh Al-Islami' (International Islamic University Malaysia 2006).[306].

<sup>40</sup> Husain Kamal Fahmi, 'Al-Sharikat Al-Hadithah Wa Al-Sharikat Al-Qabidhah', *Majallat Majma' Al-Fiqh Al-Islami Li Mu'tamar Majma' Al-Fiqh Al-Islami* (14th Sess., Munadzamah Al-Mu'tamar Al-Islami 2003).[464].

<sup>41</sup> Sheehy (n 2).[294].

Based on the above discussions on the ruling of limited liability from Shariah perspective, it is observed that many contemporary scholars permit it based on analogy with several cases found in the classical *fiqh* texts such as *al-`abd al-madhun*, *sharikah al-`inan* and *mudharabah*. However such analogy is also criticized by other scholars with several justifications. For instance, Al-Qarahdaghi argued that for *al-`abd al-madhun*, during when the slave is unable to settle the debts in the business, it is the responsibility of the owner to settle it since he is the actual owner of the slave and the business. As such, there is no such limited liability in this case.<sup>42</sup> Furthermore, for *sharikah al-`inan*, many contemporary scholars examined its Islamic feature and found that the liability of partners in the *sharikah al-`inan* is always unlimited in accordance with their respective capital ratio. This is because the *dhimmah* of *sharikah* is inseparable from the partners and hence, they incur all the debts arising from the *sharikah*.<sup>43</sup> However, it is understood that some argue that *sharikah al-`inan* applies limited liability feature in a sense that the partner is liable in accord to his capital contribution. Hence, he cannot incur liabilities of his co-partner more than his capital contribution.<sup>44</sup> For *mudharabah*, Al-Haqil revealed that the *rabbul mal* is not liable for losses incurred in *mudharabah* beyond his capital investment in two situations: when it is duly caused by the *mudharib*'s negligence or misconduct; or when it is done below or within the capital invested. If the *mudharib* conducted any transaction that amounts to increasing more capital than what he has invested and it is later permitted by the *rabbul mal*, he then will bear the losses arising from transaction.<sup>45</sup> In addition, another argument used to justify limited liability is the application of the concept of *hajah* under Shariah. It is however refuted that the concept of *hajah* is estimated by the extent thereof i.e.

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<sup>42</sup> A'li Mahyuddin Ali Al-Qarahdaghi, *Buhuth Fi Fiqh Al-Bunuk Al-Islamiyyah* (1st edn., Isdarat Wazarah Al-Awqaf wa Al-Shuun Al-Islamiyyah Qatar 2010).[217-218].

<sup>43</sup> Abi Umar Abdullah Muhammad Al-Hammadi, *Al-Sharikah Dzat Al-Masuliyah Al-Mahdudah Fi Al-Fiqh Al-Islami Wa Qanun Dawlah Al-Imarat Al-Arabiyyah Al-Muttahidah* (1st edn, Dar Al-Muayyad 2007).[359].

<sup>44</sup> Zuhairah Arif Abd Ghadas and Engku Rabiah Adawiah Engku Ali, 'Partners' Limited: Limited Liability in Partnerships Structure: An Overview of The Common Law and The Shariah' (2009) 1 Shariah Law Reports xlv 45.[55].

<sup>45</sup> Al-Haqil (n 35).[357-348].

it must be limited to the extent that is permitted<sup>46</sup> in order to avoid from its abuse. This Shariah principle has its merit given the application of limited liability does give harm to external parties, such as unsecured creditors in tort cases and secured creditors in contract cases.

In relation to the third group's view above, it is revealed that limited liability may be criticized under Shariah in other aspects. First, limited liability is an example of consuming someone's wealth unjustly. Allah says "*do not consume one another's wealth unjustly...*"<sup>47</sup> As far as limited liability is concerned, the release of debt that is originally attached to the company due to the contention that the shareholders are not liable for such debts amounts to their consumption of creditors' property unjustly.<sup>48</sup> Second, allowing limited liability seems to contradict the Shariah principle of obligation to settle debts.<sup>49</sup> Indeed, Allah obliges the debtors to immediate the settlement of debt as such delay could cause harm to the creditors such as they would face bankruptcy if their debts are not paid off. Allah says: *Indeed, Allah commands you to render Amanah (trusts) to whom they are due.*<sup>50</sup> Based on this verse, the phrase '*amanah*' comprises all kinds of trusts owed to human beings that must be preserved such as rights of people and trust over properties.<sup>51</sup> In the context of *sharikah*, all debts arising from the business are borne by the partners responsibly since such debts are considered as *amanah* upon them to fulfil the creditors' rights. Third, in considering the *fiqh al-maalat* (consequence of action) under the realm of *maqasid al-Shariah* (objective of Islamic law), applying limited liability gives more actual *mafasid* (harms) than its *masalih* (benefits). Hence its ruling of permissibility should be changed in striking balance between the two aspects.

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<sup>46</sup> Ahmad Kafi, *Al-Hajah Al-Shar'iyah Hududuha Wa Qawa'iduha* (1st edn, Dar Al-Kutub Al-Ilmiyyah 2004).[188].

<sup>47</sup> Al-Quran Al-Karim, Surah Al-Baqarah, verse 188.

<sup>48</sup> Al-Hammadi (n 43).[406].

<sup>49</sup> Rizkiah and Muhammadin (n 3).[28].

<sup>50</sup> Al-Quran Al-Karim, Surah Al-Nisa', verse 58.

<sup>51</sup> Al-Hujailani (n 26).[50-51].

## Conclusion

In conclusion, the approach to the principle of limited liability differs between Malaysian company law and Shariah.. The former governs limited liability in the corporate business legal structure while the latter set it out in a contractual arrangement. Under *sharikah al-`inan*, the liabilities of partners are limited in a sense that they incur losses in accordance with their capital contribution. This does not entail that their liability is confined to their unpaid capital investment alike the company limited by shares. This Shariah principle is agreed upon by all the classical scholars because *sharikah* is founded on the concept of *`adl* (justice) among the partners that is not the case in the company law. Also embodied from *wakalah*, *sharikah* entails a single entity inseparable from the partners regardless of multiple *sharikah* or *mudharabah* contracts incorporated among themselves. By contrast, corporate group adopt limited liability among its corporate entities. The recent study has shown that the debate among the contemporary scholars on the legitimacy of limited liability which has no basis under the Shariah, remains valid and continues until present.

Overall, discussing the sustainability of business post endemic of COVID-19 entails a need to revisit limited liability as among the legal features of corporate group. From Shariah perspective, limited liability has contentious issues that need for addressing. This attempt is crucial since Shariah also supports sustainable business agenda but the way it manifests differs from the legal or conventional mainstream. The paper concludes that the direct application is limited liability into corporate group which undertakes Shariah-compliant businesses is untenable due to their different natures and business structures. Such findings necessitate to explore further a new business model for Shariah-compliant corporate groups which are and should be structured based on *sharikah* principles.

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