
A CRITICAL ISLAMIC PERSPECTIVE TOWARDS AGENCY THEORY

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Abstract

Agency theory is the value of the economic system of capitalism. The purpose of this paper is to examine and criticize agency theory based on an Islamic perspective. Islamic perspective is considered very important developments. An overview of these different theories, along with principal-agent agency theory. By following these criticisms, then, emerging theories and alternative perspectives that need discussion. That is the perspective of Islam is considered a very important development. The results of the study show that agent contract principles in an Islamic perspective are based on the ASIFAT concept, namely: Akhidah (obedience to Allah Ta'ala), Shiddiq (true), Fathanah (intelligent), Amanah (honest/trustworthy) and Tabligh (communicative). Contract between principal and agent in an Islamic perspective are based on amanah contracts and give each other noble character in carrying out these amanah.

Keywords: Agency theory, ASIFAT, amanah, contract

1. INTRODUCTION

Agency theory has a long history and has again become a major work since it is based on formative economics-based works of Spence and Zeckhauser (1971), Ross (1973) and Jensen and Meckling (1976). Since these early works in the field of economics were published, scholars have studied theoretically for various mechanisms in explaining market failures implied in the earliest agent conceptions (Berle & Means, 1932/2009; Smith, 1776/1952). Scholars also look for principal-agent problems as well as an important instrument from the view of incomplete contracts of companies developed by Jensen and Meckling, 1976, Fama, 1980, Fama and Jensen, 1983a, 1983b, Mahoney, 2005, Agarwal, et.al. 2014. The theory was taken up by researchers in finance and management by Kallmuenzer, 2015, Yusof, 2016, Kultys, 2016, Zongning, 2017 and Kumalasari and Sudarma, (2018).

Agency theory is one of the dominant theories of organizations and management due to its specific focus on the relationship between principal and agent (Dalmácio and Nossa, 2004; Zongning, 2017 and Payne and Petrenko, 2019). The agency theory aims to globally explain organizational behaviours by putting an emphasis on the relationship between the manager as the company's "agent", and the shareholder as the "principal" (Zongning, 2017). Jensen & Meckling (1976) states that agency relations arise when one or more principals pay agents to act on their behalf, delegating the power to make decisions to him. In the context of financial management,

this relationship arises between stakeholders and managers and between shareholders and bondholders.

There are a number of limitations of agency theory (Agarwal et.al. 2014; Shleifer and Vishny1997; Daily et al. 2003). Agency theory assumes complete contracts (eg contracts that serve all the possibilities that might occur such as inconvenience, conflict, unforeseen circumstances, disputes, etc.). Bound rationality does not allow for a complete and efficient contract. Information asymmetry, transaction costs, and selfishness are possible conditions that cannot be addressed in a contract. Agency theory assumes that contracts can eliminate agency costs but in reality arise agency costs. The many imperfections in the market indicate that this assumption is invalid. Shareholders are assumed to only be interested in financial performance. Directors and management are assumed to have job responsibilities from shareholders. The board has a number of roles in making company policy. Most corporate governance research is conceptualized as a deterrent to managerial interests. Agency theory does not value agent competence.

Agency theory is the value of the economic system of capitalism (Zongning, 2017) because it eliminates the sense of human values such as: taste, intuition, spiritual, mutual trust, mutual respect, mutual trust and honesty. The context of agency theory including aim to be selfish, either by the principal or agent. Management behavior tends to benefit directors as controlling, this is because directors are part of management, and managers have been appointed and recruited by directors.

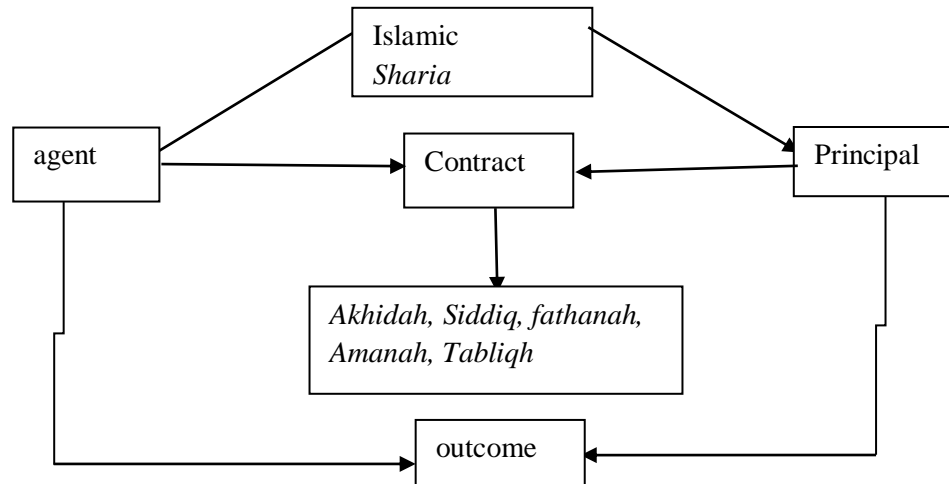
From the explanation above shows that the agency theory there are many problems that conflict with Islamic economics based on the Qur'an and Hadith. While criticism of the agency theory has been done by several studies such as Yusof (2016), Kultys (2016), Zongning (2017) and Kumalasari and Sudarma (2018) criticizing problems that occur between principals and agents. While there has been no research criticizing the agency theory based on the Islamic perspective. This is what drives us to study and criticize agency theory based on an Islamic perspective.

2. METHODOLOGY

In this study, we use secondary data as a source to find explanations of theoretical information that can be useful in discussing agency theory from an Islamic perspective. Secondary data obtained by reading the literature of Islamic sharia studies such as the Quran, hadith and *fiqh*. after studying and understanding Islamic studies in depth will result in discussion of agency theory criticism based on to Islamic perspective. Literature based on Islamic studies by studying at Islamic rules regarding agency theory so that a correct discussion can be taken about agency theory.

3. RESULTS AND ANALYSIS

Figure 1: Agency theory Islamic perspective



Based on table 1 above, Islamic Sharia as a guideline for Principals and Agents so that all actions and policies of principals and agents must be based on Islamic Sharia. The agent contract principles in an Islamic perspective are based on the ASIFAT concept, namely: *Akhidah* (obedience to *Allah Ta'ala*), *Shiddiq* (true), *Fathanah* (intelligent), *Amanah* (honest/trustworthy) and *Tabligh* (communicative). The principles of the contract are as follows:

a. *Akhidah*

Akhidah is a tool for Muslims to maintain their behavior in principal and agent contracts. Obeying *Allah Taa'la* will always guard his actions from things that are forbidden by sharia. This *Akhidah* appears in two main principles, namely:

1. *Allah Taa'la* is the owner of the world and all of its contents and only *Allah Taa'la* governs everything according to what He wants. In the work, humans are the holder of the trust entrusted by *Allah Taa'la* for work that is actually wholly owned by *Allah Taa'la*.
2. Allah is the creator of all living things and all creatures only pray and obey all commands to *Allah Taa'la*.

b. *Shidiq*

Principals and agents must have the characteristics of *shidiq* who can be trusted and responsible. By the nature of *shidiq* the principal contract and the agent will be responsible for everything he does. Responsible for always protecting human rights and the rights of *Allah Taa'la* by not forgetting obligations as social people. Responsibility in Islam has a fundamentalist aspect, namely, first the status of the human *khalifah* is united with responsibility. a good *khalifah* always performs good deeds between the principal and the agent. Second, the responsibility of a *khalifah* is done voluntarily without coercion. If this concept is carried out in principle and agent contracts, then the workings are carried out in ways that are correct, fair and honest. The application of this behavior will not bring harm to the other party because the contract between principal and agent performs the morals according to Islamic sharia to always help and respect others.

c. Fathanah

Fathanah is an intelligence that includes intellectual, emotional and spiritual intelligence possessed by the principal and agent. Someone who has a *fathanah* attitude not only controls the field, but has a strong determination. Decisions made by principals and agents show a professional based on moral attitudes such as the character of the Prophet *Muhammad Rasulullah Shallallahu 'alaihiwasallam*. Principals and agents who are *fathanah* are not only intelligent, but also have wisdom in thinking and acting. In addition, the nature of *fathanah* makes himself an example because of his expertise and personality that is able to foster a comfortable and harmonious situation.

d. Amanah (honest/trustworthy)

Honest is the similarity between the news delivered with the facts. In the principal contract and honest agent is the most important value in the employment contract. This honesty is one of the reasons for making contracts that are carried out in accordance with Islamic sharia, which is the most fundamental of all relationships between principals and agents.

e. Tabligh

One of the roles of the *tabligh* attitude which is the character of the morality of the Messenger of Allah is to convey the truth through good character. Principal and agent contracts really require *tabligh* attitude to convey complete and honest information between the principal and agent.

Table 1: Schematic of agency theory Vs Islamic perspective

Theory element	Agency Theory	Islamic Perspective
Key idea	Principal-agent relationships should reflect efficient organization of information and risk-bearing costs	Principal- agents carry out the <i>amanah</i> to advance the company
Unit of analysis	Contract between principal and agent	Contract of cooperation between principal and agent
Human assumptions	Self interest, Bounded rationality, Risk aversion	help each other, keep the <i>amanah</i> and honest
Organizational assumptions	Partial goal conflict among participants, Efficiency as the effectiveness criterion, Information asymmetry between principal and agent	There is no organizational problem because the organization is based on the principle of <i>amanah</i> between the principal and agent
Information Assumption	Information as a purchasable commodity	Information to communicate, no as a purchasable commodity
Contracting problem	Agency (moral hazard and adverse selection), Risk sharing	There is no contracting problem because the agent is honest and <i>amanah</i>
Problem domain	Relationships in which the principal and agent have partly differing goals and risk preferences (e.g. compensation, regulation, leadership, impression management, whistleblowing, vertical integration, transfer pricing)	No problem domain because Allah Almighty supervised and guided by the Quran and Hadith

Schematic of Agency Theory above shows that there is a difference between agency theory and Islamic perspectives, especially the principal contract with the agent based on the trust contract and give good morals in carrying out the *amanah*. In the Islamic perspective they have to carry out the *amanah* in earnest and sincere to get the blessing of *Allah Taa'la* Almighty. Violating the *amanah* is an act that is moving towards treason and such a thing is a prohibited act of *Allah Taa'la*.

The verses that relate to the *amanah* is as follows:

1. *Allah Taa'la* Almighty tells us to deliver the *amanah*

- The first verse about the *amanah* is found in the word of *Allah Taa'la* in the letter *annisa* verse 58:

﴿إِنَّ اللَّهَ يَأْمُرُكُمْ أَنْ تُؤَدُّوا الْأَمَانَاتِ إِلَىٰ أَهْلِهَا وَإِذَا حَكَمْتُمْ بَيْنَ النَّاسِ أَنْ تَحْكُمُوا بِالْعَدْلِ إِنَّ اللَّهَ نِعِمَّا يَعِظُكُمْ بِهِ إِنَّ اللَّهَ كَانَ سَمِيعًا

Lo! Allah commandant you that ye restore deposits to their owners, and, if ye judge between mankind, that ye judge justly. Lo! comely is this which Allah admonisheth you. Lo! Allah is ever Hearer, Seer.

Ibnu Kathir said in the interpretation of this verse, "Allah Ta'ala preached that He commanded to carry out the *amanah* to the experts. In the hasan hadeeth of Samurah that the Prophet *Muhammad Rasulullah Shallallahu 'alaihiwasallam* said.

أَذِ الْأَمَانَةَ إِلَىٰ مَنْ اتَّعَمَكَ وَلَا تَخُنْ مَنْ خَانَكَ

"Convey the mandate to those who give the *amanah* to you, and do not betray those who betray you" (Narrated by Imam Ahmad and Ahlussunnan).

This includes all forms of *amanah* that are *amanah* for humans starting from the rights of Allah Ta'ala on His servants such as: prayer, *zakat*, fasting, kaffarat, vows and so forth. Where he is mandated and no servant knows about it, to the rights of his fellow servants, such as; entrusted goods and so forth from what they are safe without knowing the existence of evidence of that. So Allah Ta'ala commands to fulfill it, whoever does not fulfill it in the world is taken from him on the Day of Judgment. "

2. *Allah Ta'ala* asks us to maintain the *amanah*

The second verse about the mandate is found in surah al-believer verse 8 and surah al-ma' arij verse 32:

Al-Mu'minun verse 8

وَالَّذِينَ هُمْ لِأَمْتِهِمْ وَعَهْدِهِمْ رُءُوفُونَ

And who are shepherds of their pledge and their covenant

Ibnu Kathir said, "That is, if they are given the trust they do not betray, and if they promise not to be absent, these are the qualities of the believer and his opponents are the characteristics of the hypocrite, as stated in the authentic hadith.

إِذَا حَدَّثَ كَذَبًا، وَإِذَا وَعَدَ أَخْلَفَ، وَإِذَا أُؤْتِمِنَ خَانَ: آيَةُ الْمُنَافِقِ ثَلَاثٌ

"There are three hypocritical signs: when speaking of lies, if he promises to be turned away and if given the message he betrayed".

Al-Ma'arij verse 32

وَالَّذِينَ هُمْ لِأَمْتِهِمْ وَعَهْدِهِمْ رُغُونَ

And those who keep their pledges and their covenant

3. Allah Taa'la explains the mandate that we must carry while in the world

The third verse about the *amanah* is contained in surah al-ahzab verse 72:

إِنَّا عَرَضْنَا الْأَمَانَةَ عَلَى السَّمَوَاتِ وَالْأَرْضِ وَالْجِبَالِ فَأَبَيْنَ أَنْ يَحْمِلْنَهَا وَأَشْفَقْنَ مِنْهَا وَحَمَلَهَا الْإِنْسَانُ إِنَّهُ كَانَ ظَلُومًا جَهُولًا

Lo! We offered the trust unto the heavens and the earth and the hills, but they shrank from bearing it and were afraid of it. And man assumed it. Lo! he hath proved a tyrant and a fool.

Ibnu Kathir said after stating his opinions about the interpretation of the *amanah*, including obedience, obligation, din (religion), and the laws of *had*, he said, "And all these opinions are not in conflict with each other, in fact they are appropriate and return to one meaning, namely *at-taklif* and accept orders and prohibitions on their terms. And if you do it he gets reward, if you leave him punished, then humans accept it with weakness, ignorance, and tyranny except those who are given *taufik* by Allah Taa'la, and only to Allah where to ask for help".

4. Allah Taa'la talks about us who betrayed the trust

There is the word of Quran surah al-Anfal verse 27:

يَا أَيُّهَا الَّذِينَ آمَنُوا لَا تَخُونُوا اللَّهَ وَالرَّسُولَ وَتَخُونُوا أَمَانَاتِكُمْ وَأَنْتُمْ تَعْلَمُونَ

O ye who believe! Betray not Allah and His messenger, nor knowingly betray your trusts.

Ibnu Kathir said, "And betrayal includes the sins of small and large which are prevalent (which are not related to others) and *muta' addi* (which are related to others). Said Ali ibn Abi Talha from Ibn Abbas regarding the interpretation of this verse, "And you betrayed your messages". The *amanah* is the deeds *amanah* by Allah to His servants, namely *faridhah* (which is obligatory), Allah says: "Do not betray you" means: do not destroy it ". And in another narration

he said, "(Do not you betray Allah and the Prophet) Ibnu Abbas said," (Namely) by leaving his *sunnah* and acting on him".

While assumptions are needed for theories to be stingy and logical, they tend to be the main source for criticism among scholars and can potentially explain mixed empirical findings (Bosse&Phillips, 2016). By following these criticisms, then, emerging theories and alternative perspectives that need discussion. That is the perspective of Islam is considered a very important development. An overview of the different theories, along with an agent-principal agency theory is provided in Table 3.

Table 2: Comparison of agency theory and Islamic theoretical perspectives

	Principal-Agent Agency Theory	Islamic perspective
Theoretical Foundations	Berle and Means (1932/2009) and Jensen and Meckling (1976)	Forthcoming <i>amanah</i> theory
Theoretical Orientation	Alignment of interests of agents and principals	Role assignment Agent and principal
Unit of Analysis	Agent-Principal	Agent-Principal
	Self-serving	Collective serving
Model of Man Behavior	Rational	Following the nature and character of the Prophet <i>Muhammad Rasulallah Shallallahu 'alaihiwasallam</i>
	Individualistic	Cooperation agent and principal
Agent Motivation	Extrinsic	<i>Amanah</i> and worship
Identification	Low-value commitment	High commitment
Power	Institutional	Islamic Sharia
Key Mechanisms	Monitoring and incentive-based contracts	Autonomy and <i>amanah</i> -based contracts

3.1 Conclusion

Agency theory is the value of the economic system of capitalism because it removes the values of human taste such as: taste, intuition, spiritual, mutual help, mutual respect, mutual trust and honesty. The agency theory context includes aiming to be selfish, both by principals and agents. The purpose of this paper is to examine and criticize agency theory based on an Islamic perspective. Following these various criticisms, then, alternative theories and perspectives have emerged that warrant discussion. Namely Islamic perspective is considered very important developments. An overview of these different theories, along with principal-agent agency theory. Schematic of Agency Theory shows that there is a difference between agency theory and Islamic perspectives, especially the principal contract with the agent based on the trust contract and give good morals in carrying out the *amanah*. In the Islamic perspective they have to carry out the *amanah* in earnest and sincere to get the blessing of *Allah Taa'la* Almighty. Violating the *amanah* is an act that is moving towards treason and such a thing is a prohibited act of *Allah Taa'la*. Breaking the *amanah* is an act that leads to treason and this is an act of sin that is prohibited by *Allah Taa'la*.

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