The Islamic perspective on insurance:

To determine the Islamic view on insurance let us first understand how insurance works by looking at the simple example below:

Mr Rich buys the latest model of BMW and gets it insured with Dodgy Insurance. As per the terms of the agreement, Mr Rich will pay Dodgy Insurance a yearly premium in return for a promise that if the car is stolen or damaged in an accident, Dodgy Insurance will pay Mr Rich for the loss. From the above example we can tell that insurance is a contract, as it involves offer and acceptance between two parties, the insurer (Dodgy Insurance) and the insured (Mr Rich). Therefore, to be allowed in Islam it must meet the criteria laid down by the Shari’ah for allowable contracts.

In Islam, a contract has to be concluded over either:

1. An object, where the object is exchanged for some compensation (e.g. selling, trading), or given away without compensation (e.g. gifts), or,
2. A benefit, where the benefit is provided for some compensation (e.g. leasing), or without compensation (e.g. loans).

If we carefully consider the insurance contract, we will find that the contract is neither over an object, nor a benefit. Rather, the contract is concluded over a promise. For example, in the scenario mentioned previously, Mr Rich was paying a premium to Dodgy Insurance merely for the promise by the latter to compensate him should the new BMW be stolen or damaged in an accident. The guarantee in itself carries no benefit, because Mr Rich would still have to pay the premium to Dodgy Insurance even if nothing ever happened to his car. Therefore, the insurance contract contradicts the Shari’ah.

Also, as Dodgy Insurance has promised to compensate Mr Rich for any damage to the car, the insurance contract can be considered a form of guarantee. Once again, we need to use the Islamic yardstick to assess whether the insurance contract is a legitimate form of guarantee. The Shar’ah requirements of a valid guarantee can be derived from the following Hadith:

Abu Dawud narrated from Jabir who said: “The Prophet (saw) would not pray over any person who died while indebted. A dead man was brought. He (saw) said: ‘Is he indebted?’ They said: ‘Yes, two dinars.’ He (saw) said: ‘Pray for your companion.’ Abu Qatadah al-Ansari said: ‘O Messenger of Allah, they are upon me.’ The Messenger of Allah (saw) then prayed over him. From the above Hadith, we can say that a valid guarantee in Islam has the following characteristics:

1. There must exist an immediate or potential financial liability on someone for which the guarantee is made.
2. There must exist a guarantor, a person guaranteed for and a guaranteed person. For example, in the Hadith, the guarantor was Abu Qatadah (may Allah be pleased with him), the person guaranteed for was the deceased, and the guaranteed person was the one who had lent the money to the deceased.
3. The guarantor takes responsibility of the financial liability of the person guaranteed for.
4. The guarantee is made without any compensation being charged by the guarantor.
5. The person guaranteed for and the guaranteed person need not be known at the time of making the guarantee.

Using the above criteria to judge insurance contracts, we’ll find that the insurance contract contradicts a valid Shar’a guarantee in the following ways:

1. In an insurance contract, generally the guarantee is made without the existence of an actual financial liability on anyone, whether immediate or potential. Therefore, there does not exist a person guaranteed for, rather only the guarantor (the insurance company) and the guaranteed (the insured). For example, if Mr Rich accidentally hits his expensive BMW against a pole on the street, Dodgy Insurance would reimburse him the cost of repair as per the contract. However, Dodgy Insurance’s promise to pay for the damage was not made on behalf of someone who actually or potentially owed Mr Rich money for the damage. Therefore, the person guaranteed for does not exist.

2. Besides, an insurance contract requires the insured to pay a premium, whereas, in Islam, no remuneration or compensation is charged in return for a guarantee.

Considering the above points, we can see that insurance is void as a contract and also as a guarantee according to the Shari’ah, and therefore not permitted in Islam.  
Reference:  
The Economic System of Islam by Taqi ud-deen an-Nabhani
Q). What’s Islam's stance on insurance?

Insurance is a controversial issue among Muslim jurists. I go along with the view that sees it permissible with conditions. As a contract, it is a relatively new contract that in itself does not violate any Shari`ah principle.

Hence, the conditions are: It must not be interest-based, and the object of insurance must be permissible. These two conditions are satisfied in house, health, car, and most life insurance contracts. The only problem comes in some kinds of life insurance contracts whereby interest is in the core of the contract (what is known as whole life insurance, which is the most common any way). It also comes in insuring certain prohibited things such as insuring a shipment of liquor.

On the other hand, there are scholars who argue that the insurance contract contains a great deal of gharar (Arabic for: due uncertainty) that makes the contract invalid. These argue that this gharar shall be forsaken if we change the structure of the insurance contract in question, making it a cooperative that receives premiums as donations. Based on this argument, Islamic insurance companies are founded.

When such companies are available, it is of course better to deal with them because they are acceptable by all. They also offer another benefit that it invests only in ways that are permissible in Shari`ah.

Q2). What do Muslims believe about insurance? Is it acceptable in Islam to take out health insurance, life insurance, car insurance, etc.? Are there Islamic alternatives to conventional insurance programs? Would Muslims seek a religious exemption if the purchase of insurance were required by law?

Answer: Under common interpretations of Islamic law, conventional insurance is forbidden in Islam. Many scholars criticize the system of conventional insurance as exploitative and unjust. They point out that paying money for something, with no guarantee of benefit, involves high ambiguity and risk. One pays into the program, but may or may not need to receive compensation from the program, which could be considered a form of gambling. The insured always seems to lose while the insurance companies get richer and charge higher premiums.

However, many of these same scholars take into consideration the circumstances. For those living in non-Islamic countries, who are mandated to abide by insurance law, there is no sin in complying with the local law. Sheikh Al-Munajjid advises Muslims about what to do in such a situation: "If you are forced to take out insurance and there is an accident, it is permissible for you to take from the insurance company the same amount as the payments you have made, but you should not take any more than that. If they force you to take it then you should donate it to charity."

In countries with exhorbitant health care costs, one could argue that compassion for those who are ill takes precedence over a dislike of health insurance. A Muslim has a duty to ensure that people who are ill can access affordable health care. For example, several prominent American
Muslim organizations supported President Obama's 2010 health care reform proposal, under the belief that access to affordable health care is a fundamental human right.

In Muslim-majority countries, and in some non-Muslim countries, there is often an alternative to insurance available, called takaful. It is based on a cooperative, shared-risk model.
The question of insurance is a major concern of contemporary Islamic jurisprudence. Insurance is an important part of the modern business environment and it plays a vital role in today’s economy. In some cases, people are required by law to take out insurance of one form or another. Many countries make owning automobile insurance a precondition for owning a driver’s license or subscribing to group health insurance a precondition from being allowed to employ others. Financiers often will not loan money unless the property being used as collateral for the loan is insured against loss.

Moreover, people can see that there are clear and undeniable benefits to be had from taking out an insurance policy. An insurance policy provides its holder with a measure of financial security. If a person has health insurance, he can be reasonably confident that medical care will be available to him. If a person has homeowner’s insurance, he is very likely not to be homeless if his house burns down.

For these reasons, Muslims are naturally quite concerned about the permissibility of this kind of business and to what extent they can participate in it. It is one of the most extensively discussed of contemporary issues in Islamic Law and at the same time one of the issues that is most often misunderstood by the general Muslim public.

The purpose of this article is to dispel the commonly held misunderstandings surrounding this issue and to explain exactly why Islamic Law has so many difficulties with commercial insurance. In order to do this, it is necessary to have a correct understanding of what commercial insurance is.

What is Commercial Insurance?

An insurance policy is essentially a contract between two parties whereby one party (the policyholder) pays a fixed premium to another (the insurer) in return for the insurer bearing full or partial responsibility for possible financial losses incurred by the policyholder.

There are many different types of insurance policies. There is life insurance. This is where a person pays a fixed premium to an insurer so that in the event of the death of the person insured, a predetermined sum of money will be paid by the insurer to a stated beneficiary or beneficiaries, who are usually the dependents of the insured party.

There is health insurance, whereby the policyholder pays a fixed premium to an insurer so that the insurer will bear fully or partially the medical costs incurred by those covered by the policy.

There is liability insurance. The policyholder pays a fixed premium to an insurer who agrees to bear the full or partial costs of any losses incurred by the policyholder on account of legal liability.

Other forms of insurance can be taken out against the destruction, theft, or loss of specified property.
All insurance policies share in there being a payment of a fixed sum of money to a party in lieu of that party assuming responsibility for a financial loss that may or may not take place and that may or may not exceed the amount that was paid.

Clarifying Some Misunderstandings

Some people have tried to compare insurance to the practice of al-’āqilah. This is where the tribe of a person found guilty of murder or manslaughter is held collectively liable to pay the blood money to the victim’s next of kin. This is very different from the insurance that we are discussing. This is purely an issue of legal accountability and is not a commercial contract between two parties.

Another common misconception that people often have is to assume that insurance is prohibited in Islam because it somehow compromises a person’s faith and his reliance on Allah. They allege that by taking out an insurance policy, the policyholder is displacing his trust in Allah and instead relying on the insurance company.

This argument is not sustainable. As Muslims, we are commanded to consider natural causes and to take necessary precautions. This in no way compromises our reliance on Allah. We know that our providence comes from Allah. However, we must still go out to work and earn a living. We do so relying upon Allah, by His grace, to provide for us from the fruits of our labor.

We are commanded by our religion to take precautions against loss. Anas ibn Mâlik reported that one day a Bedouin riding a camel came to the Prophet (peace be upon him) and asked him: “Can I leave the camel alone and trust in Allah?” The Prophet (peace be upon him) replied: “Tie your camel first, then put your trust in Allah.” [Sunan al-Tirmidhî]

The issue with insurance is not a matter of a person’s reliance on Allah. It is purely a matter of Islamic commercial law. And this is where the problems arise.

Commercial Insurance in Light of Islamic Commercial Law

Islamic Law prohibits business transactions that include a great deal of uncertainty. For example, I cannot sell you an unspecified quantity of peanuts for a fixed amount of money. The amount of peanuts must be specified. I cannot sell you a car for a certain sum of money without the make and model of the car being agreed upon beforehand.

There are many authentic hadîth in this regard. For instance, Abû Hurayrah relates that Allah’s Messenger (peace be upon him) forbade business transactions determined by the throw of a stone and business transactions involving uncertainty. [Sahîh Muslim]

Insurance is the sale of uncertainty itself. This is the strongest reason for its prohibition, since insurance is effectively the sale of a commodity that Islamic Law does not recognize as saleable. You pay the company to assume some matter of uncertainty in your life on your behalf. In life insurance, for example, you pay a fixed premium each month – say $200 – under an agreement that if you die, the company will pay out – say $75,000. If you die in one month, then the
company has to pay you $75,000. If you live for forty years, you will have to pay them $96,000. If at that point you fail to continue to make your payments, your policy is cancelled and you get nothing back. Why is this? It is because you received for your $96,000 the benefit of their assuming your risk for you for those forty years. So you received, according to law, the commodity that you paid for during all those years and the company owes you nothing more.

There are other problematic areas with respect to insurance, though these are far less important than the one just mentioned. In many instances, insurance resembles a type of prohibited interest (ribâ al-fadl), where two parties exchange the same commodity – gold, silver, dates, etc – in unequal quantities. Taking another look at our life insurance example above, assuming that you were to die one month into your policy, this would mean that you paid them $200 dollars and they paid you $75,000. Since Islam does not recognize the assumption of uncertainty as a salable item, this becomes an example of exchanging a like commodity (money in this case) in an unequal manner.

Another problem with insurance is that it bears some resemblance to gambling. This comes as a consequence of the uncertainty inherent to the business of insurance. Insurance premiums are set based on the percentage chance that the individual policyholders will collect from their insurance. The company makes its profits by receiving more money from its customers than it pays out to those who deserve to collect. In a somewhat similar manner, a gambling casino earns its profits by calculating probabilities to ensure that its receipts exceed the winnings that it is liable to pay out.
Council of Islamic Ideology, Government of Pakistan, is constituted under Article 230 of the Constitution of the Islamic Republic of Pakistan. One of the important assignments of the Council of Islamic Ideology is to scrutinize the laws in-force in the light of Qur-ān and Sunnah and recommend to the Government such steps by means of which these laws can be made to accord with the Islamic injunctions and teachings.

The Council in its 11th Report, “Beema wa Qawaneen-e-Beema...” dealing with Shari’ah Law and Insurance, delivered on March 1, 1984, a majority decision that “The contract of insurance, in all its form, is illegal, corrupt, false, forbidden, and cannot be decreed.”

The Council has taken the view that insurance is a transaction which was not dealt with at the time when the Islamic fiqh was being developed. The 11th Report further stated that both religious and judicial scholars have a difference of opinion with regard to the form of the contract, in vogue, for conventional insurance.

The Council of Islamic Ideology’s Report on Islamic Insurance System cited the expressed opinion of the Majlis-i-Fiqhi Islami about the system of insurance in vogue as follows.

1. ‘gharar-e-fahish’ (risk)

“Praise be to Allah and prayers and peace for Allah’s messenger, his progeny, companions and for all those who are guided by Him. Now then:-

“In its first session which was held at Makkah Mukarrmah on Sha’ban10, 1398 A.H. in the Majlis-i-Fiqhi Islami (the Assembly of Islamic Jurisprudence) deliberated on insurance and its different kinds. The vast amount of writings by the Ulmā on this subject was also kept on view. Also kept in view was resolution No. 55 of Saudi Arabia’s Majlis-e-Hayat-i-Kibar-ul-Ulamā (The Constituent Assembly of Most Eminent Religious Scholars) passed in its tenth session at Riad held on 4.4.1397 A.H. declaring all kinds of commercial insurance as unlawful in Islam.

With the exception of Honourable Sheikh Mustafa-uz-Zarqa, the rest of the member of the Majlis-i-Fiqhi agreed to conclude that all kinds and types of commercial insurance, whether related to life or commercial goods and wares or other articles are unlawful in Islam for the following reasons:

“As has been mentioned earlier, in the above referred report, the council expressed the opinion that the main laws relating to insurance and the prepondering bulk of insurance business is in conflict with the injunctions of Islam, because:

1. 1. There is ‘gharar’ in these contracts.
2. 2. The element of gambling is present in its extreme form.
3. 3. There is an element of interest in these contracts and
4. 4. Such arrangements come within the definition of ‘akal-mal-batil,’ e.g. unlawful acquisition.

“The report mentioned the view points of six different school of thought; Hanafites, Malikis, Shafites, Humbalies, Zaides, (i.e. the Shiites) and Zahiris on what is ‘gharar’. (The word ‘gharar’ is a derivative from the the word ‘gharar’, which means to lure; allure; entice; tempt;
beguile; deceive; delude.’) According to these viewpoints a contract suffers from ‘gharar’ if it is about:

1. An occurrence about which the parties do not know whether it would happen or not;
2. A thing which is not within the knowledge of the parties;
3. A thing whose existence or acquisition is in doubt;
4. A thing about which it is not known whether it exists or does not exist;
5. A thing whose acquisition is doubtful;
6. A thing whose quantum is unknown.”

The Council of Islamic Ideology analyzed various forms of insurance contracts, and has ruled that gharar is present in the contract of insurance, because:

1. The parties are uncertain (apart from a life assurance policy) whether the loss contemplated under a contract of insurance would ever be payable by the insurer.
2. At the time of the inception of the insurance contract, the parties are unaware of the exact amount of compensation payable by the insurer, and the time of such payment.

Gharar also implies: uncertainty, hazard, chance or risk, such as, sale of a thing which is not present at hand; or sale of a thing whose consequences or outcome is not known; or a sale involving risk or hazard in which one does not know whether it will come to be or not, such as fish in water or a bird in air. (Glossary of Islamic financial terms. Online)

The Prophet (pbuh) decreed prohibition on transactions of ‘sale’ involving an element of ‘gharar’. The Council of Islamic Ideology deduced that any transaction containing ‘gharar’ will be deemed to have been prohibited. Fuqaha differ regarding presence of ‘gharar’, ‘ribā’, and ‘qimar’, in insurance contracts. Qimar and ribā are condemned in the Qurān while condemnation of gharar (uncertainty) is supported by the following Ahadith.

“The sale of fish which is not yet caught is not in the state of property. Likewise, the sale of fish which the vendor may have caught and afterwards thrown into a large pond, from which it cannot be taken without difficulty, is null and void because there the ‘delivery’ is doubtful.” (Hedaya page 268)

“The sale of a bird in the air, or of one, which after having been caught, is again set free, is null, because in the one case it is not ‘property’ and in the other the ‘delivery’ is doubtful. (Bukhari Vol.III, page 199, and Abu Daud Vol. II page 634)

The above and other ahadith cited by the Council of Islamic Ideology in its report are with specific reference to the transactions of sale of tangibles only where ‘delivery’ and ‘goods sold’ by the vendor to the vendee is doubtful. The elements of explicit doubt regarding the performance of such contracts make these transactions as containing gharar. And, thus, would result into controversies, casting fraudulent intentions on the part of the vendor.

The ship owner faces the risk of loss by the sea perils such as storms, collisions, drowning, grounding, pirating, high jacking, or fire, etc. A trader or manufacturer faces the risk of his merchandise fluctuating in value or being lost by fire, floods, or theft, etc. It is relevant to know
the differences between insurable and uninsurable risks i.e. uncertainties. These are of two
types:

1. Dynamic, speculative, or business risk is bilateral where the uncertainty is the possibility of gain
or loss such as can happen in any business venture because of market fluctuations, changes in
customer preferences, government regulations; adverse economic conditions, which may result
into global economic depression, and insolvency of others stakeholders which causes a domino
effect, etc.

2. Static or pure risk is unilateral wherein the probability is only of loss therefrom, such as, death,
personal injuries, sickness, hospitalization, partial or permanent disabilities; road or industrial
accidents, fires, and thefts; forgeries, personal, professional or product liabilities; sea perils and
high-jacking; tsunamis, earthquakes, windstorms, floods, water damages; kidnapping for ransom,
terrorism, strikes, riots and civil commotions, etc., are forms and events involving pure or static
risks.

Risk management in the insurance business deals with pure or static risk which is transferred
from an individual to the insurer who charges a service fee for agreeing to accept the risk. Pure
risk exists when there are no potential gains, only possibility of financial loss.

Insurers do not address dynamic or speculative risks that involve chance of loss or gain;
whereas, in static or pure risk there is only the probability of loss or no loss. The insurers
accept only pure risks within theirs retaining capacity, inclusive of reinsurance treaties, to
absorb the quantum of the probable loss. The risk must normally be accidental in nature, free
from moral hazards, predictable, measurable, spread over a large number of similar
eventualities and acceptable to the insurer.

In fiqh literature the term gharar is associated with risk and uncertainties in contractual
agreements. Bay’al-gharar prohibited by the Prophet (pbuh) includes selling runaway slave and
fish in the pond. In shari’ah a contract becomes null and void where presence of gharar in
contractual obligations is found.

Allah hath permitted trade and forbidden riba (Quran: Al-Al-Baqarahh: 275). In trading ‘al-
bay’ is a contract of sale, and no sale transactions in Islam or any other religion is free from risk
of market, physical or natural calamities. Taking these risk is the legitimate way of doing
business which is called ghorm i.e. price and market risks, etc. A person cannot expect to make
profit without assuming probability of loss or risk in his ventures.

Gharar is indeed different from ghorm, although the English translation of both has applied the
same term interchangeably: risk and uncertainty. Rosly, Saiful Azhar, writes:

“Gharar or ambiguities about the buyer or the seller, the object of the sale and its price must be
avoided. In fact, using the term “ambiguities” is more accurate than risk and uncertainties when
one is dealing gharar in contractual agreement.”

1. Insurance contract involves:

‘maisir’, or ‘qimar’ or gambling:
The Islamic Ideology Council has quoted the definition of ‘qimar’ from the book, “Al-Iqtasad ul Islam”, as that, ‘qimar is a contract under which the parties agree with each other that one of the parties would pay to other a certain sum upon the happening of a certain event.’ The Fuqaha cite the Qur-ānic verses

Scholars relying upon the above verses of the Holy Qur-ān rule that, “Any contract containing the element of ‘maisir’ would be void ab-initio.” Further, in a contract of insurance the insurer promises payment till a certain event takes place, as such, the contract contains the element of ‘maisir’ rendering it void in Shari’ah.

The Council of Islamic Ideology defines:

“Briefly, qimar/maisir means every form of gain of money the acquisition of which depends purely on luck and chance and as opposed to others equally eligible, one man may acquire income as a result of lottery, draw or as a result purely of any other chance. Gambling, wagering and all of the games of chance are included in ‘qimar’.

Since maisir’s main effect is to get something too easily without hard labour where one wins or loses by chance alone. The adverse consequences of maisir/qimar on an individual, families and upon the nations are highlighted succinctly in the Qur-ān as: Satan’s plan is (but) To excite enmity and hatred Between you, with intoxicants And Gambling, and hinder you From the remembrance Of Allah, and from prayers: Will ye not then abstain? (5:91)

Bickelhaupt, David L., writes:

“Gambling operations may involve many of the attributes of insurance, such as large numbers, spread and homogeneity of risk, and predictability. Probably this is the reason so many uninformed persons think of insurance as gambling and sometimes even feel that they have “lost the bet” if they fail to have loss equal to the cost of insurance. The distinction is not in the method of operation, which may appear similar, but in the fact that insurance concerns itself with an existing risk. Speculation and insurance are both based upon socially and economically useful risks, too, while gambling is generally regarded as a less desirable method of speculation.”

The presence of the common element of “chance “in both maisir and insurance has led many learned fuqaha scholars to perceive that insurance in vogue tantamounts to maisir/qimar or gambling and, as such, is prohibited in Shari’ah. Resemblance between insurance and gambling in both does not cast them identical in purpose, phenomenon and consequences. To comprehend the point of perception the Qur-ān clearly emphasizes that, “… because they say:‘Trade is like usury,” but Allah hath permitted trade and forbidden usury.” (Al-Bakarah 2:275).

Colinvaux, Raoul, describing the nature of insurance contracts, writes:

”Contract of insurance, like wagering contracts, are aleatory contracts “depending on an uncertain event or contingency as to both profit and loss;” for financial or other consideration
the insurer agrees to pay or otherwise benefit the assured on the happening of a specified event or contingency. "Insurance is a contract upon speculation."

To expunge the element of gambling or wager from insurance operations the Life assurance Act 1774, commonly called the Gambling Act, which is still in force, states in its preamble:

"Whereas it hath been found by experience, that the making insurance on lives, or other events wherein the assured shall have no Interest, hath introduced a mischievous kind of gambling. For remedy whereof, be it enacted ... That from and after passing of the Act, no insurance shall be made by any person or persons, bodies politic or corporate, on the lives of any person or persons, or any other event or events whatever, wherein the person or persons for whose use, benefit or on whose account such policy or policies shall be made, shall have no interest, or by way of gaming and wagering; and that every insurance made contrary to the true intent and meaning thereof shall be null and void to all intents and purposes whatsoever”.

The Life Assurance Act, 1774, laid down three rules as follows:

1. That no life insurance should be made unless the person effecting the assurance has an interest in the life assured; and, that any life insurance made without such interest shall be null and void.
2. That there shall be inserted in the policy the name of the person or persons interested in it.
3. That no greater sum shall be recovered than the amount or value of the interest of the assured.

The nature and extent of insurable interest has been ascertained principally from case law. An insurable interest is a right or relationship in regard to the subject matter of insurance contract of such a nature that the occurrence of the event would cause pecuniary loss to the insured from damage, loss, or destruction of the subject matter of the contract which may be a property, a life, or another interest. Without insurable interest, a contract of insurance is a wager or gambling contract and shall be null and void.

In Lucena v Craufurd, Lawrence J defined insurable interest as:

“The having some relation to, or concern in, the subject of the insurance, which relation or concern, by the happening of the perils insured against may be so affected as to produce a damage, detriment or prejudice, to the person insuring and where a man is so circumstanced with respect to the matters exposed to certain risks or danger, he may be said to be ‘interested in’ the safety of the thing with respect to it as to have benefit from its existence – prejudice from its destruction.” (1806) 2 B&P 269, 301 (NR).

The concept of insurable interest has been elucidated in a recent case of “The Martin P’” {Queens Bench Division (Commercial Court) O’Kane v. Jones (The “Martin P”), 2004}. Some of the general points deduced on insurable interest in the above case are as follows:

1. The concept of insurable interest was introduced as a means of distinguishing “legitimate” contracts of insurance from gaming and wagering contracts.
2. The concept had been very broadly defined “by interest in a thing every benefit and advantage arising out of or depending on such thing, may be considered as being comprehended.”
3. That which made a contract of insurance by way of gaming or wagering objectionable was that neither party thereto had, apart from the contract, any interest in the outcome of the future uncertain event, namely the possible occurrence of any of the perils insured against, upon the occurrence of which money would be payable.

4. The definition of insurable interest in section 5(23) of the Marine Insurance Act, 1906 (of UK) was not an exhaustive one.

5. However, the above section identified three characteristics which would normally be required for insurable interest to be present, namely:

   a) That the assured may benefit by the safety or due arrival of the insurable property or be prejudiced by its loss or damage or detention or in respect of which he may incur liability;

   b) That the assured stands in a legal or equitable relation to the adventure or to any insurable property at risk in such adventure; and

   c) That the benefit, prejudice or incurring of liability referred to at (a) must arise in consequence of the legal or equitable relation referred to at (b)....

Some of the marked differences between insurance and gambling are as follows:

1. Risk element is of the essence of insurance contract; the insured seeks insurance cover in view of the inherent risk of loss, and does not create the risk of loss by contract itself, as is the case with wager or gambling.

2. Insurance contract aims at neutralizing and offsetting already existing risk or chances and their consequences, whereas gambling purposely create new ones.

3. In gambling one of the parties prays that a certain event may happen, while the other party wishes that the event may not happen. This is not the case in the contract of insurance. Both the parties to the contract wish that the insured event may not happen at all.

4. The parties in gambling pose a threat of loss on each other. Whereas aim of insurance contract is to save the insured from the inherent loss.

5. The parties in a contract of insurance agree to certain mutual obligations which they have to discharge. The element of carrying out of mutual obligations is not necessary in wagering.

6. The money pooled by way of contribution in the insurance operations is mostly employed for productive purposes, whereas in gambling the money generated is likely to be diverted on unethical or non-productive ventures.

7. Gambling may lead to windfalls whereas under a contract of insurance generally the insured is monetarily indemnified to the extent of the loss suffered.

8. The distinction between insurance and wagering contracts is that insurance contracts are enforceable under law while wagering contracts are not, by legal process.

1. **C. It contains the element of ‘ribā’ i.e. interest.**

The Council of Islamic Ideology’s report quotes, verse 279 of Al-Baqarah:

For, upon a claim on an insurance policy the insured receives more than what he has paid (the premium) to the insurer, the excess amount constitutes ‘Ribā’. Usury is condemned and prohibited in the strongest possible terms. I cite below four verses 2:75-76, 3:130, 4:161 of the Holy Quran and the meaning with commentary, on ribā:
Following is the commentary on the verse 2:275 of Al-Baqarah:

Usury is condemned and prohibited in the strongest possible terms. There can be no question about the prohibition. When we come to the definition of usury there is room for difference of opinion. Hadhrat ‘Umer, according to Ibn Kathir, felt some difficulty in the matter, as the Prophet (PBUH) left this world before the details of the question were settled. This was one of the three questions on which he wished he had had more light from the Prophet. Our ‘Ulmā’, ancient and modern, have worked out a great body of literature on Usury, based mainly on economic conditions as they existed at the rise of Islam”.

An apt smile: whereas legitimate trade or industry increases the prosperity and stability of men and nations, a dependence on Usury would merely encourage a race of idlers, cruel blood-suckers, and worthless fellows who do not know their own good and therefore akin to madmen.

Owing to the fact that the interest occupies a central position in modern economic life, and especially since interest is the very life blood of the existing financial institution, a number of Muslims have been inclined to interpret in a manner which is radically different from the understanding of Muslim Scholars throughout the last fourteen centuries and is also sharply in conflict with the categorical statements of the Prophet (peace be on him). According to the Islamic teachings any excess on the capital is ribā (interest). Islam accepts no distinction, in so far as prohibition is concerned, between reasonable and exorbitant rate of interest, and thus what come to be regarded as the difference between usury and interest; nor between returns on bonus for consumption and those for production purposes and so on.

1. D. ‘Akal-e-haram,’ (The mode of illegal extortion of money.)

The report states that the presence of ‘gharar’, ‘qimar’, and ‘ribā’, make the insurance contract a transaction totally void under the tenets of Sharia’h, because the money extorted by each party, in such a contract, constitutes an illegal income.

The Ulamā refer to the verses 2:188 Al-Baqarah and 4:29 An-Nisaa of the Holy Qur-ān:

The Shari’ah Scholars have recommended that since the conventional insurance business in vogue is not based on the idea of mutual cooperation but serves as a device for extortion of money from the people to utilize it in interest bearing ventures, therefore, it is forbidden. The business aims at multiplication of capital in the hands of insurance companies and, therefore, is liable to be considered as illegal in Shari’ah! Islam cherishes equitable sharing of risk and gains as the basis of co-operation between capital and enterprise. The Ulamā of the Islamic Ideology Council have deduced that:

The above verse (A-Nissa - 4:29), can be interpreted that taking away of each other’s wealth, property or capital by unlawful means such as interest, gambling or fraud is prohibited while deriving benefit from each other’s wealth, property or capital under an equitable business deal struck by mutual consent is permitted.
The essential element of “trading” is that the return on capital employed depends upon actual operating results of the business undertaken.”

The Council’s report, Beema-wa-Qawaneen-e-Beema, page 12, recommended the following opinion about the lawful, Shari’ah compatible, form of insurance.

"There is no repugnance in Shari’ah if insurance is undertaken with the sentiments of and is founded on cooperation, reciprocal responsibility, mutual surety and volition. If, therefore, an insurance company is established in such a manner that each one of its members is insured and these insured persons enter into a mutual agreement of cooperation and reciprocal responsibility, then such agreement will be lawful in Shari’ah ...”

The Council of Islamic Ideology examined the system and laws of insurance and, proposed in its Report, Beema-wa-Qawaneen-e-Beema, in 1984, to the Government that:

In order to prepare an Islamic alternative, that is, System of Collective Responsibility and Cooperation in place of the existing insurance system, a working group may be constituted in which Ulamā of the Council and the insurance experts may be included. They may expunge un-Islamic elements from the insurance system as per Report of the Council and bring out the alternate Islamic system.

The reader should keep his mind crystal clear that Shari’ah Scholars of all schools of thought do not condemn the theme, need, importance and viability of insurance system. They question and express their reservations to the conventional model of insurance currently in vogue.

On the need and importance of insurance the Council of Islamic Ideology says:

In the early stage of the new economic system of the world, Insurance business related to a large extent to the coverage of sea-ships and their cargo. But along-with the growth of industry and trade and banking business in the Western countries the field of insurance also continued expanding in extent. Now it has come to this that sea-ships, aeroplanes, cars, factories, commercial and private buildings and besides human life, human limbs, voice, etc. are also being insured. Due to this, it has assured a regular and vast business proportion. On the strength of their capital big capitalists sell expensive policies to simple minded persons, involving real or imaginary possibilities or apprehensions. Like this, they make hundreds of million dollars annually. This capital is further invested in business and profit is reaped in astronomical figures. In other words, money-business is being indulged in , in many shapes and forms. On the one hand this giving rise to inflation, Secondly prices of commodities and services are under extraordinary pressure. Not only this but many economic evils like concentration of wealth, recessions, etc. are also coming into existence which in their own way are a big source of corruption. As, however, the individuals and nations devoid of the wealth of faith and belief have no remedy for these evils, they are treading on these paths only.

As far as developing countries and economically weak nations like Pakistan are concerned, in this matter they are absolutely helpless and are perforce the target of exploitation of the developed nations.
What is Sharia’h?

Before I elucidate further the Islamic perspective on insurance, the reader needs to apprise himself of the meaning of Shari’ah. Briefly, Shari’ah means the Islamic way of life as derived from the Qur-ān and the Sunnah (traditions) of Prophet Muhammad (pbuh). For Muslims the word of Allah is His law and command. Shariah refers to the Islamic system of law and way of life.

The traditions of the Prophet Muhammad (pbuh) being divinely inspired are not only interpretive of Qur-ānic verses but also complementary to them. I quote two ayath 4:59, and 4:80 of An-Nisāa from the Holy Qur-ān:

Thus the Qur-ān and Sunnah are the fundamental roots of Shari’ah on the basis of which fiqh was drawn by early Muslim scholars (fuqha). The two other important sources of Islamic jurisprudence are Ijma and Qiyas.

Judicial issues that cannot be resolved by qiyas are resolved through Ijma (consensus) among fuq’ah scholars. The validity of Ijma is based upon Prophet Muhammad’s saying “My people will never agree upon an error.”

Qiyas, i.e. reasoning by analogy, defines laws from known injunction to new injunction. For the validity of Qiyas, M. Hidayatullah, the former Chief Justice and Vice President of India, quotes Fatzee and Amir Ali, when the Prophet sent Mouadh Bin Jabal as Chief Justice (and the Governor) of Yemen:

“The Prophet questioned him (Mouadh) to know how he would conduct himself and this is what was said:

Prophet: On what shalt thou base thy decision?

Mouadh: On the Koran.

Prophet: If the Koran does not give guidance to the purpose?

Mouadh: Then upon the usage of the Prophet.

Prophet: But if that also fails?

Mouadh: Then I shall follow my own reason.

The Prophet (pbuh) fully approved of the replies of Mouadh and praised God that His servant was on the right path.”

The Columbia Electronic Encyclopaedia has the following entry for Shari’ah:
**Sharia**, the religious law of Islam. As Islam makes no distinction between religion and life, Islamic law covers not only ritual but every aspect of life. The actual codification of canonic law is the result of the concurrent evolution of jurisprudence proper and the so-called science of the roots of jurisprudence (usul al-fiqh). A general agreement was reached, in the course of the formalization of Islam, as to the authority of four such roots: the Qurān in its legislative segments; the example of the Prophet as related in the hadith; the consensus of the Muslims (ijma), premised on a saying by Muhammad stipulating “My nation cannot agree on an error”; and reasoning by analogy (qiyas). Another important principle is ijtihad, the extension of sharia to situations neither covered by precedent nor explicable by analogy to other laws. These roots provide the means for the establishment of prescriptive codes of action and for the evaluation of individual and social behaviour. The basic scheme for all actions is a fivefold division into obligatory, meritorious, permissible, reprehensible, and forbidden.…


After extensive research and review the working group of the Council held twelve sessions. Beside the takaful modes of Malaysia, Jeddah, Manama, Sudan, and Bahrain, the mutual insurance companies working in various countries, particularly USA, Japan and Canada were examined in detail. The members of the working group found that all the examined takaful models are incompatible with the injunctions of Shari’ah.

The concept of cooperative risk sharing is the oldest form of insurance. The Grand Council of Islamic Scholars, Majma-al-Fiqh, Mecca, Saudi Arabia, approved Takaful model as a Shari’ah-acceptable alternative to traditional insurance system in 1985.

The working group was of the view that any insurance arrangement, which was not of the mutual type, will not be acceptable in Islam. There was also a general agreement that since the constitution of the various Islamic Insurance Companies was not based on mutual sharing of the risks and the shareholders and policy holders of the companies under review are different entities, none of these could be adopted to serve as a model for the working group.

The Council of Islamic Ideology reviewed the operations of the existing takafuls in order to find a Shari’ah compatible model for Pakistan. Finally, after seven years of hard labour, the Council members unanimously approved its recommendations on 29th April, 1992, in its report on Islami Nizam-e-Beema. The Council instead of adapting any of the examined takaful models, proposed its own structure, “the Blue Print of the Islamic Assurance System,” which formed a part of the recommendations. The recommendation of the Council was printed and presented to the government on 2nd Zul Hijja, 1412 A.H. i.e. 4th June, 1992.

The worthy effort of the Council to establish an Islamic country’s system of Insurance on true Islamic mode will prove to be a milestone as a fundamental document. The system of Insurance which may be set up in future on its proposed basis will be free of the elements of gharar, qimar and ribā on account of which the conventional system of insurance in vogue failed to win the
confidence of the Muslim Um‘mah of over one and a half billion (now, in 2009, one billion eight hundred and thirty million) who have had few options when shopping for products that conform to their faith.

The Council of Islamic Ideology in its report recommended that:

The Government may promulgate a regular detailed and codified law as the first stage towards establishment of the new institutions of Takaful. This law should have, like the companies and modarabah ordinances, from the basic and essential orders down to all necessary and sectional details as well as detailed procedures of different matters, business, investments, outlines/sketches and proformas etc; full and complete.

It is interesting to note that the government did not act for thirteen (13) years on the recommendations of the Council. Insurance Reform Commission was constituted in mid 1987 under the Chairmanship of Justice (R.) M. Mahboob Ahmad. Life insurance market reopened to private local insurers through the Finance Act, of 1990, and to foreign insurers in 1994. Privatization of the State Life Insurance Corporation of Pakistan was constantly the topic of the day. Takaful companies were being established around the world in several Islamic countries. This inordinate delay on the part of the government to implement Council of Islamic Ideology’s recommendations does not seem to have any justification.

My exclusive interview in regard to Private Insurance Companies and State Life was published by the Insurance Journal, Karachi, Pakistan, in July-Aug-Sep 92. In response to one of the question in this interview I suggested a blue print and the strategy of privatization of the State Life Insurance Corporation of Pakistan (SLIC) through mutualization. I reproduced it below:

Insurance Journal: In your opinion how best can the government privatize SLIC?

Rizwan Farid:

The Paid-up Capital of State Life Insurance Corporation is only Rupees fifty-five (55) million, wholly owned by the Federal Government. The corporation has also a life fund of over Rupees twenty (20) billion which belongs to the policyholders. Every year the corporation invests substantial fund in government securities, real estate, stock and bonds and loans to the policyholders against their cash values.

In my view the government should offer its total share holding of Rs. fifty-five (55) million at a reasonable price. These shares should be bought by the corporation through its life fund as is the practice of the corporation to buy any share of an approved company. By this transaction the corporation would automatically be converted into a mutual insurance company i.e. a company wholly owned by its policy holders.

Thereafter the policy holders would elect their own Board of Directors consisting about 15 to 18 members who should first be the policy holders of the corporation and be nominated by election by the professional bodies such as Pakistan Insurance Association, Pakistan Medical Association, Pakistan Bar Council, Pakistan Chamber of Commerce and Industry, University
Teachers Federation, Pakistan Engineering Council, Association body of the Chartered Accountants, Pakistan Newspapers owners Association, Federation of Working Journalist, one nominee each elected by Karachi, Lahore and Islamabad Stock Exchanges, besides one director each elected by the Corporations officers, Area Managers, Staff and Field Workers Federations. To get the elected nominee the corporation would also have to use postal ballots.

These elected directors then would select and appoint professionally qualified and experienced persons for the positions of the Chief Executive Officer, and Executive Directors for each function division of the corporation such as, Marketing, Policy Holders Services, Actuarial, Investment, Audit and Accounts, Real Estate, Group & Pension, Personnel & General Service, etc.

In the United Estate most of the mutuals started as stock companies and converted to mutual at a later date. Out of 2153 life and health insurance companies in the United Estates 117 are mutual at the end of the year 1990. It would be interesting to note that the largest life and health insurance companies are mutual. Mutual insurance companies are very important in the U.S.A, although by number they are less than 6% but possess almost two third of the total assets of life insurance industry and accounts for about one half of the total amount of life and health insurance business in force in the United States. Similarly out of thirty (30) companies sixteen (16) are mutual writing life and health insurance business in Japan during the year 1990.

In 1984 out of 169 life and health insurance companies in Canada fifty (50) were mutual companies and many stock companies were seriously considering converting from stock to mutual companies.

In mutual insurance company the policy holders are owners of the company and theoretically they control the company. Each policy holder is eligible to vote in the elections of the board of directors on the basis of one vote for each policy holder regardless of the amount or number of policy that the policyholder owns. The operating profits are distributed to the policyholders. Since a mutual company has no stock to sell it cannot be bought by another company as a stock company can be. By means of mutualization the government can successfully avoid future takeovers by any interested and influential group of people.

By converting State Life Insurance Corporation into a mutual the Government would also succeed in its objective of Islamization as all Islamic schools of thought around the world have the consensus that mutual life insurance companies are permitted in Islam. In view of the above I would strongly suggest whenever the government should think to privatize SLIC, the best way would be to convert SLIC into a mutual company, and as a matter of fact it would be justice with the policyholders and good gesture on the part of the government.

Insurance industry professionals were anxiously expecting some dynamic legislation on some system of insurance operations compatible with Shari’ah. Earnest and Young with a local partner was engaged to draft new insurance legislation. The Insurance Act 1938 was thoroughly reviewed. Some powerful lobbies and vested interest groups who were behind the scene influenced the consultants to delete and totally drop the theme of cooperative or mutual insurance companies, and the Policy Holders Directors on the Board elected by the life
insurance policyholders of the company, in the new legislation that was introduced on August 19, 2000, namely, “Insurance Ordinance 2000”. Thus with a single and silent stroke in drafting the new legislation regarding insurance business in Pakistan the consultants deprived the life insurance policyholders of the say in the management of the affairs of the company; and also killed the doctrine of mutual insurance entities — popular name ‘Takaful’ when operated in consonance with the established Shari’ah principles — which was strongly and unanimously recommended by the Islamic Ideology Council in its recommendations of 1992.

I earnestly request the government and the parliamentarians to make an immediate amendment in the Insurance Ordinance 2000, and to insert a specific provision for ‘mutual insurance company’ operations and appointment of Policyholders’ Directors on the Board of companies.