

# *Achieving Maqasid al Shariah through Takaful*

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## 1. MAQASID E SHARIAH

### The Objectives of Shari'ah

Many jurists have tried to explain the aims and objectives of Shari'ah upon which it is established. Among these the outstanding figures are the Malikite Abu Ishaq al-Shatibi, the Shafite al-'Izz ibn 'Abd al-Salam, and the Hanbalite Ibn Qayyim al-Jawziyyah.

#### 1.1. *Definition of Maqasid Al-Shari'ah*

Maqasid al-Shari'ah that is, the objectives of Shari'ah can be defined as below:

- Maqasid al-Shari'ah comprises those benefits/welfare/advantages for which Allah has revealed His Shari'ah.
- Maqasid al-Shari'ah aims at the attainment of good, welfare, advantage, benefits, etcetera, and warding off evil, injury, loss, etcetera, for the creatures. (All this in Arabic terminology can be stated as Masalih al-'Ibad.)

Shari'ah aims at the welfare of the people in this life and in the life hereafter, and for this purpose it has advised the people to adopt such means and measures suggested by it (Shari'ah) as may result in advantage benefit/well-being to them and may ward off evil/injury/loss, etcetera, from them, not only in this world but also in the world hereafter. Same is the philosophy behind His commands and the worships prescribed for His creatures.

#### 1.2. *Classification of Maqasid Al-Shari'ah*

Provisions of Shari'ah aim at protecting its objectives. Objectives or Maqasid al-Shari'ah can be classified as under:

- Daruriyyah
- Hajiyyah

- Tahsiniyyah

### 1.2.1. Daruriyyah (Necessities)

These are the objectives which are must and basic for the establishment of welfare in this world and the world hereafter in the sense that if they are ignored then the coherence and order cannot be established and fasad (chaos and disorder) will prevail in this world and there will be obvious loss (al-khursan al-mubin) in the world hereafter.

*Daruriyyah relates to five things:*

1. Protection of Faith (Din)
2. Protection of Life (Nafs)
3. Protection of Posterity (Nasl)
4. Protection of Property (Mal)
5. Protection of Reason ('Aql)

According to Shatibi, these five protections are daruriyyah for the establishment of welfare in this world as well as in the world hereafter. The protection of the above mentioned elements can be made possible through two types of essential elements.

- a. Necessities required for bringing into and maintaining the very existence of the above mentioned elements, that is: din, nafs, nasi, mal, 'aql, etcetera.
- b. Necessities required for protecting these elements from their destruction. The worships ('ibadah) for example, aim at maintaining the very existence of faith.

Iman (attestations in words and intention), salah, zakah, fasting and hajj are the elements that are required for the maintenance of the very existence of faith (din). All such provisions of Shari'ah are said to have the aims that can be labeled as daruriyyah.

Similarly, the permission to benefit from drinkables, clothing, housing, etcetera, is meant to maintain life and hence fulfill the objective of necessities. Such matters and dealings that are required to maintain and protect the existence of property, reason and posterity also promote necessities from the point of view of bringing these into existence. On the other hand, such dealings or legal provisions (jinayat), which are required to stop destruction of the above mentioned elements will also be said to aim at daruriyyah from the point of view of the objectives of Shari'ah.

### **1.2.2. Hajjiyyat (Requirements)**

Shari'ah aims at facilitating life or removing hardships. All such provisions of Shari'ah which aim at facilitating life, removing hardship, etcetera, are said to fulfill the hajiyyah (requirements). For example, permission of hunting and use of halal goods for food, lodging, and conveyance, etcetera. Besides, the permission for qirad (profit sharing through borrowing), musaqat (profit sharing), bai salam (forward buying of a commodity which does not yet exist), which are apparently illegal interest bearing dealings, are the examples of Shari'ah provisions that aim at facilitating life or removing hardships in the life in this world. The exploitative, usurious and doubtful dealings and contracts have also been forbidden for the same purpose.

### **1.2.3. Tahsiniyyat (Beautification)**

Shari'ah beautifies life and puts comforts into it. There are several provisions of Shari'ah which are meant to ensure better utilization, beautification and simplification of daruriyyah and hajiyyah. For example, permission to use beautiful, comfortable things; to eat delicious food; to have cold drinks and juices; to wear fine clothing and so on.

## **2. Shari'ah Approves of Good and Forbids Bad:**

### **Appreciates Ease and Shuns Unnecessary Hardships**

Allah has created both "good" and "bad". Good results in goodness of man, and bad yields badness for him. Good leads to Allah's pleasure and bad leads to His anger. Man has been enjoined upon to do good and avoid bad for seeking Allah's pleasure, but he has been advised to adopt ease and shun unnecessary things for this purpose. Allah has not put any obligation upon man which is beyond his scope. Says the Holy Qur'an: Allah does not take a soul beyond his scope.

"He hath chosen you and hath not laid upon you in religion any hardship. The Holy Qur'an has stated one of the purposes of the prophecy of the Prophet (SAW) in these words: "He will enjoin upon them which are right and forbid them which is wrong. He will make lawful for them all good things and prohibit for them all the bad things; and He will relieve them of their burden and the fetters that they used to wear (7:157)

The Prophet (SAW) says, "Religion is focality. The most beloved religion to Allah is tolerant orthodoxy".

The same principle is applicable to man's economic activities, and for the maintenance of his economic needs. He has been asked to meet his need by the virtue of his labor, but to adopt such means as are easy and lawful, and not to adopt even such lawful means (for this purpose) that exhaust him. He is obliged to satisfy his hunger with halal meals and not to eat haram ones, (but in idtirar when any halal thing is not available, he is permitted to eat dead body or what is not properly slaughtered) and other unlawful things. This is in accordance with Shari'ah maxim that:

"necessity (darurah) renders prohibited things permissible".

The examples which illustrate the application of this norm are numerous. Leniency with a debtor, who is in financial strait, is an example of this principle. If the inability of a debtor to pay his debt is established, payment by installments may be permitted. "And if the debtor is in straitened circumstances then let there be postponement to the time of ease." (2:280)

(Although necessity renders prohibited things permissible yet this rule is not absolute but it is limited by the text, by the extent of the necessity and by the time of the necessity.)

### **3. Aims of Shari'ah Unchangeable**

The aims and objectives of Shari'ah are everlasting and unchangeable. They are set by Allah and their application or interpretation is not left to the sweet will of any person or class. These aims relate to both the worldly life and the life hereafter; and to take them only for the worldly benefits at the cost of the hereafter life's benefits is prohibited and condemned. However, Shari'ah is considerate in case of darurah (necessity) and hardships.

Shari'ah has set priority order for the worldly and religious affairs and the people have been enjoined upon to follow this priority order, and they are not allowed to apply their whims while following either of the two. Shari'ah has prohibited the use of some goods as well as the indulgence in certain economic activities, though sometimes or even always their use or practice may yield economic fruits or progress. Similarly Shari'ah has permitted and sometimes required the use of certain things or the initiative of certain economic activities, though apparently they do not yield such fruits as the prohibited things do. The philosophy behind the permission or prohibition of certain goods or economic activities is known to Allah (SWT). However, some of its parts have been revealed by Him and explained by The Prophet (SAW). In all such commandments, Shari'ah ensures ease and it has permitted the ease of unlawful and prohibited goods and activities in case of necessity (darurah). In this connection, in addition to the verses quoted earlier, the following references are note-worthy: "Allah desireth for you ease; He does not desireth hardship for you." (2:158)

"Allah would make the burden light for you, for man was created weak." (4:28)

The Prophet (SAW) says: "I have been sent with easy and practicable Shari'ah."

The examples of such ease are found in the permission of ijara (leasing and hiring) and salam sale (that is, sale of a commodity which is to be produced in future) and in the permission of qirad (profit sharing through borrowing) and musaqat (fruit sharing).

Shari'ah never demands its followers to undergo unnecessary hardships and difficulties in performing religious obligations and other noble deeds. However, every difficulty or hardship in Shari'ah yields worldly gains (sooner or later) or the pleasure of Allah.

A person himself should not intend to undergo unnecessary hardship in performance of any noble deed or economic activity. However, if he is put in the same, or he willingly wants to do so to seek Allah's pleasure, he shall be rewarded.

Shari'ah has discouraged the observance of rahbaniyyah, monasticism), and has appreciated the lawful earning for the maintenance of oneself and the family, and preventing oneself from begging for a living.

Shari'ah always stands for following the medium path in observing religious duties and worldly \_affairs. Allah (SWT) says, "They ask you what to spend (in way of Allah) say: What is surplus." (2:219)

Shari'ah permits and appreciates the use of lawful adornments; wearing fine dress; eating good food, etcetera, and discourages their abstinence. Says the Holy Quran: "Who has forbidden the adornment of Allah which He has brought forth for His bondsmen, and the good things of His provisions?" (7:32)

However, lust for these goods and consequently the worldly mindedness is condemned by Shari'ah. Says the Holy Qur'an: ((This life of the world is but a pastime and a game". (6:32) Says the Prophet (SAW): ((Love of world (wealth) is root of every evil."



### **Concept of *Takaful***

Although the word *takaful* does not appear in the *Qur'an*, it is derived from the term *Ta'awun*, or mutual assistance and connotes the same meaning. *Takaful* is a noun stemming from the Arabic verb "*Kafal*" meaning to take care of one's needs. *Takaful* simply means mutual help among a group i.e. each member of the group pools efforts to support the needy within the group. This is the same as mutual insurance (cooperative insurance) as was practiced in the early days of insurance and even today by certain groups. The concept of *takaful* had already existed during the time of Prophet Muhammad where the Muslims contributed to a fund under the tribal system of *Aaqilah* for the purpose of helping members of their own community who were liable to pay *diyat* (blood money).

*Takaful* is an Islamic insurance concept which is grounded in Islamic *muamalat* (banking transactions), observing the rules of *Shari'ah*. This concept has been practiced in various forms for over 1400 years. It originates from Arabic word *kafalah*, which means "guaranteeing each other" or "joint guarantee". In principle, the *takaful* system is based on mutual co-operation, responsibility, assurance, protection and assistance between groups of participants. It is a form of mutual insurance

*Takaful* involves each participant giving away as donation or *tabarru* a certain proportion of the full amount of the contributions (premium) required to be paid. The financial assistance paid to a participant facing a loss or damage is from a fund that is contributed by all participants by way of donation. After the *takaful* claims and benefits are paid, the remaining surplus is paid back to the participants. Thus, there is no element of gambling or unjust enrichment in this arrangement. As the defined fund belongs to the participants, the practice does not aim at deriving undue advantage at the expense of other individuals. Further, there is no excessive uncertainty or *gharar* with respect to the contribution and financial assistance.

*Takaful* policies allow the participants to enjoy the same level of cover provided by conventional insurance. Under the *takaful* system, the insured form a community based on the principles of co-operation, a form of mutual assistance and shared responsibilities of all members with a common interest; it attaches great significance to mutual support and solidarity. Contributions (premiums in the conventional term) by the *Takaful* policyholders/participants are paid into a common pool (Participants Takaful Fund) on the basis of a donation (*tabarru'*) to help and care for members of the community in times of need. In addition to this communal risk-sharing, surpluses are placed at the disposal of the members of community. Contributions are invested, through the Participants takaful Fund, according to strictly Islamic principles (interest is prohibited and sectors such as gambling or alcohol is excluded). Most of the profits are shared among the scheme members. In most cases, the *Takaful* company (known as the *Takaful* Operator) receives a fee or share of the investment income for managing the business that included underwriting the operations and investing the funds in accordance with *Shari'ah* principles.

### **3.1. Origin of Takaful (Islamic Insurance)**

The concept of Islamic insurance was broadly derived from the following practices that pre-dated Islam:

***Al Aaqilah***: A scheme where (a) the contributions from all tribal members were the participants in the scheme and, (b) the sharing amongst such participants of joint responsibility to indemnify the victim or the victim's family and relatives. Islam accepted this principle of reciprocal compensation and shared responsibility or mutual agreement or joint guarantee given between Arab tribes for securing of individuals or families against financial liability arising from a defined event such as the murder or injury of a member of one tribe by a member of another tribe.

***Diya*** (indemnity): The arrangement for the payment of "blood-money" to the next-of-kin or the injured party of a murder victim, where a sum of money was paid as compensation by a group of persons or the community on behalf of the

person. This is provided that the victim's family and relatives agree to accept the "blood money". It is not too different from the Western notion of paying compensation to victims.

When such an event occurred, "blood money" (*diyah*) would be payable to the family of relatives of the victim by members of the accused's tribe until the *diyah* was satisfied. The tribes would hence collectively share responsibility for sums individually owed and in this manner the financial burdens arising from unexpected but defined risks were spread amongst the whole tribe.

***Kafalah*** (guarantee or suretyship): Synonymous with *daman* (a contract of guarantee, security or collateral), whereby a third party guarantees the performance of another party involved in a contract. "This has been seen as commitment, comparable to the duty of insurer to pay the sum insured, as is the case of liability insurance". (Al Zarqa: 1962, p.27) Merchants of Makkah formed funds to assist victims of natural disasters or hazards of trade journeys. Surety called *daman Kkhatar Al-Taiq* was placed on traders against losses suffered during a journey due to hazards on trade routes. Early precursors were developed in response to perils and risks associated with long-distance trade via caravans or sea voyage.

***Aqd muwalat***, known as contract: These were entered into for bringing about an end to mutual enmity or revenge.

***Ju'hala***: The contract in which, a person promises to reward another unspecified person in exchange for carrying out a specific work for him, in spite of the considerable amount of uncertainty involved in it. (Khorshid: 2004, p. 23)

***Daman Kkhatar Al-Taiq*** (*guarantee against travel hazards*): Where a person secures a sum of money with another person before embarking on a journey. If a traveller suffers any loss during travel that money would compensate him. This is closer to modern time insurance where there are only insurer and insured. (Vardit: 1985, p.144)

**Hilf** Confederation were brought about by means of an agreement for mutual assistance among people

The pre-Islamic Arab tribes covered the losses and liabilities of individual members of a tribe in the form of mutual help. Each individual member's loss was considered to be the tribe's own liability through blood ties and settled collectively. This was to encourage mutual help in cases of tragedy and distress and share these losses collectively. The liability was to pay blood money to ease financial burden on family of the person suffering the loss. [Insurance, in general, has also been compared to *diya* whereby a sum of money paid as compensation by a group of people on behalf of a person who has killed someone. The family or relatives of the victim has the

right to require that the person's *aaqilah* pay the *diya* on his or her behalf. It has similarity like in the case where an insured person's family or relatives have the right to claim money from an insurance company]

The system of *Aaqilah* in Arabia was developed from the above practice. This is a system of shared responsibility in the form of subrogation (blood money or *diyah*) and financial compensation for bodily injury (*arsh*). It was practiced between the Muslims of Makkah (the *muhajreen*) and the Muslims of Madinah (the *ansar*). The system was accepted into Islamic practice based on a verdict of Prophet Muhammad. One day in a quarrel between two women of the Huzail tribe, one of them, an expectant mother, was killed by the other. The Prophet declared that her kin (*Aaqilah*) had to pay a penalty to the relatives of the woman who had died. *Aaqilah* system is a classic representation of joint guarantee by a group of people to help each other in the event of mishaps. This is in line with the Islamic principles of mutual help and cooperation in good and virtuous acts. The Holy *Qur'an* gives us the

essence of this principle:

"*Help ye one another in righteousness and piety ...*" [5:2]

Professor of Islamic law, Muhammad Ata al-Sid (International Islamic University Malaysia,) has commented on the system of *Aaqilah*: "The Prophet intended the *Aaqilah* concept, which has been known since the *jahiliyyah* [pre-Islamic] times, to be an exception to the general rule because of the cooperation and benevolence contained in it as Allah commanded. This signifies the legality of the co-operative principles such as of insurance that serves an important role in the social, psychological and economic welfare of individuals and societies".

Islam promotes the essence of peace, economic well-being and development of people at all levels, of individuals, family, society and the state. To implement this in our lives, Islam calls for the protection of certain basic rights. These are:

1. The right to protect religion (belief)
2. The right to protect life
3. The right to protect dignity and honour
4. The right to protect property
5. The right to protect the mind and talent

These basic rights operate at three levels of *maslahah* (welfare codes). These are, in order of priority

1. *Darura* (unavoidable necessities)
2. *Hajiyat* (general needs)
3. *Tahsinat* (to lead a decent life)

It is clear from this that the concept of insurance is well within the Islamic framework to protect life and property against mishap and misfortune, which ultimately helps in maintaining a decent life. The concepts of mutual protection amongst the Muslims took a firmer shape between the 7th and 13th centuries when Muslim traders embarked upon extensive trips by land and sea to India, China and the Islands of Malaysia, Sumatra and Java.

Financial protection was afforded through pooling of funds, which were used to compensate anyone who suffered losses through mishaps on these journeys. The historians and travellers of the time such as Marco Polo (1254-1354) and Ibn Batutah (1304-1368) brought about a fusion of ideas and information across continents. It is said that the interaction of Arab and Muslim traders and the Europeans was in fact what gave rise to the early marine insurance in Italy in the thirteenth century.

Whilst insurance of assets was reluctantly accepted, necessitated by financial prudence, greater resistance was shown towards personal lines, especially against life insurance. A combination of extended family system, misunderstanding of life "assurance" as guarantee for life and concepts of mutual social help indigenous to the Islamic culture created almost a stigma against life insurance. Such exogenous factors culminated in religious edicts over the years by leading Islamic scholars declaring and re-emphasising that conventional insurance was prohibited. This was reinforced in the first international conference in Makkah in 1976.

In Malaysia, the National Fatwa Committee also declared in 1972 that conventional life insurance was unacceptable as it was not in compliance with the Islamic principles as it contained elements of *gharar* (uncertainty), *maysir* (gambling), and *riba*.

### **3.2. Objective of Takaful**

The main objective of *takaful* is to diversify the risk among the members. In a practical sense, the main difference in this area between conventional insurance and *takaful* is that in insurance the Risk is transferred to the insurer while in *takaful* the Risk is shared mutually by the members of the common *Takaful* Fund under the *takaful* scheme.

*Takaful* can be visualised as a method of joint guarantee among participants against loss and damage that may be inflicted upon any of them (Fisher, 2002).

The members of the group agree to guarantee jointly that if any of them suffer a catastrophe, will receive a certain amount of money to meet the loss and damage.

Having an Islamic life insurance policy does not mean that one has insured one's own life, but it is a fair financial transaction catering for the benefits of certain helpless people in the society.

"It is necessary that the society should be protected by providing guarantee against 'Risk' (subsistence) for all individual constituting the fund-pooling institute. In the absence of such a guarantee, every one will suffer from the worries and anxieties. Insurance guarantee is similar to Keynesian precautionary motive of demand for money in certain respects" (Adams, 1998). Sustainance of such a guarantee is possible when there is equity, justice and economics balance in society. In case of

Takaful, every individual survive under the *kafalah* (guarantee or surety-ship) of the group. Takaful will provide cover to all entrepreneurs and individuals in the society against the spiritual and material losses. In primitive society, people lived together in form of families or tribe, where their needs were fully met and protected, through cooperation and mutual help. Consequently, they were fully protected against all sorts of loses. It was the old method of insurance.

*Takaful* aims to:

Support social solidarity.

Help protect the community from the negative impact of adverse circumstances.

Improve quality of life through the peace of mind that comes from security.

Save and invest money through a shared system that distributes profit on premiums (subscriptions/contributions) invested by policyholders on an annual basis.

### 3.3. *Basis of Takaful*

*"... a system based on solidarity, peace of mind and mutual protection which provides mutual financial and other forms of aid to Members {of the group} in case of specific need, whereby Members mutually agree to contribute monies to support this common goal." [O. Fisher]*

*"The basic fundamentals underlying the Takaful concept are very similar to cooperative and mutual principles, to the extent that the co-operative and mutual model is one that is accepted under Islamic Law."*

Notwithstanding the belief in God and *Qadha-o-Qadr* (the Divine Decree and the Will of God), The Holy *Qur'an* exhorts the individual to assist one another and to take precautions in order to minimise potential misfortune, losses or injury from unfortunate events. Although *takaful* has very old origins, the word *takaful* is a modern day usage. There references to sharing of risk and mutuality in The Holy *Qur'an* and the Hadith (record of the teachings and sayings of Prophet Muhammad pbuh) however, *takaful*, the way it is transacted today, is based on the secondary source of Islamic jurisprudence – *Ijtihad* (the process of making a decision by independent interpretation of the legal sources, The Holy *Qur'an* and the *Sunnah* - the traditions and practices of Prophet Muhammad).

The basis of the *Takaful* System is not to profit but to uphold the principle of "bear ye one another's burden." Therefore, the characteristic feature of Islamic insurance is that it is not based on profit making motive self-help through cooperation. Mutual assistance amongst members of a tribe was not originally a commercial transaction and contained no profit or gain at the expense of others. Rather, it evolved as a social institution: to mitigate the burden of an individual by dividing it among his fellow members (group persons) or tribe. In contrast, most modern insurance (even mutual stock insurance entities, but not mutual associations) is a capitalist-based commercial enterprise, where losses are projected in advance and funds (premiums) allocated to risks to cover them. Premiums are paid in line with such projections of risk.



*"Indeed, the basic difference between the Islamic and conventional conceptions of insurance is one of perspective, not economics. From a conventional perspective, insurance appears as set of bilateral contracts that transfer risk for the benefit of the individuals who choose to make that contract. From an Islamic perspective, however, insurance appears as an institution that reduces or eliminates risk for the benefit of social group. Importantly, the institutions that result from either the conventional or Islamic conception can also be described within the framework of the other: an Islamic insurance company is an institution that individuals use to shed risk, just as a conventional company is a way that a group shares risk". (Vogel & Hays 1998, p152) Some examples of the basis that are mentioned in The Holy Qur'an and the Hadith are:*

### **3.3.1. Basis of Co-operation:**

*"Help ye one another in righteousness and piety ... "* [The Qur'an 5:2]

*"Allah will always help His servant for as long as he helps others."* (Narrated by Islamic scholar Abu Daud: 817-888)

### **3.3.2. Basis of Shared Responsibility:**

*The place of relationships and feelings of people with faith, between each other, is just like the body; when one of its parts is afflicted with pain, then the rest of the body will be affected (narrated by Islamic scholars Bukhari 810-870 and Muslim Ibn al- Hajjaj .821-875)*

### **3.3.3. Basis of Mutual Protection:**

*Nobody will enter Paradise if he does not protect his neighbour who is in distress. (Narrated by Islamic scholar Ahmad bin Hanbal -780 - 855)*

It is important to emphasise that all economic activity including the fundamental *Shari'ah* principles governing contracts in general must conform to the *Shari'ah*. These include:

1. The subject matter of the contract should not be unlawful in Islam.

2. The intended objectives of the contract should not be contradictory to principles of the *Shari'ah*.
3. The contract should be free from the following elements:
  - (i) *Maysir/Qimar* (Gambling),
  - (ii) *Gharar* (absolute or high degree of uncertainty),
  - (iii) *Ghaban-e-Fāhish* (Exploitative, Exorbitant price or rate of profit)
  - (iv) *Ikrah* (Coercion)
4. The participants to the contract agree co-operate actively for their common good.
5. Every participant the contract pays a contribution in order to help those who need assistance.
6. The contract should not aim at deriving undue advantage for one participant at the expense of the other participants.

### **3.4. Elements of Gharar, Maysir and Riba in Insurance Contracts**

As a single contract, insurance violates *riba* and *gharar* rules. One party pays cash premiums in return for the promise of the other party to pay a cash sum on the occurrence of a contingent future event. So viewed, it also resembles a bet (*maysir*). Moreover, most insurance companies invest their premiums in interest-bearing investments forbidden by the *Shari'ah* (Islamic Law and Finance: Frank E Vogel and Samuel L Hayes III, 2006).

#### **3.4.1. Gharar**

A contract must be free from excessive *gharar* or uncertainty. A major source of *gharar* is lack of knowledge or absence of adequate and accurate information. In the insurance context, *gharar* refers to unexpected loss, risk, hazard and unknown danger. At the time of contracting, the insurer does not know whether it will ever be called upon to pay claims under the policy, nor the size of such

claims, if any. Similarly the insured pays a premium (price) but does not know if any financial benefit will be received in future, nor the size of such benefit. If terms of a contract are uncertain, unclear or one-sided at the expense or detriment of the other party (to the contract) then it is unacceptable from a *Shari'ah* perspective. When a person seeks insurance cover it is not the amount of compensation received when something happens to the person or the person's property. What the person buys is peace of mind, a promise. This is the tangible result for the money paid. If something happens to the person or to the person's property, the person is compensated and the loss is redeemed. If nothing happens, the person is happier because the person does not have to contend with any misfortune. "Others argue that insurance is a hedging against risk through personal means rather than depending on the public services or family support, which may not be realized." [Anwar: 1994, p1317].

An element of *gharar* exists in any insurance contract and to a certain extent could be tolerated in a *takaful* contract (as *gharar-e-yasir* where *gharar* is greatly minimised and, therefore, acceptable from the *Shari'ah* standard). According to Islamic jurisprudence, the factor of uncertainty disqualifies a contract if:

- a) It is incorporated in a financial contract
- b) Its contractual effects may be substantial.
- c) It affects real contractual interests.
- d) There is no genuine need for such a contract.

The majority of Muslim jurists are of the opinion that the first three conditions hold good in the case of an insurance contract, but that the fourth has now become inoperative and inapplicable. This is because insurance is a genuine need to safeguard the economies and properties of both government corporate bodies and individuals. However to ensure that uncertainty does not disqualify an insurance contract, it is necessary that:

- a) The insurance cover is a genuine and essential need.

b) The interests of the insured can only be safeguarded through effecting insurance and in no other way.

c) The insurance is transacted on a co-operative basis.

The concept of co-operative principles is clearly explained in the *takaful* contract wording under which ownership of the premium is not with the insurance company. Instead it is jointly owned by participants who pay these premiums (as their contributions) to a *takaful* pool (the *takaful* fund). Returns from the pool are either the benefits payable under certain circumstances or as share of profits (or surplus) in proportion to individual's contribution. The participants' entitlement to share in *Takaful* profits is balanced by the possibilities of sharing any losses in the pool. This is essential in order to minimise *gharar* (the lop-sided condition favouring one party at the expense of other). Nevertheless, the loss sharing aspect is a last resort after other methods have been exhausted such as recourse to reserves and access to interest free loan from shareholders (called *qard hasan*) to correct the deficit. The last resort situation is in the shape of increase in price for future coverage rather than retrospective recovery for past losses.

### 3.4.2. Maysir

Gambling (*maysir or qimar*) is clearly forbidden under the *Shari'ah*. As far as insurance for profit-making is concerned, it is argued that the insurer effectively "bets" that the contingencies insured against will not occur. The fact that such "betting" is done scientifically with the use of statistical tables and probability distributions does not alter the situation. Most forms of modern day gambling do in fact make use of scientific tools of analysis. However, there are major differences between a game of gambling and insurance.

1. In a game of gambling, there is a conflict of interest between the players. Gambling games are zero-sum games. If a particular team wins a basket ball game, a gambler betting on its win will gain; but only at the cost of another gambler who bets on a defeat. Hence, such gambling has the potential of

bringing major conflicts, social discords in addition to bringing financial ruin to some parties. In insurance on the other hand, both parties – the insurer and the insured hope that the contingencies insured against will not occur.

2. Gambling generates risk that does not exist before one enters gambling, while the sole purpose of insurance is to reduce, minimize or eliminate risks that are inherently present. Therefore, the analogy between insurance and gambling may not be sound and indeed, insurance may be the opposite of gambling rather than being similar to it.

Conventional insurance seeks to draw a line of distinction between gambling and insurance with the requirement of “insurable interest”. This implies that the beneficiary in insurance (with the exception of life insurance), must have an insurable interest in the subject matter, or at least an expectation of acquiring such interest. While this avoids the possibility of using insurance as a device for gambling in the conventional sense, the scope of *maysir* (and *qimar*) in *Shariah* is much broader and includes any form of unjust enrichment of one party at the cost of another. The issue of unjust enrichment is very significant when the insurance business is organised as a stock corporation.

The stockholders gain by maximising the insurance surplus. The problem is considerably reduced in a mutual insurance company where policyholders themselves own the organisation. There is however, still a possibility of unjust enrichment within the group of policyholders, which needs to be carefully avoided or minimised.

Thus, the prime difference between gambling and insurance is the context of excess uncertainty and gains attached to it. Generally, gambling is an abrupt shift of the decision maker from states of certainty to more risky involvement in a lottery. On the other hand, Insurance deals with transfer mechanism in decision making process from the participation condition in lottery to a state of certainty, the lottery involved being in which there is at least one possible outcome with negative payoffs or zero sum game. Moreover, the insurance also restrict the

decision maker to greater possible cases of positive outcomes with positive payoffs.

### **The difference between Gambling and Insurance**

The two main principles are the prohibition of *Riba* and *Gharar* which refers to the selling of items having an uncertain existence or uncertain characteristics making the transaction risky and similar to gambling. It is therefore important to distinguish insurance from gambling.

Yusuf Ali, in his translation of The Holy *Qur'an*, comments on Sura Al-Baqara [2:219], "Insurance is not gambling, when conducted on business principles. Here the basis for calculation is statistics on a large scale, from which mere chance is eliminated. The insurers charge premium in proportion to the risks, exactly and scientifically calculated". In gambling, it is possible to win or lose by creating that risk. In insurance, the risk is already there and the aim is to try to minimise the financial effects of that risk. Insurance shifts the impact of that risk to someone else and relieves the person of risk. *Gharar* includes gambling (*maysir*) as well as all forms of business in which monetary gain comes from mere chance, speculation and conjecture and not from work. Three main differences distinguish between a gambling contract and an Insurance contract is:

Although the argument on the differences between gambling and insurance was understood to some extent but Islamic scholars maintained that due to *gharar* (uncertainty of terms) an element of *maysir* existed. This was related to the fact that a small amount of premium secured a large amount of sum insured, only payable if certain event took place. If it didn't, the contributor lost the premium. On the other hand, the Insurance Company stood to lose out if total claims exceeded total premiums. It was also maintained that, in case of life assurance, upon happening of the event, the insured (or his or her beneficiaries) did not know how this amount of sum insured was generated from a small premium paid.

These areas are taken care of through the co-operative principles of Islamic insurance. Under this, the “large amount in proportion to the premium paid” comes out of a fund that is collectively owned by the participants. They had agreed at the time of joining, to give up their individual rights to help each other at the time of need (the insured peril). Alternatively they do not lose out if the insured peril did not occur within the agreed time period, as they are rewarded for their willingness to help each other through the mechanism of profit sharing.

### 3.4.3. Riba

*Riba* which is prohibited in the *Shari’ah* refers to transactions involving unequal exchange of the same thing and also refers to income derived from interest gained from investment and lending. In conventional insurance, the money paid in premiums is never equals to the money received in compensation.

*“The insured received less or nothing, as the case may be, in exchange of the premium when (1) he removes the policy, (2) fail to pay on premiums, (3) does not experience peril deserving compensation. Furthermore received payment against the insurance may be far greater than premium if a hazard strikes. So riba accrues to the insured if the compensation is more than the premiums, and so to the insurance when compensation falls short of premium. As a result insurance contract, Interpreted as exchange of money, cannot be free from riba. Another reason that the insurance premium is invested by insurer in interest-bearing securities”. (Anwar, 1994, p.1321).*

*When the insurance contract is seen as sarf (that is sale of monetary value for monetary value), the difference between the premium paid and the sum insured cannot but be described as riba as insured may receive a sum exceeding by far the instalments that he paid (Dasuqi: 1967 p.177)*

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