

**IN THE NAME OF ALLAH, THE MOST GRACIOUS, THE MOST MERCIFUL
MAY PEACE, BLESSINGS, AND MERCY OF ALLAH BE UPON PROPHET MUHAMMAD ﷺ**

HISTORICAL BACKGROUND OF INSURANCE AND TAKAFUL

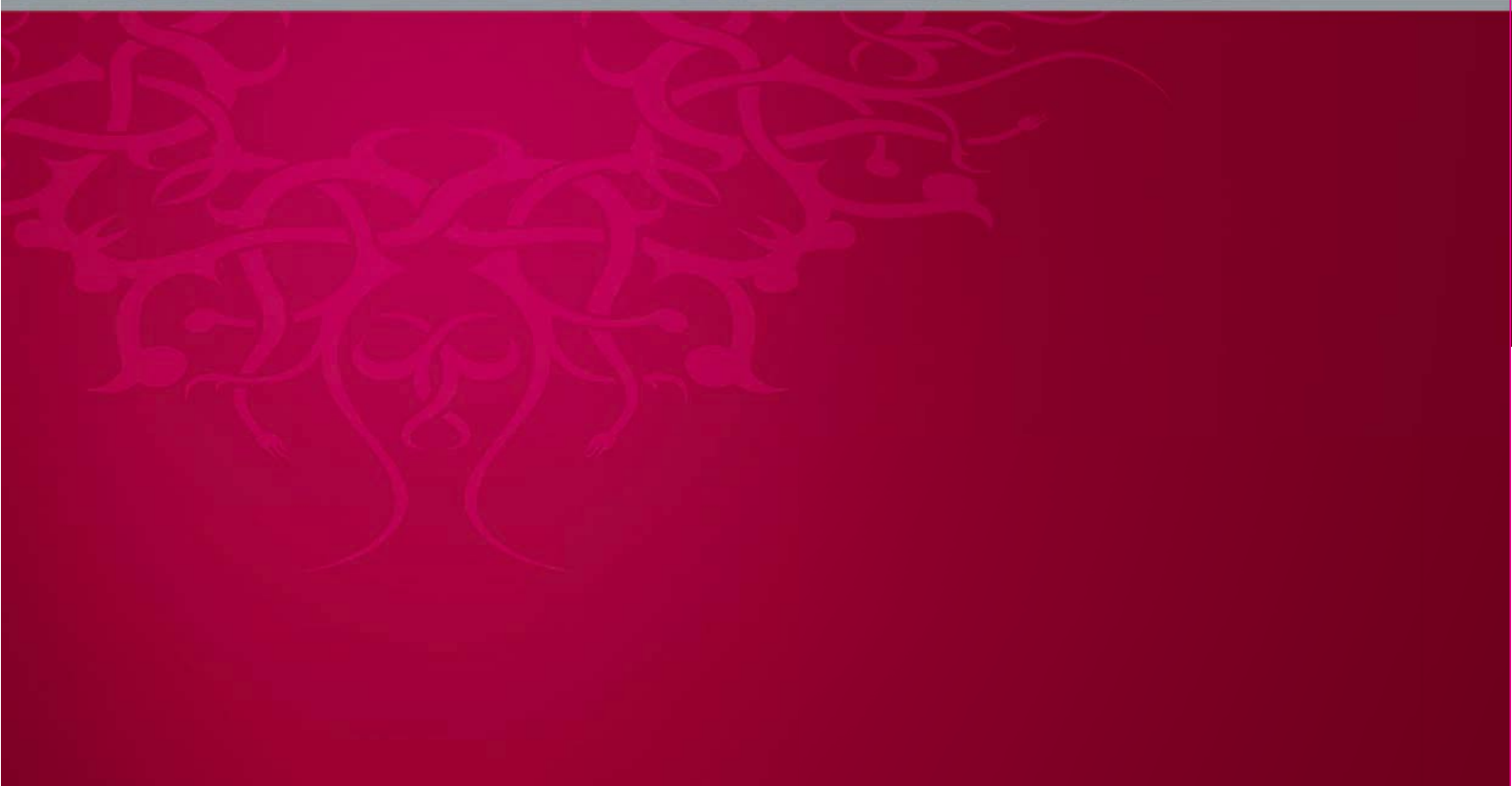
It is generally believed that the history of insurance began with marine insurance in the fourteenth century. It was invented as a solution to the problem of sea piracy and protect from losses due to the possibility of ship sinking in high waters. Both carried immense financial risk. Insurance served to protect against these and other such financial risks.

However contrary to the general belief, we find attempts to mitigate risk of loss in high waters in Chinese and Babylonian civilizations two to three thousand year before Hazarat Essa (May peace be upon him). The Hammurabi code recorded such practices of Babylonians around 1750 BC. Greeks and Romans created "Benevolent Societies" which were earlier forms of life and health insurance.

Similar institutions were available for welfare of general public and trading fraternities in Islamic Societies. While going through Islamic history, we find the following on risk management techniques being practiced in Islamic societies.

Managing risk is therefore nothing new and is very much permissible in Islam if practiced justly.





Few of such instances are as follows:

1. DHAMAN KHATR AL-TAREEQ:

This is an understanding between two people wherein one of them guarantees the other (a trader) of safety and security in adopting a particular route, and compensation for any losses incurred along the way. So if that person adopts this path on account of the guarantor but then finds himself robbed and his valuables snatched away, the guarantor will then be Shar'an (legally) liable to recompense him.

2. DHAMAN AL-DARK:

If a person was hesitant in purchasing a slave in fear of the possibility of him being a free man, but does so nevertheless on account of another person's guarantee, he was Shar'an (legally) allowed to claim refund either from the guarantor or from the seller of that slave if later the slave was indeed proven a free man. A person who influences a sale by promising to compensate if the item is proved faulty, is legally bound to fulfill his promise if the sale results in loss to the buyer.

3. AQILA:

Aqila is a risk-sharing mechanism in which the payment of blood-money (diyat) due on the murderer is, under some situations, paid off collectively by his/her community members.

4. AQD-E-MUWALA'AT:

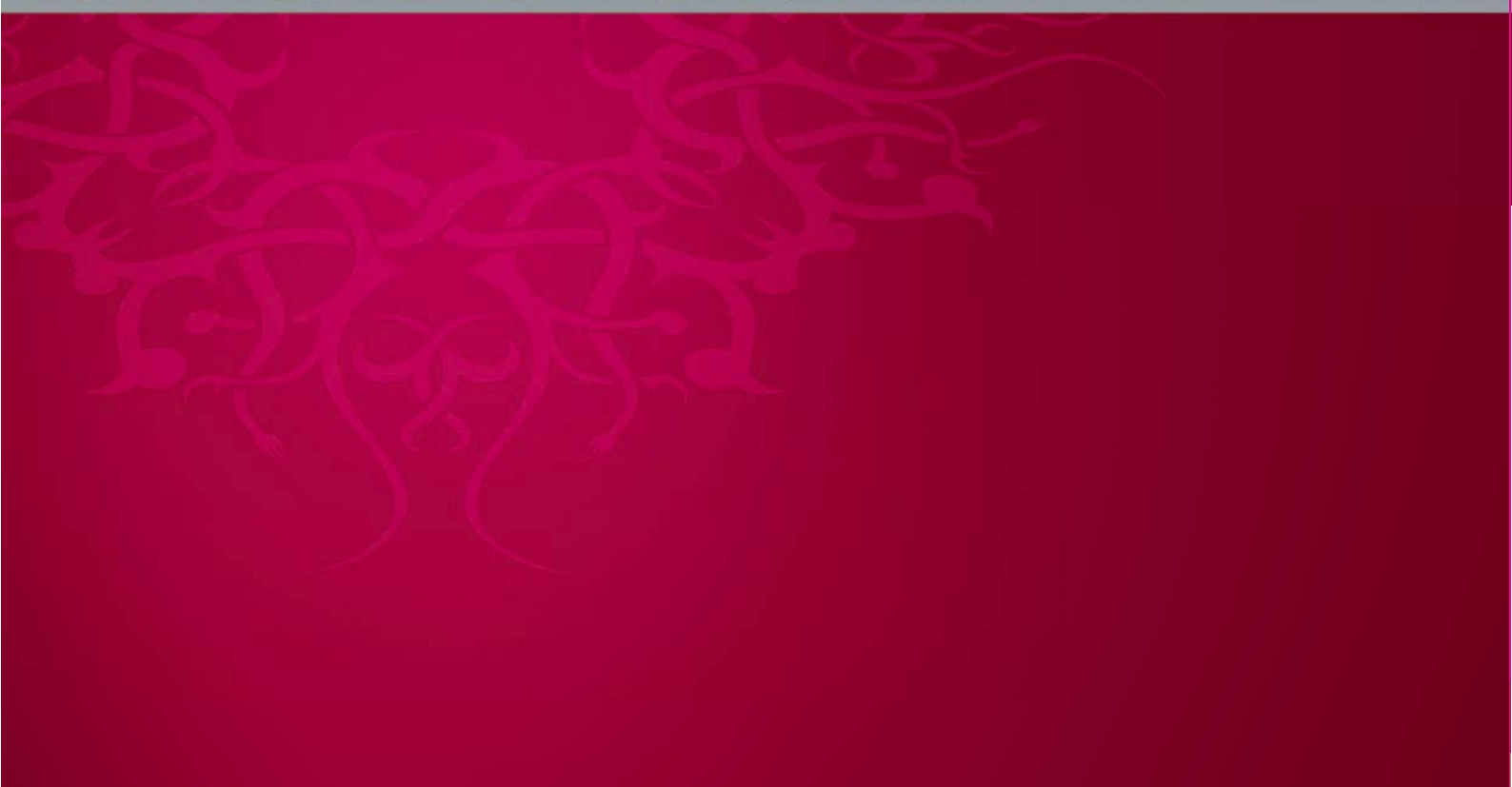
Aqd-eMuwal'at is when a person embraces Islam at the hand of another person and then makes an agreement with him or with any third person that he will become the inheritor of his wealth after his death and that all liabilities of his wrongdoings during his lifetime will be upon him. That agreeing person will have to comply accordingly. This is a clear example of mutual cooperation.

All these risk management techniques are based on the principles of brotherhood & mutual solidarity.

5. ASSURANCE TO TRADERS

Seljuk Sultan Gias ud din in 12th century compensated those traders from state treasury who were robbed while travelling within Seljuk territory.





Going forward, conventional insurance contracts in its present forms were introduced in Genoa in 14th Century. First such known contract was issued in 1347 AC.

First known book on insurance was written in 1488 AC by Pedro de Santerna, which was published in 1552 AC.

London being center of global trade had ever increasing demand for Marine insurance in 17th century. In 1680 Mr. Edward Lloyd established a coffee house where ship owners, merchants and ship captains would usually visit. The coffee house soon became a source of reliable shipping news and a meeting place for parties wishing to insure cargoes and those ready to underwrite such ventures. The Lloyd of London today is a leading market place for different types of insurance, although it works differently than an insurance company.

From the foregoing, it is evident that insurance started as an act of compassion and a way to promote and safeguard trade and society but was later converted in to a major commercial activity by Europe.

Many believe that conventional insurance first got introduced in Islamic Fiqh in the twentieth century, but this is not so. Research tells us that the first fatwa issued on the subject was by a renowned Jurist from Syria by the name of Allama Ibn Abideen Shami (may Allah be pleased with him) in his famous book titled “*Radul Mukhtar*” (which is also known as *Fatawa Shamia*. This fatwa is regarded as an authentic fatwa).

In fact, we find that insurance was very much a norm in the days of Allama Shami (may Allah be pleased with him). Traders were accustomed to paying additional amount over routine costs for the transportation of their goods overseas. This additional amount was called “Sokara”. Sokara means insurance and security. The insurers promised to compensate for any loss to their cargo while at sea against these premiums. This was marine insurance in action.

Allama Shami declared the practice of this form of insurance impermissible. He used the term “Sokrah” for Insurance. Since that time Ulema has declared insurance as impermissible in Islam.

REASONS FOR THE IMPERMISSIBILITY OF CONVENTIONAL INSURANCE

The conventional Insurance Contract is a commutative contract which involves some ills due to lack of its conditions. These ills are ;

1. Riba (Interest)
2. Qimar/Maysir (Gambling)
3. Gharar (Uncertainty)



The conventional insurance contract is a commutative contract (compensatory and bilateral), in which premium is the cost and the sum insured/assured/covered is the subject matter. There will always be fluctuations in the money involved, and being a sales contract with money being exchanged from both sides, any such fluctuation will automatically fit the description of "interest". Interest is, staying relevant to a financial institution, defines as one party giving money in exchange for less or more money, which is exactly what happens when a conventional insurance company receives premiums and pays less or more money in return, depending on whether the covered risk materializes.

Likewise, gambling also is a fundamental part of the conventional insurance contract. Gambling is defined as a transaction whereby any of the contracting parties, after placing their goods or money at stake, can win or lose the other's stake depending on an uncertain outcome without compensation. Hence, one party wins the other's amount completely without paying anything in return, or loses everything without being paid anything in return.

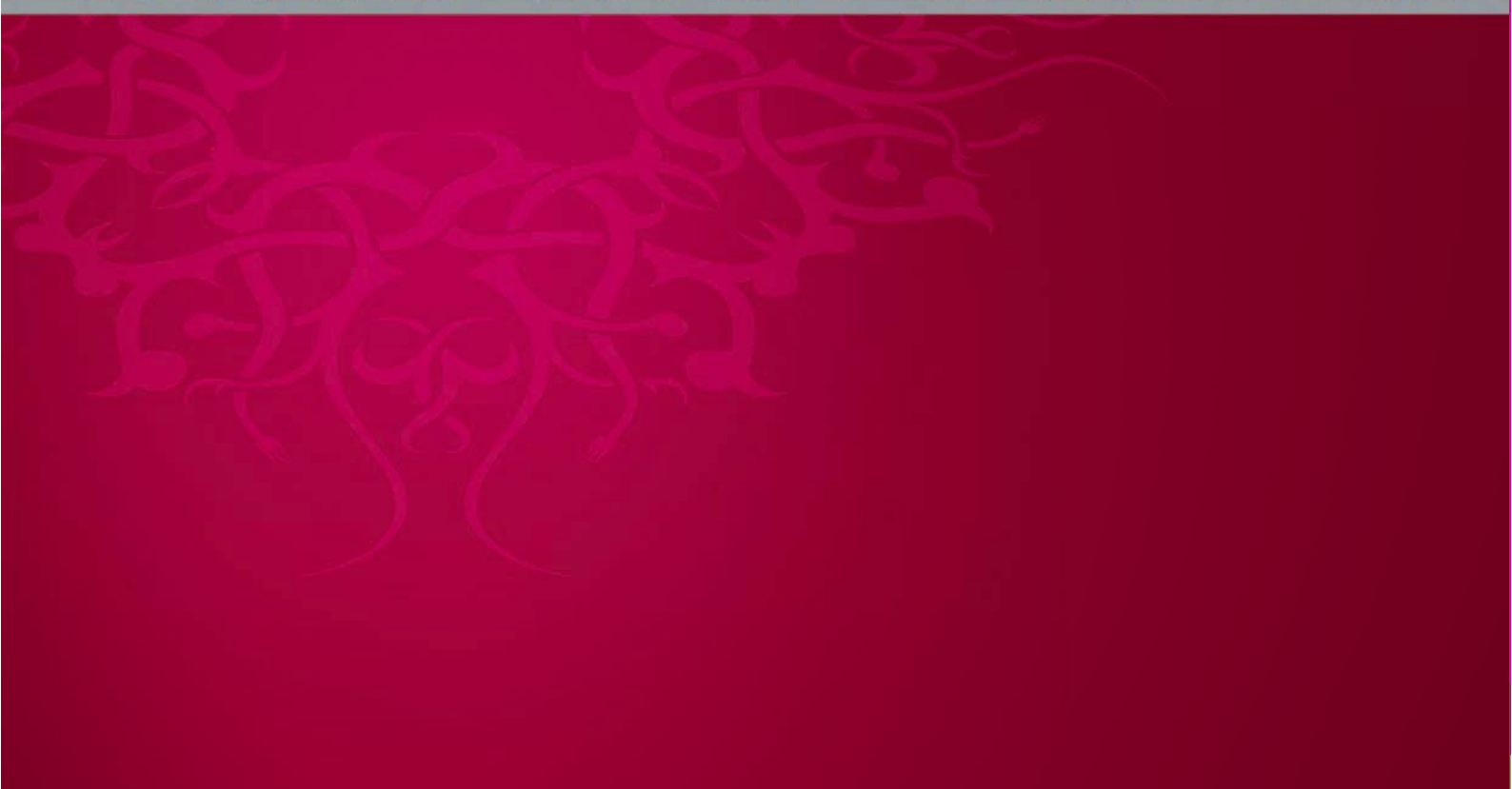
Finally, the third damning feature of a conventional insurance contract is "Gharar", translated as "uncertainty". In a technical sense, it means "at least one party's compensation being subject to uncertainty due to an uncertainty in the very object being contracted". In insurance, the insured does not know for sure whether he will be paid his capital with interest, or will be paid the insured sum in case the risk for which he insured materializes, and might end up receiving more than he paid to the insurer. This excessive uncertainty, when coupled with the price he pays, the subject-matter for which he pays or the time period over which his payments are distributed, render the conventional insurance contract impermissible in Islamic Shari'ah.

As noted earlier, helping someone in time of need, which is the underlying benefit of insurance is not only allowed but encouraged by Shariah. Muslim Ulema researched on the finding an alternative permissible way to make the system available for the benefit of general public and the economy. This was a general search for finding ways to do financial transactions avoiding Riba and other ills especially establishing a banking system which complies with Islamic Shariah. Moreover, Insurance and Modern Financial institutions go hand in hand with each other. It was therefore necessary to propose a Shariah Complaint alternative to conventional insurance as well.

Effort on devising such alternatives started in middle of the last century but bore fruits in the seventies when general fatwas were issued in favor of a proposed model of Islamic insurance. First Islamic Insurance (Takaful) company was established in 1979 in Sudan. More companies in different part of the Islamic world were established in later years. In 1984, the first ever law was enacted in Malaysia to regulate the Takaful Industry. Growth of Takaful, while keeping with in the limits imposed by Shariah, without having Re-Takaful Companies to enhance the overall capacity of the industry was impossible. Therefore in 1997 ASEAN Re-Takaful International was established.

In 2003, an Ijtima of Ulema of Pakistan was held in Jamia Darul Uloom Karachi to discussed permissibility of Takaful.

In 2005, Government of Pakistan issued first ever Takaful Rules to regulate the Takaful Operators. In 2006 first Takaful Company was established. In 2007 Pak-Qatar Family Takaful was issued license to be the first Family Takaful company of the Country.



TAKAFUL

Takaful is a community-pooling system based on the principles of brotherhood and mutual help wherein participants contribute in a fund to help those who need it most in times of financial difficulties.

REFERENCE OF TAKAFUL CONCEPT IN HOLY QURAN & SUNNAH

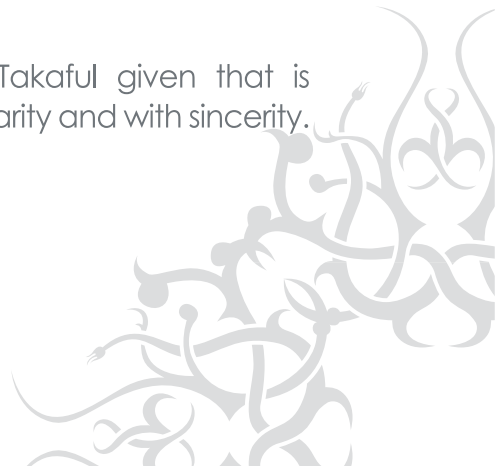
Takaful is not a recent invention. In fact, its reference is available in the Holy Quran and Sunnah. The reference is in connection with the divine commandment for brotherhood and mutual solidarity which is exactly what Takaful stands for.

It is mentioned in the Holy Quran:

- “Cooperate with one another in matters of righteousness and piety.” (Surah Maida: 2)
- “Muslims are brothers to one another.” (Surah Hujarat: 10)
- “The believers, in their affection, mercy and sympathy to each other, are like the body, if one of its organs suffer and complains, the entire body responds with insomnia and fever.” (Hadith Muslim: 4685)
- In the sixth year of the Hijri date, the Prophet Muhammad (PBUH) made a pact with the Jews of Medina which is generally known as the ‘Meethaaq-e-Madina’. This pact was based on the principles of brotherhood and mutual solidarity and as such one of the clauses states that “every member will have to pay just compensation for their respective tribe”, meaning that the responsibility of freeing the slave will be on the shoulders of those to whose tribe the slave will belong. This is a prime example of the concept of brotherhood and solidarity in Islam.

Such kinds of pacts have been existent during the rule of the Caliphs as well, though not by the name of Takaful. However the spirit of Takaful has always been there: different people through community-pooling help create a common fund which is used to benefit them in times of need.

Therefore, there is no doubt about the permissibility of Takaful given that is functioning on the principles of brotherhood and mutual solidarity and with sincerity.



THE MODUS OPERANDI OF TAKAFUL

Different models are in practice in different parts of the world. We will briefly introduce you to these models before delving in to details of the model adopted by Takaful Operators in Pakistan.

All Takaful Models are based on mutuality and donating for a charitable purpose (Tabbaru).

The model used by Malaysian operators established after promulgation of Takaful Act 1984 is known as Modaraba Model taking its name from the Modraba arrangement on which the pool is managed. Here the risk is shared on the basis of Tabbaru and underwriting profit (Surplus) are shared on the basis of Modraba.

Another arrangement which is usually practiced in Middle East excluding Saudi Arabia is known as Wakala Model. In this model, the operator manages the pool as an agent of the pool, which has money collected from the participants on the basis of Tabbaru. Saudis use co-operative model, which in essence is a form of mutual insurance with certain conditions to make it Shariah Complaint.

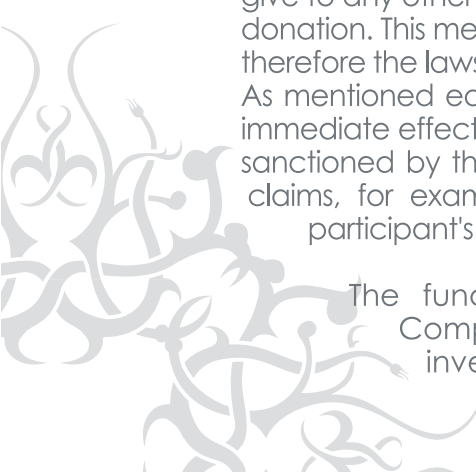
The model used in Pakistan is known as Wakala-Waqf Model. This is an enhancement over the Wakala Model where the pool is formed as a Waqf. Waqf is juristic person in Shariah, whose ownership rest with Allah (SWT) and no other person can claim it ownership. By creating a Waqf, certain anomalies observed by Ulema are eliminated from the Wakala model.

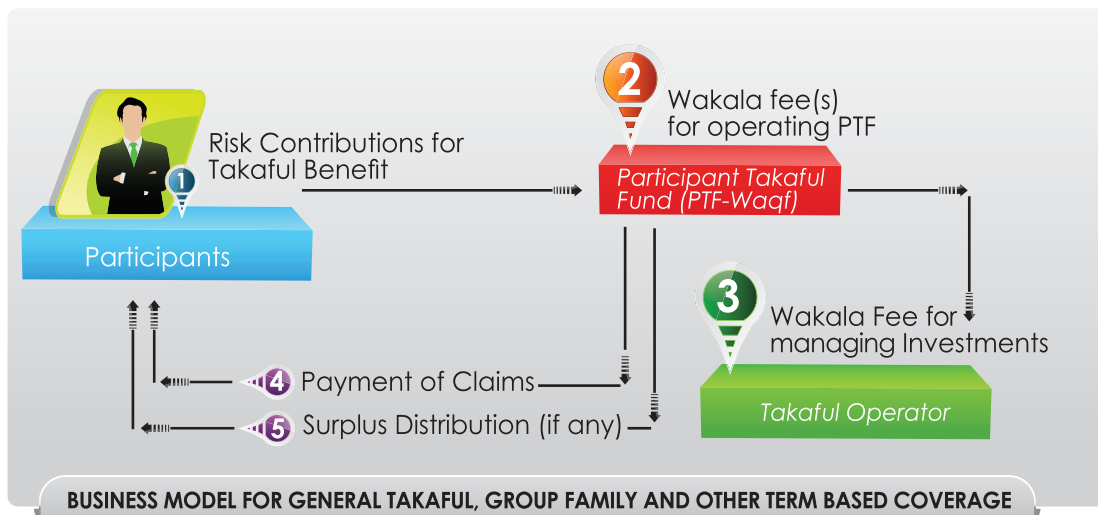
The shareholders firstly would create a Waqf Pool in order to initiate the Takaful activities. Because they had been the ones to establish this Waqf they are called the Waqif, whereas the ownership of the Waqf is transferred to Allah Almighty. People are able to benefit from it for their risk mitigation purposes after acquiring a membership of this Waqf Pool which is legally referred to as the Participants' Takaful Fund or PTF.

The Shareholders thereafter formalize certain conditions for the Waqf which will form the basis of its operations. Based on the Fiqh ruling these conditions are judged to be as effective and valid as if they would have been laid out by the Shariah itself. This means that the Waqif, by virtue of its legal position, can therefore stipulate that financial benefits may only be provided to those who contribute to the Waqf Pool. The relationship of the participant and the Waqf on the other hand is merely a relationship of an Aqd Taburru.

The contributions paid by the participants are recognized as Taburru'at and not as Waqf, and in fact become the property of the Waqf. This is akin to the charity we give to any other Waqf; the charity given is not considered as Waqf but simply as a donation. This means that the participants immediately lose their right of ownership, therefore the laws pertaining Zakat and even the Inheritance law won't apply here. As mentioned earlier, these contributions become the property of the Waqf with immediate effect and thus benefits from it need to be according to the conditions sanctioned by the Waqif, such as utilizing these contributions for the payment of claims, for example. Hence, it is the Waqf Pool which compensates for the participant's loss and not the Takaful Operator.

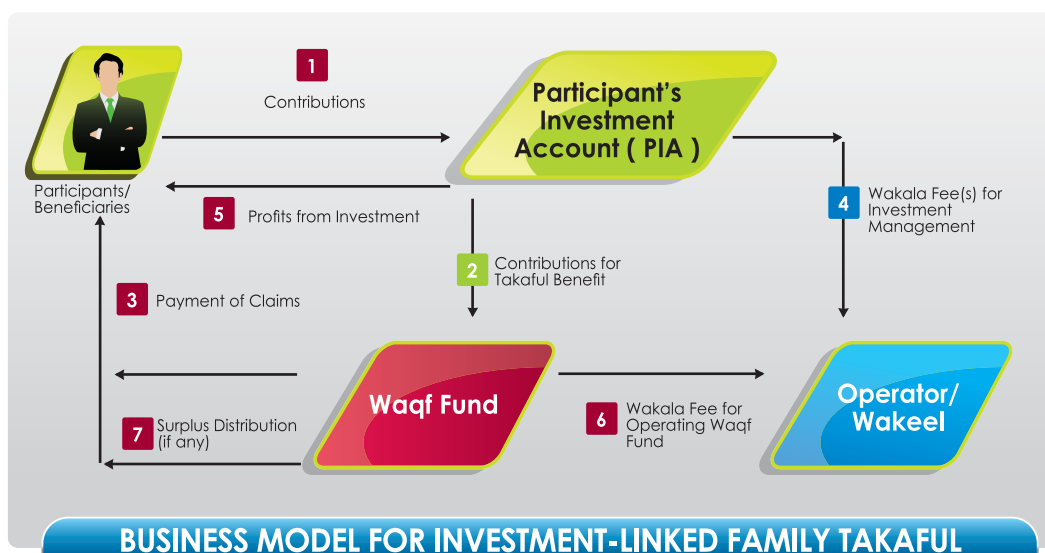
The funds available in the Waqf Pool are invested in Shariah Compliant business avenues. Any profits realized from these investments are returned to the Waqf thereafter.





THE ROLE OF THE COMPANY IN TAKAFUL SYSTEM

The company or the operator serves as the Wakeel or the Manager of the Waqf Fund and charges a 'Wakala fee' for it. This fee is paid from the Waqf Fund. As the Wakeel, the Operator must invest the funds available in the Waqf Pool in Shariah-compliant businesses for profits. Since the Operator is the Mudarib (working partner) and the Waqf Fund is the Rabul-ul-Maal (sleeping partner), any profits made from the investments are shared between the two on pre-defined percentages.



TAKAFUL



DIFFERENCE BETWEEN CONVENTIONAL INSURANCE AND TAKAFUL

	TAKAFUL	CONVENTIONAL INSURANCE
Nature of Contract	Contract of Guarantee (Aqd Kafala)	Conventional Insurance is a contract of Compensation (Aqd Mua'wza)
Contribution/ Premium	The Contribution paid to the Waqf belongs to the Waqf; the Operator is not the owner of this amount.	The premiums paid by the insured belongs to the insurance company
Investment Profit	Since the owner of the Waqf Pool is the Waqf itself, all investment profits also return to the Pool and not to the Operator.	In conventional insurance, all investment profits belong to the insurance company.
Claims	Payable from Participant's Takaful fund(Waqf Fund).	Payable from overall fund of the company
Surplus /Underwriting Profit	No provision for underwriting profit for the Operator. Can be given to the Participants only	Belongs to Company Shareholders. Insurance companies will make profit if the claims are lesser than the premium
Deficit	Qardh-al-Hasan is given to the Participants Takaful fund.	Financed from shareholders fund i.e. company
Shariah Supervision	A Shariah Board is an integral part of any Takaful setup which supervises the investment activities of the company. As per the Takaful Rules 2005, a Shariah Board comprising of at least 3 scholars is compulsory.	In conventional insurance, no such kind of supervision takes place nor is there any law concerning it. The insurance company simply invests their funds in any business they deem fit, irrespective if the business is Shariah-compliant and Halal.