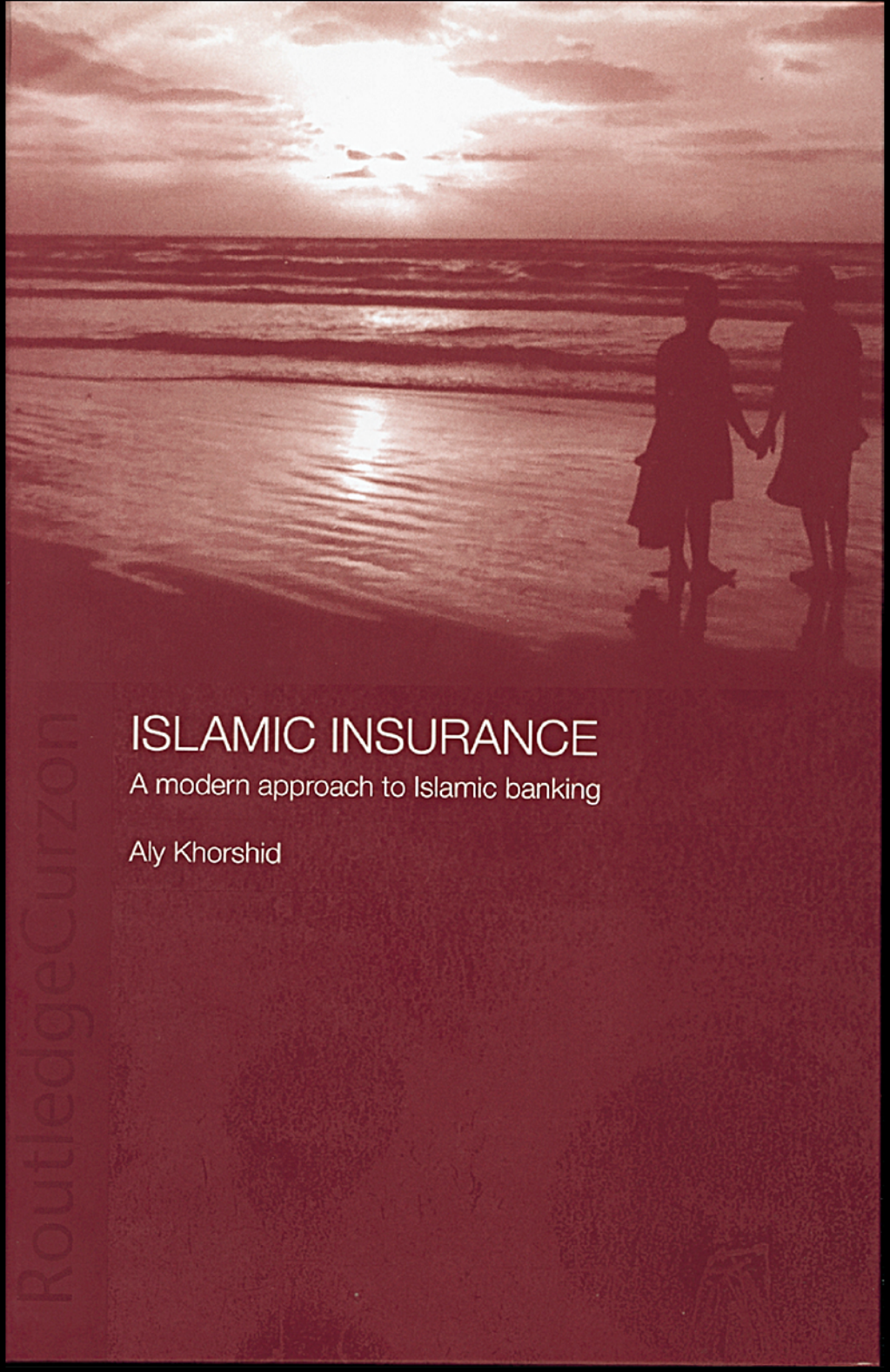

ISLAMIC INSURANCE

A modern approach to Islamic banking

Aly Khorshid

RoutledgeCurzon

ISLAMIC INSURANCE

Some Muslims believe insurance is unnecessary, as society should help its victims. 'Insurance', however, need not be a commercial venture. In its purest sense, it is assistance with the adverse effects of inevitable afflictions, an arrangement beneficial to all. Schemes to ensure the livelihoods of traders and communities have been in existence for millennia. Commercial insurance, on the other hand, was invented ostensibly for the same ends but with the chief beneficiaries being the shareholders and directors. Among the countless revelations Islam passed on, two prohibitions, namely *riba* (usury) and *gharar* (risk), have been used by legislators as grounds for the prohibition of insurance. Islam is not against making money, and there is no inherent conflict between the material and the spiritual. Islamic law allows *ijtehad* (initiative) to the benefit of the people as long as there is no harm to other people. Muslims can no longer ignore the fact that they live, trade and communicate with open global systems, and they can no longer ignore the need for banking and insurance. There is no prohibition in Islamic law against banking or insurance, similarly, Muslims can create insurance schemes that use their faith as the immutable basis for a working model.

Aly Khorshid demonstrates how initial clerical apprehensions were overcome to create pioneering Muslim-friendly banking systems, and applies the lessons learnt to a workable insurance framework by which Muslims can compete with non-Muslims in business and have cover in daily life. The book uses relevant Quranic and *Sunna* extracts, and the arguments of pro- and anti-insurance *jurists* to arrive at its conclusion that Muslims can enjoy the peace of mind and equity of an Islamic insurance scheme.

Aly Khorshid, born in Egypt, received his PhD from the University of Leeds in 2001. He is a researcher in Islamic economics, and a consultant to Islamic banks and Islamic institutions in both the Middle East and Europe. Besides being a company director, he is also on the board of management of several companies. Dr Khorshid has published various articles on Islamic economics.

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To my late parents
who would have been pleased
to see this book published
and to my wife Noha, and my children

CONTENTS

	List of tables	ix
	Introduction	xi
	Acknowledgements	xiv
1	The meaning of insurance in Islam	1
2	*Riba* (Usury) and *Gharar* (Risk)	31
3	Pre-modern and modern *jurists*' standing on insurance	44
4	The development of mutual insurance in the West	97
5	The development of Islamic banking and insurance in Malaysia: a case study	113
6	The development of Islamic banking and insurance in Saudi Arabia: a case study	132
7	Basic principles for an insurance scheme acceptable to the Islamic faith	155
8	Conclusions	166
	Appendix 1: *Mudaraba* for investment and savings and *Takaful* among Muslims (Shahab El-Din 1990)	173
	Appendix 2: Arabian insurance guide: Islamic re-insurance operating principles	180
	Appendix 3: Glossary of mutual insurance using case studies from the USA, Australia, Canada, Japan and Finland	183

Appendix 4: Glossary of Islamic financial terms 206

Notes 208
Bibliography 216
Index 223

TABLES

5.1	Number of financial institutions	128
5.2	Number of branches/Islamic banking scheme counters	128
5.3	Financing deposit ratio	129
5.4	Total assets 1994–March 2002	129
5.5	Total deposits 1994–March 2002	129
5.6	Total financing 1994–March 2002	130
5.7	Deposit services	130
5.8	Retail/Consumer banking	130
5.9	Corporate banking	131
5.10	Treasury/Money market investment products	131
5.11	Trade financing	131
5.12	Other products and services	131
6.1	Number of national and foreign insurance companies in the States of the Gulf Co-operative Council as at 31 December 1985	136
6.2	Financial situation of the NCCI, 1993–9	136
6.3	Growth (or fall) in Saudi insurance market by category	137
6.4	Policyholders' assets	147
6.5	Shareholders' assets	147
6.6	Policyholders' liabilities and surplus	148
6.7	Shareholders' liability and equity	148
6.8	NCCI financial highlights for 5 years (1997–2001)	149
6.9	Annual report – financial statements – balance sheet as of 31 December 2000 and 2001	149
6.10	Shareholders' assets	150
6.11	Policyholders' liabilities and surplus	150
6.12	Shareholders' liability and equity	151
6.13	Annual report – statements of insurance operations and accumulated policyholders' surplus for the years ended 31 December 2000 and 2001	151
6.14	Costs and expenses	152
6.15	Accumulated policyholders' surplus	152

6.16 Annual report – statements of shareholders' income for the years ended 31 December 2000 and 2001 152
6.17 Annual report – statements of policyholders' cash flows for the years ended 31 December 2000 and 2001 153
6.18 Cash flows from investing activities 153
6.19 Cash flows from financing activities 154

INTRODUCTION

What is it about insurance that is so divisive and emotive to modern Muslims? Is it not that Islam is a religion based on peaceful coexistence with fellow man, with the maintenance of stable and constructive societies? This second question is perhaps the most germane; the answer is yes, Islam is a society that cares for its most unfortunate members, the result of which is a community that can thrive, free from crime, bitterness and sorrow. And if this is the case, if communities and nations pull together to assist those most in need, there is a distribution of wealth and resources unrestricted by a nadir of charitability. The gains of the rich and comfortable, be they from skill or fortune, will help the poor with their losses, be they foolish or calamitous. Under a system such as this, why bother getting personal insurance?

There is another reason why insurance is frowned upon and outlawed in Islamic States and among Islamic communities: interpretation of many Quranic edicts brings the conclusion that insurance is not only unnecessary but highly unlawful Islamically. Chief among these are the outlawing of *riba* (usury) and *gharar* (risk). The lending of money at high rates of interest, or the payment of money for nothing are both linked with commercial insurance and contribute to its proscription. *Riba* is considered extremely anti-Islamic, and references to it pepper the Quran, each mention adding to its significance. Insurance is a risk. People in the West willingly pay money to insurance companies in order to buy peace of mind, with no guarantee of return. In one sense, never having to make a claim is a good thing as it suggests mishaps or tragedies have been avoided. In another, this means that the insurance company has literally been given the money, and the insured is out of pocket. Even the most generous no-claims bonus will not square this circle. To the Muslim, things that happen on earth are the will of God, and so to insure against them could be construed as questioning his actions.

Insurance is, however, something that the Muslim participates in five times a day; what is prayer if not a form of insurance premium in the hope of a divine dividend at the end of life? Faith itself is insurance, and the Quran states many examples of how worldly insurance is as sensible and as beneficial to community as is faith. This book methodically explores many of these

examples, and the conclusion that insurance is intrinsically bad begins to look unfounded.

An additional reason for Islamic proscription is that insurance companies can (indeed, need to) accumulate vast sums of money, much of which is invested. To be suitable for a Muslim to be the insurance company's customer, these investments must not be involved with forbidden aspects of Islamic life: things like pork and alcohol. Few insurance companies can give this assurance.

If the history of insurance is taken as a whole, commercial insurance is a relatively recent invention. This book details several historical insurance schemes where no money changes hands and several where it does. It is concluded that insurance, when applied Islamically and equitably, need not invoke anathema among Muslims, and can be used to the greater good of the community. Mutual insurance and Social Security systems are looked into to provide a basis on which a model can be founded.

Similar apprehensions have been experienced by Islamic States and organizations attempting to create Western-style banking systems for government and the populace. Two case studies – those of the Malaysian *Takaful* Act and Saudi Arabian systems – are used to demonstrate ways in which Islam and finance can, by focused and careful readings of *Sunna* and application of business sense, combine to create a system that is as acceptable to Muslims as it is to the financial world. Assurances that the bank does not partake in any transactions or decisions that would contravene the requirements of a truly Islamic life are given to investors, who can go on to benefit from a stable banking system safe in the knowledge that they are not infringing their devotion to God by proxy. While this book does not pretend that banking and insurance are one and the same, the two industries have undeniable parallels and banking can provide insurance with precedents. First, the physicality of the structures of the institutions is in many ways similar, and there are similarities between interest payments and overdraft charges and dividends and premiums. Second, the example of the *Takaful* Act in particular demonstrates how a desired end can be reached by inclusive intellectual, clerical and financial discussion with the beneficiaries being the general public and, therefore, community, nation and faith.

The fact that there is no mention of what we today would call insurance in the Quran is used as sufficient evidence that it is fundamentally wrong. Considering that the Quran is over a thousand years old, it is little wonder that there is no mention. There is also no mention of computers, aircraft or steam trains, but their introduction can largely be described as beneficial. Supporters of insurance consider the way in which insurance was introduced to the Islamic world (by Christian traders and sailors) and the timing of it (at a time of mutual mistrust between the two worlds) to be the sparks of the anti-insurance blaze, rather than any inherent wrong in an Islamically-designed and wholly beneficial system. Often, the result of the debate is conceived before Quranic interpretation is used to justify it – and interpretation can provide powerful arguments both ways when used by influential parties.

This book describes the Western approach to insurance in some detail. If nothing else it shows what a complex business insurance is, and will ensure that anyone attempting to formulate an Islamic insurance system takes a deep breath and is fully informed before embarking on a journey that will have to deal with prohibitions, legislation and financial perplexities. But at its heart, this description shows in no uncertain terms that problems and opposing interests can be overcome by time, conciliation, openmindedness and intellectual and governmental application.

Eventually, we must conclude that insurance is as natural a part of today's financial and societal framework as are banking and transportation, and that any individual, nation or religion that refuses to use it is at an immediate disadvantage, and the gulf between the Islamic and non-Islamic worlds can only widen. Islam is not anti-business – indeed, its Prophet Mohammed was himself a businessman of repute – so the principles of a fair system must be in place in order to thrive. By blocking a mechanism that allows business to experiment and cover losses, the world of Islam will ever be at a disadvantage – and there are many *jurists* who agree. Insurance does not have to contradict a single law of the Quran – these laws are unbreakable – but by careful consideration and cooperation, insurance can become a part of the Muslim's life.

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1

THE MEANING OF INSURANCE IN ISLAM

Introduction

To Muslims, Islam is a complete way of life that endeavours to construct the entire fabric of human life and culture in the light of values and principles revealed by God for man's guidance. The basis of Islamic belief is included below as a guide to readers unfamiliar with the details of the religion. In essence, Islam revolves around Mohammed's Revelation of the word of God, Allah, and a Muslim must adhere to His teachings, which are covered by the 'Five Pillars' of Islam.

The world of early medieval times, when Islam was young and starting its spread, was of course a very different place than the world of today or, indeed, of any period in the interim. Like any revealed faith, it has had to reinterpret – and then justify or forbid – trappings of an ever-changing human environment (the discoveries of lands hitherto unknown to adherents, new inventions, scientific discoveries, changing mercantile and financial methods, the migration and merging of civilizations and peoples, to name but a few). It was up to *Imams*, scholars and clerics to debate and decide whether an innovation or discovery could be circumscribed by Islamic teachings; their weighty opinions were and are hard to contradict, versed as they are in the technicalities and implied messages behind every passage of the Quran, just as a solicitor's knowledge of the minutiae of a legal Act is essential in fighting a legal case. In banking and insurance schemes that were benefiting Western traders and businesses, many of the scholars saw contradictions with Quranic teaching should their application spread to Muslim lands. The second part of this chapter explores Islamically legitimate banking as an example of how careful and fastidious interpretation, not the mere search for loopholes, can find practicable and beneficial solutions.

Islamic revelation

Just as Christianity is an updated version of Judaism, Islam is a more modern interpretation of Christianity. The three major religions of the world share many common points but jar on many others, the fundamental areas of disagreement

being the veracity of the two Prophets, Jesus Christ and Mohammed; Jews believe in the revelations of neither and Christians dismiss Mohammed's teachings. Muslims see the rapid spread of Islamic teaching and faith as proof that Mohammed's word is indeed the teaching of Allah himself, but since belief in revelation often has more to do with the personality and the miraculous deeds of its bearer than the truth in the teachings themselves, the Christian and pagan world of contemporaneous Europe checked Islam's growth, limiting its footholds to what are now Spain, Turkey and the Balkans. Its rise throughout the Middle East was, however, unstoppable, and European crusaders found anti-Islamic propaganda a sharper sword in the battle to retain power bases and sustain Christianity. This resulted in a deep-rooted scepticism of Islam in Europe that, despite starting to erode thanks to the works of non-Muslim scholars in the nineteenth and twentieth century, is still very strong.

The most absurd myths that historians have ever repeated are the legends of fanatical Muslims sweeping through the world and forcing Islam upon conquered races at the point of the sword. This contradicts the sense of justice that is one of the most wonderful ideals of Islam (DeLacy: (n.d.:8). As Naidu (n.d.:167) states, 'A sense of justice is one of the most wonderful ideals of Islam, because as I read in the Quran, I find these dynamic principles of life not mystical, but practical, ethics for the daily conduct of life suited to the whole world.'

But Islam has a still further service to render to the cause of humanity. It stands, after all, nearer to the real East than Europe does and it possesses a magnificent tradition of inter-racial understanding and cooperation. No other society has such a record of success in uniting in an equality of status, of opportunity, and of endeavours, so many and so various races of mankind. Islam still has the power to reconcile apparently irreconcilable elements of race and tradition. If ever the opposition of the great societies of East and West is to be replaced by cooperation, the mediation of Islam is an indispensable condition. In its hands lies the solution to the problems that Europe faces in its relations with the East. If they work together the hope of a peaceful issue is immeasurably enhanced. But if Europe, by rejecting the cooperation of Islam, throws it into the arms of its rivals, the outcome can only be disastrous for both (Gibb: 379).

Many Muslim economists believe that a re-orientation of this approach and a reconstruction of the entire framework of economic analysis and policy are needed if Muslims are not to be disadvantaged.

The Muslim economist starts from the assumption that economics neither is, nor can be, totally value-free; nor is it totally value-neutral. What is important is that this is hardly a desirable state of affairs.

By studying the way Islamic banking has overcome the restrictions placed upon it by the religion, restrictions that limit investors as much as the banks themselves, we can recognize ways in which insurance can become legitimized while remaining within a strict Islamic framework.

The concept of God in Islam

Every language in the world has one or more words to refer to God and to other lesser deities. Muslims maintain that Allah is the sacred and unique name of the one true God. The term has no plural or gender, in contrast to 'gods', or 'goddesses' of other religions. It is interesting to note that Allah is the personal name of God in Aramaic ('A branch of the Semitic group of languages spoken in parts of Syria and the Lebanon' (*Chambers Twentieth Century Dictionary*)), the language spoken by the ancient Jews and Jesus, and the sister language of Arabic.

To a Muslim, Allah is the Almighty, the Creator and the sustainer of the universe, with whom nothing can compare. The essential monotheism of Islam is summed up by a famous passage from the Quran:

> In the name of God, the Merciful, the Compassionate. Say (O Mohammed) He is God the One God, the everlasting refuge, who has not begotten, nor has been begotten, and equal to Him is not anyone.
>
> (112:1–4)

This passage introduces the idea of refuge, which earthly insurance caters for but is here provided forever by God.

God's attributes

According to Islam, if the Creator is eternal and everlasting, then it follows that his attributes must also be eternal and everlasting. God can neither lose any of these qualities nor acquire new ones. According to the Quran:

> God has not taken to Himself any son, nor is there any god with Him: for then each god would have taken off that which he created and some of them would have risen up over others. And why, were their gods in earth and heaven other than God, they (heaven and earth) would surely go to ruin.
>
> (23:91)

In Islam, as in other monotheistic religions, the concept of God is constantly equated with his oneness. There are innumerable Quranic verses that attest to this attribute, refuting the existence of other gods as false, for example:

> For ye do worship idols besides God and ye invent falsehood. The things that ye worship besides God have no power to give you sustenance; then seek ye sustenance from God, serve Him and be grateful to Him: to Him will be your return.
>
> (29:17)

The Prophet

The inspired man who founded Islam was born about AD 570 into an idol-worshipping Arabian tribe, the *Quraysh*. Mohammed's father died before Mohammed was born and, because he was orphaned at birth, he was always particularly sympathetic towards the poor, the widowed and the orphaned, as well as to slaves and downtrodden people. By his twentieth birthday Mohammed was already a successful businessman and became a director of camel caravans for a wealthy widow (Khadija). When he reached the age of 25 his employer, recognizing Mohammed's merit, proposed marriage. Despite her older years, he married her, and remained a devoted husband as long as she lived (Rahman 1981: 21). At Mohammed's own death, an attempt was made to deify him by some hysterical Arabs who thought that worshipping Mohammed was worshipping God, but the man who succeeded him (Abu Baker) resisted the hysteria, claiming the eternity of Allah.

Prophethood is not unknown among revealed religions, but in Islam it has a special status and significance. According to Islam, Allah created man for a noble purpose – to worship Him and lead a virtuous life based on His teachings and guidance. The Prophet was there to let humans know the role and purpose of their existence through clear and practical instructions from Allah. The Quran states that Allah has chosen from every nation a Prophet to convey the message to the people:

> We send not a messenger except [to teach] in the language of his [own] people, in order to [make] things clear to them. So Allah leads astray those whom he pleases and he is exalted in power, full of wisdom.
>
> (14:4)

The Prophet is the best in his community, morally and intellectually. This is fundamental, as a Prophet's life serves as a model for his followers. His personality should attract followers to his message rather than driving them away by an imperfect character. Once he has received the message he is infallible. Minor mistakes are usually corrected by further revelation (Iqbal 1987: 583).

The content of the Islamic Prophet's message to mankind not only defines a clear concept of God and His attributes, the Creation, the unseen world, Paradise and Hell but also God's purpose for human beings, the rewards for obedience and punishments for disobedience. Furthermore it lays out how to organize society according to God's will – clear instructions and laws that, when justly applied, will result in a happy and ideal society (Rahman 1981: 22).

The role of the Quran

Islam asserts that humanity has received divine guidance through only two channels: first, the word of Allah and, second, the Prophets who were chosen by

Allah to communicate his will to human beings. These two concepts of God and Prophet go hand in hand and any attempt to understand one without the other is doomed to failure (Amin 1985: 22).

In the tradition of major monotheistic world religions, Islam is unique in that its scripture, i.e. the Quran, was revealed during the lifetime of its last Prophet, Mohammed. The Prophet himself was also responsible for its revelation, a divine manifestation, and after his death the task of compiling and preserving the Quran fell to the companions of the Prophet and, later, the Caliphs. The preservation and maintenance of the original manuscript (*Hafiza*) is well documented. Eventually, once copies were made, the holy work left Arabia to have a huge impact on what were to become Muslim territories beyond Arabia (Al-Sharawi 1988: 109).

Muslims believe that, as the last revealed book of God, the Quran was preserved, as it was to become the book of guidance for all humanity. As evidence of this they point to the universality of its address in that it speaks to all mankind: 'O Man! What has seduced you from the Lord?' (4:1), and:

> O Mankind! Fear your Guardian Lord who created you from a single person, created out of it his mate and from them twain scattered like seeds, countless men and women.
>
> (4:1)

The concept of worship in Islam

The concept of worship in Islam is commonly held to mean performing ritualistic acts such as prayer, fasting and charity. This somewhat limited concept of worship is only a small part of its significance in Islam. The traditional definition of worship in Islam is a comprehensive one that includes almost everything in an individual's daily activities. Everything, in fact, that one says or does to please Allah (Al-Sharawi 1988: 2:128).

Islam looks at the individual as a whole. He or she is required to submit completely to Allah, as the Quran instructed God's prophet Mohammed:

> Say [O Mohammed] my prayer, my sacrifice, my life and my death belong to Allah; He has no partner and I am ordered to be among those who submit [i.e. Muslims].
>
> (6:162)

The natural outcome of such submission is that all aspects of life are organized according to the instruction of God. Islam, as a way of life, requires that its followers model their life according to its teachings in every aspect, religious or otherwise.

It is worth emphasizing that even performing one's social duties and responsibilities is considered a form of worship. The Prophet deemed that acts

done for the benefit of the family are considered acts of charity. Familial duties such as feeding and clothing members of one's family and kin also constitute worship. Even enjoyable, pleasurable activities, providing they are performed according to the instructions of the Prophet, are considered acts of worship. The key here would appear to be conforming to Islamic norms. If an activity conforms to the guidelines laid down by God through his Prophet, all actions related to its performance can be considered to be worship.[1]

Although the non-ritual aspects of worship are many, and embrace all aspects of life, this should not detract from the importance of ritual worship. Such acts, if performed in true spirit, elevate people morally and spiritually, enabling them to carry on their daily activities according to the guidance of God. The ritual aspects of worship are referred to as the Five Pillars of Islam.

The five Pillars of Islam

Islamic faith is built on five 'Pillars'. The irreducible Pillar is a state of faith, a belief in the oneness of Allah. Branching from this belief (which is volitional and could be described as an action) are four other activities of faith, each of which is a vital part of Islam. The ritualistic Pillars are well known to the non-Muslim world, the frequency of their being carried out ranging from daily to at least once in a lifetime. Their respective relevance to insurance will become clearer; as a guide to readers with little knowledge of Islam, the Five Pillars are a good starting point from where to explore the ethos of the religion.

A discussion of the ritual and non-ritual aspects of Islamic worship reveals that although the ritual aspect is more clearly defined, Muslims believe that all activities, provided they conform to Islamic norms, promote love of God as He alone is the provider of this code of life. It is clear that the concept of worship in Islam is a comprehensive one that regulates human life on all levels – individual, social, economic, political and spiritual – providing guidance in every detail. In theory at least, Muslims believe that this complete code of life leaves a believer in no doubt as to how to live and work, encouraging all Muslims to strive to please their God who knows and sees everything (Ghazali 1990).

The first Pillar: Shahada (witnessing)

Shahada is a state of faith and reflects a genuine belief in Allah and testifies his oneness and, consequently, the rejection of any other deity. Of the Five Pillars, this is the one that encompasses all others, the tip of the pyramid. Adherence to the other four is irrelevant without this fundamental belief.

The second Pillar: Salah (prayer)

Salah is the verbal testification that there is but one God and that Mohammed is His messenger. It is a ritual prayer that occupies a key position for two reasons:

first because it is the distinctive mark of the believer, and second because it precludes, in theory, an individual from all sorts of sin and temptation by providing him with direct communion with his Creator five times a day, and allows him access to correct behaviour. Regarding Allah, the Quran states: 'You alone we worship and You alone we turn to for help. Guide us to the straight path' (1:5,6).

The third Pillar: Zakat (poor-dues)

Zakat (poor-dues) is an important pillar of Islam. In the Quran, *Salah* and *Zakat* are generally mentioned together. Like *Salah*, *Zakat* is a manifestation of faith that affirms that God is the sole owner of everything in the universe, and that what men possess is merely entrusted to them. God ultimately makes trustees of His believers. This is illustrated by the verse: 'Believe in Allah and His messenger and spend of that which He made you trustees' (57:7). In this respect, *Zakat* is an act of devotion which, like prayer, brings the believer nearer to his Lord.

Aside from its spiritual significance, *Zakat* is, in practice, a means of redistribution of wealth in a manner that narrows the gap between classes and groups, thereby contributing to social stability. Muslims believe that the practice of giving alms to the poor purges the souls of the rich of selfishness and the souls of the poor of envy and resentment against society. *Zakat* is therefore not always a personal act of worship. Where it is not given freely it can, if necessary, be exacted by force.

The fourth Pillar: Seyam (fasting)

Seyam (fasting during the daytime during the month of Ramadan) is a well-known pillar of Islam. The main function of fasting is to make the Muslim pure 'from within', just as the other aspects of the *Shari'a* make him pure 'from without'. Muslims hold that by fasting, and engaging in the spiritual purity fasting brings, they are able to respond to what is true and good and shun what is false and evil. This principle is outlined in the Quranic verse: 'O you who believe, fasting is prescribed for you as it was prescribed for those before you, that may gain piety' (2:183). In a well-authenticated tradition, the Prophet reported Allah as saying (of the Muslim): 'He suspends eating, drinking, and gratification of his sexual passion for my sake.'[2]

The fifth Pillar: Al-Hajj (the pilgrimage)

Every year on the ninth day of *Zou al-Haja* there is a pilgrimage to Mount Arafat and Mecca. It is the duty of each Muslim to take part in this pilgrimage at least once in his lifetime, provided he is financially and physically able. It is a very important pillar of Islam, and displays a unity unique to the religion. Muslims

from all corners of the world, wearing the same dress (to signify equality regardless of wealth, colour, language, etc.) respond to the call of *Hajj* in one voice and language: '*Labbaikah allahumma labbaik!* [Here I am at your service, O Lord!].' Muslims performing the *Hajj* are required to exercise strict self-discipline and control, not least because Mecca is a holy place where sacred things are revered. Even the life of plants and birds is made inviolable so that all elements are in harmony: 'And he that venerates the sacred things of God, it shall be better for him with his Lord' (22:30). The pilgrimage is in response to the call made by the Prophet Abraham (the Father of the Prophets) on this day.

Islam's moral system

Islam has laid down some universal fundamental rights for humanity as a whole, which act in the same way as insurance cover. Such rights and obligations are to be observed and respected in all circumstances. To achieve these rights, Islam provides not only legal safeguards but also a moral system. Thus, whatever leads to the welfare of the individual or society is morally justified and promoted. Whatever is injurious to either is morally bad. Islam attaches great importance to the love of God and to the love of man but warns against too much familiarity. The Quran states:

> It is not righteousness that ye turn your faces towards East or West; but it is righteousness to believe in God and the last day and the Angels, and the book and the messengers; to spend of your substance, out of love for Him, for your kin, for orphans, for the needy, for the wayfarer, for those who ask, and for the ransom of slaves; to be steadfast in prayers, and practise regular charity; to fulfil the contracts which ye made and to be firm and patient, in pain [or suffering] and adversity and throughout all periods of panic. Such are the people of truth, the God-fearing.[3]
>
> (2:177)

This verse provides a Muslim with a picture of a righteous, God-fearing man. Such a man should be firm and adhere to such beneficial regulations, but he should also not neglect love of God or his fellow human beings. This is the standard by which a particular mode of conduct is judged and classified as good or bad. Such guidelines provide the nucleus around which a system of moral conduct should revolve. Before laying down any moral injunctions, Islam seeks to plant firmly in the human heart the conviction that human dealings are with God, who sees everything at all times and in all places. The human being may hide from the whole world but cannot hide from God; he or she may deceive everyone but cannot deceive God; he or she can flee from the clutches of everyone but God. Islam, therefore, makes God's pleasure the objective of human life and by this it has established a system and standards of morality which pave the way for the moral evolution of humanity.

By making divine revelation the primary source of knowledge, Islam gives a permanent anchor to its moral system with some scope for adaptation and innovations. This scope does not, however, allow for moral fluidity. It provides a sanction to morality in the love and fear of God, which impels humanity to obey the moral law even without external pressure being exerted. Through belief in God and the Day of Judgement it provides a powerful persuasive force for a person to adopt moral conduct.

Islam's moral system lays down a way of life which is based on promoting good and preventing evil. Through this system, conscience and virtue should prevail. Those who respond to this call are gathered together into a community and given the name 'Muslims'. The singular object underlying the formation of this community (*Umma)* is that it is commanded to embrace goodness and eradicate evil. The basic moral teachings of Islam cover the various aspects of a Muslim's life – the broad spectrum of personal moral conduct through to social responsibilities.

The consciousness of God

The Quran specifically mentions the consciousness of God as the highest level a Muslim should aspire to: 'The most honourable among you in the sight of God is the one who is most God-conscious'[4] (49:13).

Humility, modesty, control of passions and desires, truthfulness, integrity, patience, steadfastness, and the fulfilment of one's promises are all moral values that are emphasized throughout the entire Quran, as in the following verses:

> And God loves those who are firm and steadfast.
>
> (3:146)

> . . . and vie with one another to attain to your sustainer's forgiveness and to a Paradise as vast as the heavens and earth, which awaits the God-conscious, who spend for charity in time of plenty and in time of hardship and restrain their anger, and pardon their fellow men, for God loves those who do good.
>
> (3:133–4)

In a way that summarizes the moral behaviour of a Muslim, the Prophet said:

> My sustainer has given me nine commands: to remain conscious of God, whether in private or in public; to speak justly, whether angry or pleased; to show moderation both when poor and when rich; to re-unite friendship with those who have broken it off with me; to give to him who refuses me; that my silence should be occupied with thought; that my looking should be an admonition; and that I should command what is right.

The gratitude and fear of the Muslim believer

Islam requires its followers to surrender themselves to God and to believe in the oneness of God, in the sense of His being the only Creator, the only one worthy of worship whom no craven images can replace. In addition to this a Muslim is also required to have faith in God, the evidence and proof of which lie in his actions. The Prophet is quoted as saying: 'None of you [truly] believes until his inclination is in accordance with what I have brought.'[5] The whole concept of Muslim faith is bound with the idea that a Muslim is grateful to God for the feelings of euphoria his faith gives him. This gratitude is, in fact, the essence of *ibadah* (worship). A non-believer is called *kafir*' which means 'one who denies a truth' and also 'one who is ungrateful'.[6] A believer loves, and is grateful to God for the bounties bestowed upon him, but is aware of the fact that his actions, whether mental or physical, are far from godly. A Muslim, in theory, should always be aware that he will have to atone for his sins, either in this life or the hereafter. He, therefore, fears God, surrenders himself to him and serves him with great humility. Such a mental state means that Muslims should, at all times, be mindful of God. Such awareness of God is therefore the life force of faith, without which it would fade and wither away.[7]

Social responsibilities of the Muslim

Islam's main assertions concerning social responsibilities are based on kindness and consideration for others. Since a broad injunction to be kind is likely to be ignored in specific situations, Islam lays emphasis on specific acts of kindness and defines the responsibilities and rights of various relationships. In relationships, a Muslim's first obligation is to immediate family, parents, husband or wife and children, then to other relatives, neighbours, friends and acquaintances, orphans and widows, the needy of the community, fellow Muslims and, finally, fellow man and animals.

Respect and care of parents is stressed in Islamic teaching and is a very important part of a Muslim's expression of faith.

> Your sustainer has decreed that you worship none but him, and that you be kind to parents, whether one or both of them attain old age in your lifetime. Do not say to them a word of contempt nor repel them, but address them in terms of honour. And, out of kindness, lower to them the wing of humility and say: 'My sustainer!' Bestow on them your mercy, even as they cherished me in childhood (17:23–4).[8] And render to the relatives their due rights, as also to those in need, and to the traveller; and do not squander your wealth in the manner of a spendthrift.[9]
>
> (17:26)

On the subject of neighbours, the Prophet Mohammed is reported to have said:

> He is not a believer who eats his fill when his neighbour beside him is hungry; and does not believe whose neighbours are not safe from his injurious conduct.[10]

According to the Quran and *Sunna*, a Muslim has to discharge his moral responsibilities not only to his parents, relatives and neighbours, but also to the whole of mankind and animals, trees and plants – to life itself. So, on the level of essential moral characteristics, Islam builds a comprehensive system of morality which aims to realize the potential of humanity.

Traditional Islamic financial instruments

For great periods of post-classical history, the Middle East has been the hub of trade for the known world. Its geographical location made it a stop-off, a warehouse, and a stock exchange for traders from every part of the known world. Spices, minerals, foodstuffs, fabrics, luxurious and essential from all its surrounding regions passed through its ports. Of course, different regions, with their own prevalent belief systems, also had their own financial instruments. To some lawmakers of what is now known as the Middle East and, therefore, of Islam, these transactional devices breached a fundamental prohibition of the Quran, namely *riba*. It has been used as the main factor in prohibition since the insurance industry's introduction, and deserves close attention. Indeed, the use of the word 'industry' is in itself telling: the implications are obvious yet, as will be seen, it is overcoming this element of insurance that offers the very solution for an Islamic system.

Approximations (meanings) of insurance – *Aman* and *Ta'min*

The noun *Aman* denotes security, peace, safety, protection. *Ta'min*, the word which one usually associates with insurance in Islam, is the *masdar* of the second form, *ammana*, to re-assure, safeguard, guarantee. The derivative noun, *amin*, denotes a guard or a secure place. *Amin*, for example, constitutes one of the designations for Mecca.

Imana is the *masdar* of the fourth form *amana* (to believe), and denotes fidelity, loyalty, confidence, trust. The noun *Iman* denotes faith, belief in. The tenth form, *istaamanah*, denotes a request for protection or for indemnity. These are some of the derivatives of *Amina*, all of which combine to produce a common meaning of peace of mind, trust and lack of fear (*Al Mujmaa al Wasit*, 1964: 1:38).

References to *Aman* in the Quran

There are said to be 879 instances of the word *Aman* or its derivatives in the Quran (Al-Baqi 1958: 81–93), the majority in the form of the noun *Iman*. In *surat al Nisa* (Quranic chapter), for example, there is the following:

> And if one of you deposits a thing on trust [*Amina*] with another, let the trustee faithfully discharge his trust [*u timana amanatahu*] and let him fear his Lord.
>
> (4:58)

and in *surat Yusuf* (Quranic chapter) we read that:

> God commands you to render back your trusts [*ammanat*] to those to whom they are due.
>
> (12:64)

Furthermore in *surat al Qassas* (a Quranic chapter) one reads:

> He said 'Shall I trust you (*Amina*) with him with any result other than when I trusted with his brother's aforetime?'
>
> (28:26)

And finally, in *Surat Al Umran* there is a telling homily:

> Among the People of the Book are some who, if entrusted [*Ta'min*] with a hoard of gold will readily pay it back [whilst] others, who if entrusted with a single silver coin, will repay only on demand.
>
> (3:75)

Peace of mind, absence of fear, protection of the self, protection of one's wealth and one's offspring, protection against the vicissitudes of fate, poverty and disease, protection during travel and protection of one's residence are all encompassed within the Islamic understanding of insurance, under the following three classifications:

1 Faith as insurance (*al-Ta'min al Imani*).
2 Insuring the Hereafter (*al-Ta'min al Akharuwi*).
3 Worldly insurance (*al-Ta'min al Dunyawi*).

Pre-modern *jurists'* standing on insurance

Ibn Abdin's strictures on marine insurance

Having completed a survey of Islamic financial instruments in practice, these will now be evaluated in the light of the *juristic* interpretations of *Shari'a* prescriptions on insurance. However, the current system of insurance, with its structure and rules, is a modern invention, reflecting the absence of any guidelines or provisions for Islamic *jurists* in the past. It is considered both modern and alien, part of the influx of foreign laws and rules brought to

Muslims from the West during the latter part of the nineteenth century. Ibn Abdin[11] was the pioneer *jurist* who wrote about insurance; he was followed by many modern Islamic *jurists* and scholars in this field. This chapter will review, analyse and contest their views.

Ibn Abdin wrote about marine insurance only because it was the first of its kind that came into existence in Islamic countries. The reason for that was the extensive commercial activity between East and West during the booming industrial revolution in Europe, as the foreign traders who used to visit Muslim countries required some kind of insurance to guarantee their import deals.[12]

Ibn Abdin referred to the issue of marine insurance in his treaties entitled 'Scrutinized Answers for Dispersed Questions', particularly in a chapter titled 'The Trust of the Unbeliever' in the section on 'Al jihad' (The Holy War) in a postscript. There he wrote:

> It was customary that if traders wanted to hire a boat from a non-Muslim owner, they made their payment of rent to that man, as well as depositing a certain amount of money with another non-Muslim agent who lived elsewhere on Islamic territory. They used to call that deposit the 'sowkra' which was proposed against all kinds of risks that might occur to the boat or its contents during the journey, such as fire, sinking or piracy, etc. The agent was paid for his services as a warrantor and his appointed proxy, who lived in the coastal area of Islamic territory, collected the Sawkara from the traders, with permission from the Sultan, and accordingly repaid them the equivalent of the damage done to their goods at sea, if any.

Having given that vivid account, Ibn Abdin added that 'It seems to me that the traders have no right for any money to be returned to them in lieu of their perished goods, as that would be a commitment to offer something non-committable.' Hence, he believed, such a kind of insurance was illegal from the point of view of the *Shari'a*. It would be a void and groundless contract as it was based on the guarantee of an uncontrollable event. Ultimately, no Muslim living on Islamic territory could be allowed to have a contract with an insurer in an Islamic region, unless the contract was totally compatible with the revelation and teachings of Islam. Under such a financial deal, from an Islamic point of view, it would not be compulsory for the insurer to repay the insured any money for any unforeseen risk. The trader should also be involved only in the payment of the necessary minimum, such as normal fees and charges collected from visitors to Jerusalem.[13]

Ibn Abdin, in defending his viewpoint against any possible disputation that might arise, referred to the depositee who would charge the depositor for keeping the deposit. In such a case, the element of guarantee had to be intact, as the depositee was responsible for the safekeeping of the deposit whilst in his possession. That is unlike the case of insurance where the money was not in the

possession of the Sawkara payer, but always in the possession of the boat owner. But, if the Sawkara payer were the same boat owner, then he would be a hireling responsible for both labouring and safekeeping. However, neither party could guarantee the avoidance of natural risks such as death or drowning.

He also referred to some other kinds of pledge that differ from insurance. If a guarantor pledged the safety of somebody by tempting him to travel a certain route for his own security, then any money taken against that pledge should not be in the form of insurance. In that case, the guarantor, owing to ignorance of the real degree of danger, would not actually be in a position to guarantee the real safety of the traveller. But, if he were able to ascertain how dangerous the travel paths were, then he would be legally entitled to a commission, just as the depositee was. However, the rule would be that 'The tempter should not guarantee unless he is in firm knowledge of the danger ahead.'

Ibn Abdin was trying to clarify the difference between insurance in the case of a boat's sinking and in the case of highway robbery. Both cases appear to be incompatible with 'the rule of guarantee'. However, in the case of the recipient of Sawkara, there is no intention to tempt traders while being ignorant of the potential dangers. The condition for the guarantee is that the danger has to be known to the tempter but not the tempted. On the other hand, in the case of robbery, both parties have to know the volume of danger to the same degree, otherwise the condition of guarantee would not be fulfilled.

The goal Ibn Abdin wanted to achieve was to highlight the conflict between insurance and a pledge. He wanted to prove, at one and the same time, the absence of temptation on the part of 'the insurer', and ignorance of the expected danger on the part of 'the insured'. Thus, any commitment by the insurer would be illegitimate, and the insurance could never be a legal pledge, as in the case of the deposit.

Ibn Abdin differentiated between the insurance contract concluded in a non-Islamic territory and that concluded in an Islamic territory. He suggested the following views:

1 If a Muslim trader, having a non-Muslim partner, had an insurance contract with a 'Sawkara' recipient in an Islamic land, who collected the insurance deposit in lieu of the perishable goods, it would be legal for the trader to regain the money, as the contract was conducted between two non-Muslim parties on Islamic territory, if the money was restored to the trader with his consent.
2 If that trader was living in a non-Muslim territory, where he had made the insurance contract, it would be legal for him to collect the insurance money in the Muslim territory because of the imperfection of a contract issued in a non-Muslim territory. It would be allowed as he would be in receipt of money from a non-Muslim, although insurance is illegitimate and unjust if it rewards unforeseeable risks, but the injustice is being done to non-Muslims with his consent.

3 If the contract was signed in an Islamic region, but the settlement of the contract occurred in a non-Islamic region, the trader would not be allowed to receive any insurance money in lieu of the perished goods even with the consent of the non-Muslim party. That is because the void contract was issued in an Islamic region.

From this set of arguments, we can first conclude that marine insurance, which used to exist in Ibn Abdin's time, was taboo as it entailed a commitment in relation to the unforeseeable on the part of the non-Muslim insurer. Nor was it a legitimate form of pledge based on specialist knowledge imparted to the traveller or trader to enhance his security in return for a commission. As such it had to be an illegal contract to be avoided in Islamic territories. Second, Ibn Abdin makes clear that Islamic rules and provisions should only be implemented in Islamic territories. According to the Abu Hanifa school of Islamic law, Muslims should not be liable for their deeds outside Islamic territories, even if they are responsible for the same deeds inside Islamic territory. The justification for this is that the *Imam* of Islam would not be capable of executing the restrictions that God has placed on man's freedom of action outside of his jurisdiction.

However, Ibn Abdin also argued that 'A Muslim is allowed to commit in the non-Islamic region only what he is allowed to commit in the Islamic region.' In the same way, the *Imams* Shaf'i, Malik and Ibn Hanbal decided that Muslims should be liable and loyal to Islamic regulations wherever they are. Eventually the matter was decided by the interpretation and application of the *Ulama* (the ruling of Islamic *jurists*). The predominant trend calls for Muslims' thorough devotion and commitment to the restrictions imposed by Allah, and the principles and values of Islam at all times and in all places. Nonetheless, the Abu Hanifa school of Islamic law considers the power of Islam, which enables the *Imams* to apply Islamic provisions as conditional in circumstances of war, especially for Muslim prisoners in non-Muslim countries. However, it is not credible that *Imam* Abu Hanifa intended to appeal to Muslims who move to non-Islamic countries to renounce the religious rules and conduct of the *Shari'a*.

Islamic banking in the West

Conventional banks and their regulatory authorities were initially sceptical about a system of banking whose guiding principles were based on religious values and ethics. But the 1990s have seen several Western banks considering establishing their own Islamic banking units. Attracted by the enormous growth potential, they hope to use their expertise to create sophisticated deals to generate innovative solutions to the problems facing Islamic investors.

London is already fast becoming a centre for handling Islamic financial instruments, where deals are arranged by established banks such as: ANZ Grindlays, Citibank International, Kleinwort Benson, Saudi International Bank

and the Al-Rajhi Banking & Investment Corporation (ARABIC). The Dallah Al Baraka group and the United Bank of Kuwait (UBK) also have a number of investment companies in London (ibid.: 56).

Cooperation and integration

Eddie George, the Governor of the Bank of England, told the Arab Bankers Association (ABA) in London in 1994 that he welcomed the presence of well-run Arab banks in Europe's largest financial centre, although he recognized the difficulties in finding satisfactory means of accommodating the principles of both Western and Islamic banking within a single regulatory structure. He argued that these problems will have to be solved if institutions are to be permitted to offer more general Islamic banking facilities in the UK:

> One such problem is how to classify Islamic funds in terms of the British legal framework. To what extent, and in what precise forms, are funds placed with an Islamic institution 'capital-certain', thus falling within the UK's Banking Act definition of deposits or to what extent are they participating in a collective investment scheme, falling under the Financial Services Act? My understanding is that Islamic funds may fall into either of these categories or indeed others, but we certainly need to deepen our understanding of the developing principles and practices in this area. But whatever form they take, I think it is likely that the concepts will be familiar to the supervisors and regulators here; and that we can find satisfactory answers to these questions, perhaps through the organizational structure.
>
> (Ibid.: 1997: 57)

With the exception of Denmark, the rest of Europe has, as yet, shown little interest in Islamic banking. But growing EU trade with the Muslim world, and an increasing Muslim population in Europe, mean that there is an untapped demand for Islamic banking services. The real competition tends to be between Western institutions themselves, which have developed strong Islamic trade finance departments. They are structuring deals in cooperation with Islamic investors and banks. Some such banks have their own *Shari'a* advisers.

At the retail banking level in the Arab world, the major conventional banks have made few developments of their own in offering Islamic banking services. But the growth of private Islamic companies and the subsequent collapse of the largest investment company, Al-Rayan, has encouraged Egypt's four big banks to reconsider. These banks, which include the National Bank of Egypt, now accept deposits for *Mudaraba* profit-sharing and offer Islamic financing for small-business clients. With their deposits growing steadily, conventional Arab banks can now offer a secure environment for Muslim depositors and investors.

Insurance and the Islamic contractual framework

The contenders for arguing the validity of insurance, along with the advocates of its permissibility, generally try to assimilate the insurance contract into one of the Islamic nominate transactions. The advocates insist on this assimilation in order to provide evidence that insurance is totally in breach of Islamic law, as it does not comply with the regulations of the contract that it is deemed to correspond to. The contenders assert that insurance is equivalent to an Islamic contract, and therefore is valid being within the provisions of the *Shari'a* and indirectly acknowledged by it (Moghaizel 1990: 162).

Insurance and Mudaraba

Mudaraba, one of the major Islamic concepts, is referred to in the context of insurance[14] and it is often evoked to provide an 'Islamic' insurance scheme.[15] *Mudaraba orgirad* is a major exception to the prohibition of *gharar*. It is a contract whereby one party (*rabb al-mal*) entrusts a sum of money to another party (*Mudarib*) to trade with for an agreed percentage of the profits (Ibn Qaduma 1972: 5:22). The latter is deemed to be the agent to the provider of the capital.

It is essential that the respective shares of the profits are fixed on a proportional basis, and do not consist of a lump sum. The profits are allocated after the return of the capital to the investor. There may even be a multiplicity of investors entrusting capital to a *Mudarib* (ibid.: 46–8). The agent is free to conduct his trading according to commercial practice if no particular restrictions have been stipulated by the investor. He can deduct the expenses that he incurred from the capital handed to him and the contract can be terminated at will, by either party, even if a duration has been fixed for the contract.[16]

A hire contract is considered as an invalid *Mudaraba* (*Ijra*) and in this case the agent is remunerated by a wage and does not share the profits and is entitled to his business expenses only (Al-Sharkhasi 1913: 22:67).

Conventional insurance, as it is practised today, is not a *Mudaraba* contract. Firstly, the intention of the parties to form a *Mudaraba* contract is non-existent.[17] What the insured is seeking is security and an eventual return. The insurer invests the premiums as his own funds and he alone gets the profits (except in mutual insurance and with-profit life policies). Obviously, in non-life policies, the premiums paid by the insured, which some identify with the capital of the investor in a *Mudaraba* being paid by instalment, are not returned to the policyholder. The payment of the sum insured, if it takes place, is not equivalent to the sum of the premiums paid by the insured plus profits. If it were so, the insured would then only get the sum of his savings invested, and the concepts of distribution of risk and pooling of premiums, which are at the heart of insurance, would be missing.

Therefore, a *Mudaraba* contract in which the capital invested must be returned with any eventual profits, and where there is a possibility of loss which will be subtracted from the invested capital, is not in any respect close to the established idea of insurance. In relation to with-profit life insurance policies, the intention of the parties to *Mudaraba* (that the share of the profit allocated to the investor is a proportion of total profits and not a lump sum) is lacking.

In with-profit policies the returns that the insured benefits from are essentially different from the *Mudaraba* returns. While addendum found in policies state that 'It should be clearly understood that the amounts payable on policies taken out now may be more or less than those shown', this does not render the contract a *Mudaraba*.

In fact, under a with-profit policy, the death benefits, in case the life-insured dies before the due date of his returns under the policy, will usually be equal to a lump sum computed on the basis of the monthly premium (e.g. 250 times the monthly payment).

This is clearly in conflict with *Mudaraba* rules, which include, as a requirement of utmost importance, the determination of the profits on a proportional basis. The sanction of the contradiction of this rule invalidates *Mudaraba*.

If the insured does not die before the policy matures, the returns that he or she will obtain are initially fixed as lump sums, with the clause mentioned above included in the policy and warning the insured that the returns cannot be precisely forecast, since rates of interest and inflation, which affect investments made by the insurer, may vary. Such returns, even if they are not precise pre-determined lump sums, do not consist of a proportion of the profits made by the insurer on the investment of the total of the premiums paid by the insured, as is the case in a true *Mudaraba* contract.

It is fair to surmise that today's established concepts of insurance are not *Mudaraba* contracts. It may be possible to change such policies in such a way that would put them in the ambit of *Mudaraba* contracts without depriving them of their main function – providing financial security to the insured. There seem to be no affirmative answers to the question: 'Can the mechanism of *Mudaraba* contracts as regulated by the *Shari'a* be a convenient support for an insurance scheme?'(Uways 1970: 102–4).[18]

The first mechanisms to be excluded are all indemnity policies. Obviously, the sum insured should always be a lump sum, equal to the contingency faced by the insured. Any amendment to this aspect would upset the basic principle underlying such policies. As far as the adaptability of life insurance (with profit) to *Mudaraba* contracts is concerned,[19] the following objections leave little doubt that such an enterprise would be pointless.

First, the *Mudarib* or agent is not held liable if the capital handed to him is lost while in his trust if he was not responsible for the loss. This means that in case of unsuccessful investment, an investor could lose all his capital without having any claim against the agent. Any clause to the contrary would invalidate the *Mudaraba*[20] and however remote and improbable the chances of actual loss

may be, such potentialities, which should be stated in the contract, would certainly not be suitable for a person seeking financial security and contemplating a considerable return on precious savings. In this regard current life policies undoubtedly contain less *gharar* than the contract of *Mudaraba* (Ibn Qaduma 1972: 5:44).

Second, the *Mudaraba* is primarily a contract between two parties and not a collective contract. The mixing of capital, provided by various investors at different stages, is subject to a number of restrictions such as the prerequisite condition that no subsequent *Mudaraba* is valid if it is liable to prejudice the previous one (ibid.: 46). Such potential prejudice is, in each individual case, inescapable.

The third objection is that the *Mudaraba* can be terminated at will by any of the parties to it (Ibn Rushid 595 AH: 2:240), even if the duration has been laid down in the contract. Any clause to the contrary would be null and void.[21] Thus the insured would be able, at any moment, to rescind the contract and insist on having his capital returned to him (Al-Mardawi 1986: 5:448). This permanent facility to rescind, to which the insured is entitled, is yet another major impediment to the use of *Mudaraba* in the creation of an 'Islamic' insurance scheme, since the insurer will not be able to invest in any venture in which money is not available on demand.

A fourth point is that in a *Mudaraba* the agent cannot entrust the capital of the investor to another person or institution for investment without the express authorization of the investor. It is obvious that the insistence of such authorization or any other requisite express authorization, consistent with the rules governing the *Mudaraba*, can easily be made in the contract between the 'insured' and 'insurer'. However, the need for express authorization is yet another confirmation that the *Mudaraba* contract is only intended to be a transaction between two persons whereby an owner of capital can trade with it by retaining the services of an agent, bound to abide by the instructions of the provider of capital, as the agent is working for him even though the agent is not considered an employee.

It is the concepts of intent and context, under which the *Mudaraba* contract is regulated, that prevent it being adaptable to a collective project like insurance. The very nature of *Mudaraba* necessitates the absence of even the most elemental principles of an insurance contract.

Fifth, it should also be noted that the profits of *Mudaraba* cannot be stipulated for the benefit of a third party (Ibn Qaduma 1972: 5:64–5). In the case of the death of the investor, the returns under the contract will be distributed to the legal heirs in accordance with the Islamic inheritance rules and cannot be paid specifically to the spouse and/or children of the investor whom he may wish to benefit. In the case of a life policy, the sum insured, being paid out of the estate of the insurer, is not subject to the inheritance rules applicable to the distribution of the properties which form the estate of the insured, who as a result can designate any beneficiary he wishes.

While *Mudaraba* may be a useful mechanism for Islamic banking,[22] the situation is markedly different in insurance. Each contract has a different role and is therefore regulated in a dissimilar, and even irreconcilable way, even if it is presumed that the investor had relinquished some of his rights (such as the right to impose restrictions on the agent as to the country and field invested in). However, as this concept is one of the most 'daring' Islamic contracts, the temptation to try to introduce it as a support for new transactions was great.

The introduction of insurance through *Mudaraba* has been achieved through combining it with other concepts, such as the principles of solidarity and mutual help amongst Muslims which are completely alien to a genuine *Mudaraba* contract. This resulted, in many respects, in the misconstruing and misapplication of *Mudaraba*.[23] The fact is that the original *Mudaraba* was undermined by being taken out of context and put into a totally different one.

We can conclude that capitalism cannot be 'Islamicized' by introducing *Mudaraba* in all economic transactions (Moghaizel 1990: 172).

Insurance and waqf

Waqf is the retention of a property that cannot be sold, and assignment of the usufruct (Ibn Qadumah 1972: 5:544) for the benefit of a charitable or humanitarian objective, or for a specified group of people, such as the members of the donor's family.[24] The profits and returns produced by the property subject to the *waqf* belong to its beneficiaries and, if they are succeeded, it then goes to the closest relatives of the stipulant or, according to another Hanbali opinion, to the poor (ibid: 569). *Waqf* is a contract, despite the fact that it is constituted by a unilateral act and does not need the consent of the beneficiaries,[25] who in many cases are a category of people such as the poor or destitute.

Waqf must be perpetual and cannot be temporary. The founder of each one states: 'This property is a *waqf* for one year for the benefit of X'.[26] The founder of a *waqf* is motivated by humanitarian considerations. He strives to aid the community and thereby be rewarded, after death, for his charitable act. Although, *waqf* of movables is not generally prohibited, *waqf* of money is not allowed under Hanbali law.[27] Furthermore, a *waqf* dependent upon a contingency is not valid except where such a contingency is the death of the founder of the *waqf* (ibid.: 571).

Waqf must not contain any stipulation which contradicts its object; for example, the entitlement of the stipulant to revoke the *waqf* at will (ibid.: 551–2). The founder cannot designate himself as a sole beneficiary of the *waqf*. He can, however, provide for his right to spend the products of the *waqf* in a manner benefiting others (ibid.: 550–2; Ibn Rhajab 1970: 131).[28] He can also devote the *waqf* to a category of people to which he belongs (Al-Khafif 1941: 2:463).

Waqf is administered and managed by a *Mutawalli* or a *nazir* for a remuneration. He is appointed by the founder who may appoint himself as a

Mutawalli when constituting a *waqf*. The *Mutawalli* has the powers to carry out all acts which are advantageous to the *waqf* and its beneficiaries in compliance with the stipulations defined by the founder and recognized by the *Shari'a*. The use of the *waqf* mechanism in order to set up a valid insurance scheme has been advocated by Muslim *jurists*.[29] However, no such scheme seems to have so far materialized because the insurmountable obstacles inherent in the rules regulating *waqf* damage the feasibility of this sort of project.[30] Some of these obstacles follow.

1 *Waqf* is a kind of *Sadaqa*, that is, a charitable and pious donation, aimed at obtaining a reward after death. The motive of the founder is to get closer to God by disposing of a part of his property for the benefit of others who are in need of it. By contrast, in conventional insurance, the insurer is not motivated by a pious and charitable intention when he insures his property or liability. He is motivated not by a feeling of responsibility towards the community but by the wish to preserve his assets. A *waqf*, initiated by any motivation other than piety, is not a true *waqf*. As far as life insurance is concerned, where the beneficiaries are clearly third parties, the motivation of the founder to provide for his heirs and secure for them a decent life might be seen as a valid basis for constituting a *waqf*.[31] However, other fundamental impediments still exist in relation to the nature of the property which is the subject of the *waqf* and its beneficiaries.

2 One of the conditions pertaining to the subject matter of *waqf* is its perpetuity[32] so that any property which cannot be benefited from except by being disposed of or consumed cannot form the subject matter of a valid *waqf* (Ibn Qaduma 1972: 5:585). This means that as far as money is concerned, the sums payable in compensation of a loss sustained by a beneficiary of the *waqf* must proceed solely from the profits made out of the lawful investment of the money subject of the *waqf*, without deducting any amount from the capital raised and pooled by the founders of the common *waqf*. Thus, in order to secure the payment of all compensations from the returns obtained on the investment of the capital of the *waqf*, such capital must be substantial and would be beyond the *waqf* of the average person. In addition during the first years the insurers would have to wait until a fund is constituted out of the capital raised and invested in order to provide for the payment of compensation to the prejudiced beneficiaries.

   It is evident that such a scheme is not practical, or even feasible, because of the nature of *waqf* as a retention of property and allocation of the returns it produces to designated beneficiaries.

3 It might be said that in the context of an insurance scheme, each founder will designate as beneficiaries the group, or those insured, participating in the scheme. The fact is that a number of people will leave the group of beneficiaries when they wish to put an end to their participation in the scheme. On the other hand, new contributors will be taking part in the

scheme. The consequence is that the beneficiaries of the common *waqf* will constantly change. This is strictly prohibited by Hanbali law and leads to the invalidity of the *waqf* itself (ibid.: 552).

4 It might also be said that it is acknowledged by the *Shari'a* that the payment of benefits must be dependent upon certain qualifications which would, in this case, be the condition that payment be made only to those who have suffered prejudice due to a loss or damage sustained (ibid.).[33] While this point of view may be useful in setting up an insurance scheme in the form of *waqf*, it should be pointed out that a stipulation making the payment of benefits conditional upon an uncertain event's happening[34] may meet objection stemming from the position of Hanbali law with regard to additional stipulations in a *waqf*, an area in which their interpretation is not flexible.

Any valid clause must contribute to increasing the charitable and pious nature of the *waqf*. The principle here is not the validity of clauses, in contradiction with the object of the *waqf*, but rather the irrelevance of all clauses inserted by the founder of the *waqf* if they are not of the essence of the *waqf*.

In addition to the foregoing, other rules governing *waqf* form obstacles to its introduction into an insurance plan. An example of such obstacles is the requirement that the beneficiaries be determined.[35] In the case of insurance the beneficiaries (the other insured persons) are not known to the founder and they change continually.

So, as a result of its specific nature, it is evident that *waqf* cannot serve as a vehicle to set up an insurance scheme.

Other Islamic financial instruments

Insurance and onerous donation

The onerous donation, *hiba bi shart al-awad*, whereby a recipient commits himself to perform an obligation in return for a gift, is an accepted Islamic principle (Al-Khafif 1941: 2:468). It is, however, considered a sale (Yusuf 1969 2:330) and is therefore subject to the provisions applicable to such a contract.[36] Many commentators have argued that a transaction such as this is indeed an onerous donation, or at least a rudiment of it (Qardawi 1978: 226; Izz al-Din Bahr al-Ulum 1979: 37–9). Others argue that it is difficult to agree with this view, as one of the conditions of a valid *hiba bi shart al-awad* is the determination of compensation to be awarded by the recipient (Al-Khafif 1941: 2:468; Yusuf 1969: 2:330) and such a transaction is not possible in insurance, since the sum insured, payable by the insurer (recipient), depends upon the extent of the prejudice suffered by the insured (as is the case of indemnity insurance) and is thus impossible to determine in advance. Moreover, the application of the rules relating to sales renders the contract invalid because of *riba*, among other

things, caused by the disparities between the sum of the premiums and the sum insured in both life and non-life insurance.

Other Islamic laws used to 'legitimize' insurance

Comparisons drawn between insurance and Islamic contracts are aimed mainly at legitimating insurance by demonstrating that similar practices are acknowledged by Islamic law. In the latter case, it is not a question of identifying insurance in terms that appear to validate it in Islamic law, for while this may be an interesting academic exercise, the similarities are purely accidental. Many proscribed transactions appear to have similar principles to insurance but it must be borne in mind that these contracts were designed for completely different contexts. Many contractual mechanisms have been subject to such analogies. The principal ones are touched upon in the following paragraphs.

Kafala (guarantee)

The validity of *Kafala*, which usually involves an undefined subject matter, is often cited. An example of this would be if one says: 'I stand as surety for all debts of X' (Ibn Qaduma 1972: 4:536). This has been seen as a commitment, comparable to the duty of the insurer to pay the sum insured, as is the case of liability insurance (Al-Zarqa 1962: 57; Al-Muhmud 1986: 68–9).

The idea of a similarity between *Kafala* and general insurance practices has been rightly dismissed (Bakhit 1906: 4). Their only common feature, the transfer of liability, cannot alone justify such comparison, as the disparities between the two are too numerous.[37]

Diyya (blood money)

Insurance, in general, has also been compared to *diyya* – a sum of money paid as a compensation by a group of people (often the tribe) on behalf of a person who unintentionally killed or injured someone, often to prevent any retaliation on the part of the victim's family. Such comparison, however, is flawed, as in this latter case there is no contract between the group of people paying the *diyya* and the person who committed the unintentional crime.

Ji'ala

This is a contract whereby one person promises to reward another unspecified person in exchange for carrying out a specified task. This contract is deemed exceptionally valid because of the need for it (Ibn Qadumah 1972; Al-Khafif 1941: 2:332–3; Ibn al-Qayyim 1968: 2:5), in spite of the considerable amount of uncertainty involved in it. *Ji'ala* is evidently far from being similar to the insurance contract.

Muwalat

Muwalat is the contract whereby one party agrees to bequeath his estate to the latter, on the understanding that the benefactor will pay any *diyya* that may eventually be due by the former. This contract is invalid in Hanbali law, which rejects contractual inheritance (Ibn Qadumah 1972: 6:381). *Muwalat* has often been described as a kind of liability insurance (Al-Zarqa 1984b: 1:560; *a contrario* Muslehuddin 1966: 179).

Comments on Islamic insurance loopholes

It is clear that the insurance contract *per se* cannot be reduced to one of the above-mentioned transactions, and therefore cannot be seen as indirectly legitimated by Islamic law. However, some conclusions can be drawn from the existence of such mechanisms. For example, the *Shari'a* embodies a number of contracts which, like insurance, are inherently aleatory (e.g. *Kafala*, *Ji'ala*) albeit in exceptional situations. Such practices were allowed because of the demand for them and because they did not involve potential iniquities leading to unjustified gain and advantage for one party, with corresponding disadvantage and unfair loss for the other. In this manner, *gharar* should not be seen as a paramount prohibition applicable without regard to its consequences and context. It is not forbidden.[38]

Other considerations come into play where *gharar* is concerned, such as the role of the transaction in question, the rationality of the need for it, and the eventual causes of unlawful gain that would result from it. These elements are the determinant factors in the validity of the principles of 'exceptional contracts', that is, contracts which do not fall within the limits of the major transactions (such as sale, gift or hire) regulated by Islamic law. None of these exceptional transactions would apply normally if the principles regulating contracts were applied without consideration to specific situations.

It should also be acknowledged that insurance has often been compared to other Islamic contracts and, as a result, has been held to be invalid. It has been equated, for example, as a contract of *sarf* (exchange money) and thus been declared invalid, due to the disparity between the sums paid by each party (because of the existence of *riba* in the contract) (Muslehuddin 1966: 177). This may be fine in theory, but in practice insurance is certainly much more complex than a contract of *sarf* involving a mere exchange of commodities. First, an insurance contract involves payment of the sum insured, which will not be paid out if the event insured against does not occur. The possibility of this is made clear for both parties at the time of the conclusion of the contract. A contract of *sarf*, on the other hand, contains by its very definition an exchange of values which is certain to take place, otherwise it ceases to be a *sarf* contract.

Additionally, one cannot disregard the elements inherent in insurance, such as the pooling of premiums, the determination of the sum insured according to

the prejudice suffered in indemnity insurance, and other such insurance mechanisms which bear little relation to a simple contract of barter.

To reiterate, it would appear that methods which merely study the validity of new contracts and attempt to fit them forcibly into nominate Islamic contracts spring from a prejudiced view of the *Shari'a* and have been proven to be unwarranted. A more appropriate route to follow is to make use of the contractual freedom afforded by Islamic law, rather than insisting on an obsolete scheme of basic nominate transactions, acknowledged, at the time they were devised and recognized by the *Shari'a*, as highly sophisticated and able to serve the needs of that time. As far as insurance is concerned, it is obvious that as a concept it does not correspond to any of the nominate contracts of Islamic law and, more importantly, it cannot be adapted to fit these, whatever modifications are devised, without being deprived of its major features.

Insurance and Zakat

Zakat is one of the five pillars of Islam, which is liable to be a source of gain. It represents the solidarity of the rich with the needy prescribed by Islam. The purpose of *Zakat* is to provide assistance to those who lack the basic necessities of life. It is often thought that, in relation to insurance, *Zakat* could be considered as an Islamic alternative to insurance. The beneficiaries of *Zakat* are enumerated in the Quran:

> The alms are only for the poor and the needy, and those who collect them, and those whose hearts are to be reconciled, and to free the captives and the debtors, and for the cause of Allah, and [for] the wayfarer.
>
> (Surat al-Tawba (Repentance): 9:60)

It is worth noting that the phrases 'In the way' or 'cause of Allah', are very flexible notions that could be extended to an unlimited number of situations, where there is a justified need for financial help, such as medical aid and scholarships (Al-Sha'rani 1975: 49–58). *Zakat* and other such wealth distribution practices sanctioned and demanded by Islam play an important role in alleviating the prejudicial consequences of supervening risks (Abd al-Rasul 1968: 115). However, *Zakat* cannot replace insurance, as in many respects it is a profoundly different concept.[39] *Zakat* is paid in order to please God and is a compulsory Islamic duty. Insurance is, in most cases, voluntary. The payment of *Zakat* aims at providing for the needy, whereas the insured's intention is to secure for himself financial assistance in case of misfortune. As for social security, risks covered by *Zakat* are mainly social risks. *Zakat* is based on the solidarity of the community's members and the duty of the State to promote social justice. *Zakat* is therefore akin to social security, as noted earlier (ibid.: 49) and is considered part of the Islamic social security system.

It is precisely for this reason that *Zakat* cannot be considered as providing an alternative to insurance. Insurance mainly covers non-social risks, and *Zakat* has no provision for this. In any case, *Zakat* funds would not be technically applicable to insurance, as its contributions are proportional to taxable property and bear no relation to the indemnity payable in cases of misfortune. Consequently, *Zakat* funds would not adequately protect against risks other than social risks, and were such a modification forged it would negate the essence of *Zakat*, which would be unthinkable from an Islamic point of view (Moghaizel 1990: 189).

The evolution of Islamic financial institutions – some examples of implementation

The practice of many modern Islamic scholars to put forward Islamic alternative economic theories and the emergence of 'Islamic' financial institutions is a relatively recent phenomenon and is still in a formative phase. The Islamic banks are well known today as the very first 'Islamic' firms to be set up. Over 45 Islamic banks and other financial institutions currently operate according to the 'Islamic' interest-free profit-and-loss system (PLS) (Wilson 1987: 10).

Four principal legal techniques used by Islamic banks are the contracts of *Mudaraba*, *Musharaka* (whereby both the customer and the bank contribute to providing capital dedicated to a specific venture), *Ijara* (lease financing) and *Murabaha* (cost plus trade financing) (Al-Ashkar 1987: 32–5). The achievements of Islamic banks have been judged by many as very successful (Parker 1987: 23–6), while other less enthusiastic commentators have expressed more cautious opinions because, in the end, the success of these institutions depends to a great extent on their competitiveness and their performance in the international markets (Delwin 1986: 8, 16–20).

A problem faced by 'Islamic' financial institutions in general, and Islamic banks in particular, has been the lack of an appropriate legislative framework to support their establishment and promote their growth. This problem has, to a considerable extent, been eased by the enactment of special regulations, sensitive and applicable to the nascent Islamic financial structure.

One example of this new legislative trend is the Pakistani *Mudaraba* Ordinance,[40] which arose from the Islamicization of commercial laws in Pakistan. *Mudaraba* is defined as 'Business in which one person participates with money, and another with efforts or skills or both his efforts and skills, and shall include Unit Trusts and Mutual Funds.' The establishment and the control of the scheme is the duty of a registrar, especially appointed, as well as a tribunal created for this purpose. The *Mudaraba* is either a multi-purpose or a specific-purpose *Mudaraba* and it can be either for a fixed period or for an indefinite period; *Murabaha* is used to fund trade-related transactions on a cost-plus funding basis (Parker 1994: 14).

What is specific to the Pakistani *Mudaraba* Ordinance, as compared with the Malaysian Islamic legislation, is that the religious supervisory board, charged

with checking the lawfulness of the operations conducted, is constituted by the government, and not by the company concerned, by virtue of a clause in its articles of association. The religious board, which has the power to order modifications, is required to give a certificate in writing, stating that the *Mudaraba* is not contrary to the *Shari'a*. This certificate is a prerequisite of the authorization which allows the floatation of the *Mudaraba*.

Section 18 of the Ordinance requires that the apportionment of the profits between the company and the investor be computed in such a manner that the former's portion does not exceed 10 per cent of the net annual profits. When 90 per cent or more of the annual profits are distributed to the investors, the income of the *Mudaraba* is exempted from income tax. The final notable point of the *Mudaraba* Ordinance is that, by virtue of Section 14, the company is required to circulate to all investors its annual balance sheet and profit and loss account, the auditors' report and a general report on the *Mudaraba*'s activities and prospects.

Another example of recent Islamic legislation is the Islamic Banking Act of 1983 and the *Takaful* Act (1984) of Malaysia.[41] Under the Islamic Banking Act of 1983, Islamic Banking has to be transacted by an Islamic bank (which cannot be a foreign bank) specially licensed for that purpose. The bank's activities must be subject to the control of a religious advisory body in charge of ensuring that the bank is not carrying out its business in a manner contrary to Islamic law.[42]

The Central Bank of Malaysia is granted wide supervisory powers over Islamic banks. It can demand that the bank hold a minimum amount of liquid assets at all times,[43] can also impose restrictions on credits granted to a single customer,[44] and enjoys the conventional investigatory powers of Central Banks under conditions of secrecy. Section 34–1 provides for banking secrecy. This ideal is somewhat compromised by a qualification exempting from secrecy the Central Bank and a competent minister, whose task it is to direct the Central Bank to investigate books, accounts and transactions of the bank if he 'has reason to believe the bank is carrying on its business in a manner detrimental to the interests of its depositors', in which case the Central Bank may also assume control of the business of the bank.[45] Finally, it should be noted that the implementation of the Islamic Banking Act 1983 led to consequential amendments of a number of other Malaysian laws.[46]

Another example of Islamic legislation which is relevant is the Turkish Decree No. 83/7406, dated 16 December 1983, concerning the foundation of Special Financing Institutions allowing Islamic banking in Turkey.[47] As Turkey is formally a secular State, the Decree does not expressly cite Islamic financial institutions and does not mention the *Shari'a* or any religious supervisory board, but it does establish profit-and-loss sharing financial institutions, which are services offered by Islamic banks.

These Special Financing Institutions administer current accounts on which no return is paid, as well as participation accounts, whereby the funds are deposited against a 'contract to participate in the profit and loss of operations'.

The Special Institutions, which are submitted to the control of the Central Bank and the Prime Minister's office[48] may finance commercial and agricultural activities, give letters of guarantee for projects abroad, and procure and sell in instalments or lease to firms the relevant equipment to secure investment. The new regulations are laid down in a manner which ensures an advanced and profitable integration in the economy. The Special Financing Institutions are regarded as ventures leading to beneficial financial results for the economy by mobilizing deposits through various investment channels, rather than as an opportunity for Muslims to invest their money in a manner sanctioned by the *Shari'a*, as is the case with certain 'Islamic' commercial legislation in force in other countries. This is hardly surprising given that, in Turkey, the introduction of the new Islamic regulations provoked opposition from those deeply committed to the secular character of Turkish law. Accounts may be opened by Turkish citizens working abroad in a foreign currency[49] and a special procedure has been established enabling those depositors to transfer abroad the profits earned on their account (although the Prime Minister may order that these profits be invested in a specific enterprise and field).

It is evident from this legislation that structures permissible in a *Shari'a* framework are being transplanted into existing conventional economic systems. Without qualifying, for the moment, the success of such structures, it might safely be said that the concept of an Islamic enterprise has arisen in practice, and efforts are being made to elaborate this concept in legal terms. However, it is too early to pass a definitive judgement on the viability of the new institutions and how competitive and lucrative they are likely to be.

The main feature of an 'Islamic' enterprise is that it must be acceptable to Islam and the *Shari'a*. Therefore, it has to adhere to a set of rules which embody Islamic restrictions as to the nature of the contracts entered into by the firm, and the investments made, stemming from the prohibition of *riba* and prejudicial *gharar*.

Prospects for the future

The marketplace became increasingly crowded with Islamic institutions in the 1990s. In June 1991 Saudi Arabia's largest bank, the National Commercial Bank, started its own Islamic banking division and hopes to become the market leader within five years. Kuwait's International Investor, which opened in 1992, has already established itself as one of the most innovative institutions in Islamic capital markets, having negotiated a KD143m deal to lease seven Airbuses to Kuwait Airways.

However, Islamic commercial banks in the Gulf and elsewhere have continued to suffer from short-term losses as a result of the difficult financial climate faced by their clients, and profits are generally low. The Faisal Islamic Bank of Egypt lost US$54m in 1991 and Al-Baraka lost US$13m in 1990 in London, although Al-Rajhi has maintained its position as the strongest and

most profitable of the Islamic commercial institutions, largely thanks to the stability and resilience of the Saudi economy (Wilson 1997: 61).

The future lies in the continued development of Islamic banking instruments, by Islamic bankers, economists and *Shari'a* scholars. Although the *Shari'a* sets out key principles to be observed in business, it does not provide a detailed, codified body of financial law. The development of new financial products is therefore a complex issue, as Islamic financiers seek to apply Islamic ideals to transactions, while accommodating contemporary commercial needs and the demands of a sophisticated business environment.

Methods of accounting which currently vary between Islamic banks and countries will need to be harmonized for the better comparison of statistics and the successful development of international banking relationships. Basic monetary management principles will also need to be agreed on and standardized to increase inter-bank cooperation.

The general public, who often think of Islamic banking principles as consisting solely in prohibiting interest on savings, will need to be better informed about the services available. If Islamic banking is to attain its market potential, small depositors need to be attracted by accurate information about a broad range of financial products. Banks will need to reduce their current dependence on *Ijara* (leasing) and *Murabaha* (cost-plus) – often popular because of the low risk associated with the practice – and be forced to develop genuine profit-and-loss (PLS) investments (Siddiqi 1985: 112).

Conclusion

God revealed the Quran to his messenger Mohammed, whose life and teaching (*Sunna*) has been donated to Islam according to God's guidance. Muslims believe that the Quran, revealed to Mohammed and preserved by God, became the book of guidance for all humanity, and is furthermore the final message from God to all people and completes the doctrines of Judaism and Christianity. Muslim worship is a gratitude to God in the form of testifying to God, praying, paying *Zakat*, fasting and pilgrimage. The Muslim argument against material insurance posits that since society has an obligation to care for its weak and unfortunate, the self-protection granted by an insurance policy has no place in society.

Modern authors are trying to devise an economic system which would be consistent with Islam yet differ from capitalist consumer society, whilst acknowledging the principle of private property. One prerequisite of such a system is that contractual and economic public policies must be strictly and precisely framed by positive legislation, so that the supervisory body, in charge of controlling the conformity of transactions with Islamic rules, does not act with full authority. This is particularly relevant in those cases where the supervisory body is appointed and remunerated by the company (and would then tend to be complaisant with its policy), as well as when this body does not

come under the company's remit (where it would then be inclined to follow a restrictive pattern according to each situation). The whole issue depends upon the consistency of the economic alternative structure proposed by modern *jurists*, such as whether it proves to be a real alternative rather than a formal amendment of the capitalist system. This is far from being the norm, as 'Islamic' economic methods generally materialize in isolated ventures and not as part of a radical reform of existing models.

The implementation of the concept of 'Islamic' insurance did not coincide with the emergence of Islamic banking. The formation of insurance companies proposing Islamically lawful insurance policies started no earlier than 1983, and, unlike Islamic banking, the field has so far remained unregulated except in rare cases, the most significant being Malaysia. It is surprising that Saudi Arabia has so far achieved very little in this regard.

2

RIBA (USURY) AND *GHARAR* (RISK)

Riba

A principal argument against insurance, one whose case is strong and deserves careful analysis, is that of the Quran's and *Shari'a*'s banning of usury and other forms of economic transaction which are deemed to be unproductive or to give unfair advantage to one party at the expense of the other. The history of insurance as it developed in the Arab world has traditionally been limited to joint sharing of common risk. This is a slight deviation from the purely societal interpretation of the mutually caring community, as particular interest groups could individualize risk to their collective advantage, even when it could benefit their competitors. The Islamic concept of insurance is, we recall, not primarily an economic or material concept, but one based on faith in God and the daily following of Islamic moral law which, under the protection of God, enhances security, well-being and prosperity in this life, and ensures a heavenly life hereafter. This chapter details those Islamic legal, *juristic* and Quranic codes that have a bearing on insurance. As will be seen, the whole concept is interwoven with the principles of the faith.

Usury (*riba*) in the *Shari'a*

Modern definitions

At the root of the anti-insurance argument is the Islamic objection to *riba*, lending at interest. The literal translation of the Arabic verb *riba* is derived from the Arabic root *raba* and means 'increase' and refers to the practice of lending money at an exorbitant (and therefore unlawfully high) rate of interest. The noun *riba* literally means surplus excess. Some English definitions of the word 'usury' are: 'the practice of loaning money at an exorbitant rate of interest' (*Collins Dictionary*) and 'an addition to the principal of a loan, usually interpreted as interest payments or receipts for both commercial and private loans' (Wilson 1987). The word has unsavoury connotations (being connected, for example, with Hitler's anti-Semitic reasoning) and, since the level at which

'exorbitant' is reached is less than clear, accusations of it can be levelled against money-lenders of any kind at the whim of those in power. The word *riba* is applied where there is a perceived additional increase in an object of transaction over and above its original value, size or amount (Wilson 1985: 24). As a technical term, *riba* means usury and interest, and in general any unjustifiable increase in capital for which no compensation is given.

Traditional usage

In the pre-Islamic era *riba* – as it was then practised – was generally held to be the increase of money in consideration for an extension of the term of maturity of a loan. Pre-Islamic Arabs would pay premiums on loans and would receive a certain amount, leaving the principal sum untouched. When the maturity date expired they would claim the principal sum from the debtor. If it was not possible for the debtor to repay this sum they would increase the principal sum and extend the term. It was transactions like these with a fixed time limit and payment of interest, as well as speculation on the part of the lender, that formed an essential element in the trading system of the pre-Islamic era (Al-Tabari 1978: vol. 4). A debtor who could not repay the capital, either in money or in goods, with its accumulated interest when it fell due, was given an extension of time during which to pay. However, the sum due was then doubled. Such practices are clearly referred to in the Quran (Kurashi 1945: 89).

Quranic injunctions concerning *riba*

In the Quran, the first verse dealing with *riba* is in *Surat al-Rum*:

> That which ye do for increase through the property of other people, will have no increase with God: but that which ye lay out for charity, seeking the countenance face of God will increase. It is these who will get a recompense multiplied.
>
> (30:9)

According to Quranic exegesis,[1] this was revealed in Mecca before the emigration (*Hijra*) to Madina, that is, before the prohibition of *riba* which the verse heralds. Another verse which mentions *riba* prior to its formal prohibition is:

> For the iniquity of the Jews we made unlawful for them certain food goods and wholesome things which had been lawful for them, in that they hindered many from God's way. That they took usury, though they were forbidden, and that they devoured Man's substance wrongfully. We have prepared for those among them who reject a grievous punishment.
>
> (4:160,161)

The first express prohibition which mentions *riba* and bans it for the first time is: 'Oh ye who believe! Devour not usury, doubled and multiplied; But fear God; that ye may really prosper' (3:130). This was the first verse directly to impose a ban on usury. In interpreting this verse, the exegesis agrees that the expression 'multiples' does not ban the practice of charging interest in general but rather describes the usury practices of the day. In this they assume that the concept of multiples of multiples is no more than a description of a state of affairs, which was a precursor to the imposition of the ban (Kotb 1978: part 1:130).

Later verses, however, reveal an intensification of this prohibition:

> Those who devour usury will not stand except as stands one whom the Evil one by touch hath driven to madness. That is because, they said, trade is like usury; but God hath permitted trade, and forbidden usury. Those who after receiving direction from their Lord, desist, shall be pardoned for the past, their case is for God to judge; but those who repeat the offence are companions of the fire: they will abide therein for ever.
>
> God will deprive usury of all blessing, but will give increase for deeds of charity: for he loveth not creatures ungrateful and wicked. Those who believe, and do deeds of righteousness and establish regular prayers and regular charity, will have their rewards with their Lord: On them shall be no fear, nor shall they grieve.
>
> Ye who believe! Fear God and give up what remains of your demand for usury, if you are indeed believers. If ye do it not, take notice of war from God and his Apostle: but if ye turn back, ye shall have your capital sum; deal not unjustly, and ye shall not be dealt with unjustly.
>
> (2:275–9)

In these verses *riba* is both condemned and prohibited in the strongest possible language, whilst trade or industry which increase the prosperity and stability of individuals and nations is considered legitimate. Dependence on usury is seen as facilitating unproductive activity. The Quran also advocates further concessions on behalf of debtors (2:280). Creditors are asked: 1 to relinquish past claims arising out of the practice of usury; 2 to give time for payment of capital if a debtor is in financial difficulty; or 3 to write off the debt altogether as an act of charity. The Quranic verses condemning *riba* clearly prohibit any unlawful acquisition of wealth at the expense of others. This condemnation is applied to different practices, either by individuals or by nations, the principle being that any profit that a person acquires should be through his own exertions and not through exploiting others (Yousuf 1938: 1062). The Quran regards *riba* as a practice of non-believers. It demands, as a test of belief, that it should be abandoned.

The Quran does not prohibit all forms of profit derived from business transactions. The usury mentioned therein applies to debts and is not related to

sales and purchases. Usury in sales is not subject to the stipulations of the Quranic verses (Al-Masri 1987a: 52). Here the use of the term usury, although a general one, is intended to give a specific meaning: that of the practices of usury in the pre-Islamic era, which involved doubling and multiplying of debt.

The Prophet's sayings on Riba

The Prophet's authenticated sayings (*Hadith*) that deal with the subject of *riba* are numerous, so only a small number of them will be mentioned here. The usury condemned by the Quran is 'debt usury' whereas the *Sunna* mainly deals with the concept of 'sale usury'. Although debt usury is mentioned in *Hadith* literature, the *Sunna*'s contribution to the subject confines itself merely to enforcing the Quranic injunctions against *riba* and outlining in detail exactly what is banned. It is generally understood that *riba*, as forbidden in the Quran, refers to interest on loans. Anything that goes beyond this is regarded as a later development. According to Issa (1974), the study of economics did not begin until the eighteenth century, although the idea of economic thought came much earlier (also documented by Al-Najjar (1974), who agrees with Issa's differentiation between science and ideas).

The first example of the Prophet dealing with debt usury was when a tribe, the *Thaqeef*, claimed repayment of its debt from another tribe, the *Bani Muqeera*. This was a past debt remaining from pre-Islamic usury practice. The Prophet told the *Thaqeef* that the Quran ordered the abandonment of such practices. The second time the Prophet encountered the old problem was when he spoke in his last sermon (on the occasion of the farewell pilgrimage). The Prophet is quoted as condemning usury among members of his family:

> Every usury is disparaged, and the first usury I disparage is ours [Abbas Bin Abd Al-Muttalib's usury – i.e. the Prophet's relatives' usury]. It is all disparaged.
>
> (Salus 1990)

The *Sunna* serves to underline and clarify the prohibition of debt usury as originally outlined in the Quran. This example illustrates the way in which the *Sunna* confirms the prohibition of debt usury and prescribes and bans sale usury. The *Hadith*'s view on sale usury is illustrated by a group of traditions. There are a considerable number of *Hadith*s which deal with this subject, but the most famous and generally accepted is:

> Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates and salt for salt, the like for the like, hand to hand [*yad-in-bi-yad*, i.e. immediate sale]. But if the kinds differ, then sell as you may like it from hand to hand.
>
> (Bukhari and Muslim (repr.) 1990: book 9:5854)

Another *Hadith* is that narrated by Abu Sa'id Al-Khdry on the Prophet; he says:

> Do not sell gold unless an equivalent for an equivalent; do not prefer one and not the other [i.e. no discrimination between equivalents]. Do not sell what is available now for what is not available at the place of sale.
> (Abu Saaid Al-Khdry 1985: 1967)

By interpreting these traditions, Muslim *Fuqaha* (*jurists*) distinguish two types of sales usury (Al-Khadri 1958):

1 Increase Usury (*riba al-fadl*), which occurs when there is a transaction where items of the same kind of commodity capable of *riba* (*mal ribawi*) are exchanged or where there is an increase in either item over the other, even if they differ in quality. Therefore, when items of the same type are exchanged in sale, if either of them carries an increase over the other, this increase is considered *riba* (Sayoti 1980: 1:365).
2 Delayed Payment Usury (*riba an Nasi'ah*), a form of sale usury that occurs if there is a sale where both items are properties subject to usury (*mal ribawi*) but only one of the items is received at the time and place of the sale and the other item is received at a later date. Therefore, delayed payment usury occurs when an item, available at the place of sale, is sold for an item which is not available at the place of sale, even if the two items exchanged are equal in quantity in order to avoid increase usury. Equality of exchange of both items does not hold here, as there is a time difference in their exchange (Al-Tabari 1978: 4:63).

This issue is, however, one on which not all Islamic *jurists* are united. A close examination of all the different views postulated reveals great divergence in both interpretation of the Quranic verses and of the Prophet's *Hadith* on the subject of *riba* (ibid.: 66). Though such divergences are classic examples of the ever fluid and ongoing debates in the realm of Islamic jurisprudence, they should be seen as differences of detail rather than major disagreements. It is worth noting that in spite of such differences on the finer details, the opinion of the majority is in favour of the Quranic call for cancellation of a debt if the debtor is in financial difficulties. All are agreed that this stipulation follows the verses that prohibit *riba* (Issa 1974):

If the debtor is in a difficulty, grant him time till it is easy for him to repay. But if ye remit it by way of charity, that is best for you if ye only know (2:280).

Unlike its precursor – medieval Christianity – which allowed the offer of interest as a gift (even though this was regarded as a dangerous exception), Islam does not allow even voluntary interest in the form of a gift to the lender. However, the post-Reformation Christian standpoint on this is very different from Islamic thought, as it is now far removed from its origin (Taylor and Evans 1987: 19).