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BASIS AND MODELS OF TAKAFUL: THE NEED FOR IJTIHAD

Religious basis

An Islamic alternative to conventional insurance system is known as Takaful. This is based on the concept of Ta'awun (mutual assistance). Under this system, members of the society mutually and voluntarily agree to contribute money to support a common goal of providing mutual financial aid to the members of the group in case of specific need. This is a system based on mutual protection and solidarity.

Ta'awun, forms the basis of many Islamic practices. The teaching of Islamic principles has led to several forms of mutual assistance, both social and economic. Takaful, as was practiced in the sixth century actually evolved from tribal practices of mutual assistance dating back to pre-Islamic times.

In the present day, Takaful mechanism has evolved from three Quranic principles viz mutual protection, mutual cooperation and mutual responsibility. The Quran mentions in several places regarding protection from hunger and fear. The Quran say , "(He) who has fed them against hunger and made them safe from fear." (Quraish :4) The Prophet (s) said, "Indeed a believer is one who can give security and protection to the life and property of mankind." (Ibne Mazah) The Prophet also said, " A person is not a believer if he sleeps comfortably on a full stomach while his neighbor suffers from hunger." Regarding cooperation, the Quran says, "Help one another in furthering virtue and God-consciousness(Taqwa) and do not help one another in furthering evil and enmity."(Maida 5:2)

The Sunnah has also established the principle of cooperation. The prophet said, "A Muslim is the brother of a fellow Muslim. He should neither commit oppression upon him nor ruin him; and he who meets the needs of a brother, Allah will meet his needs and he who relieves his brother from hardship, Allah will relieve him from the hardship to which he could be put on the day of judgment (Muslim). He further said;

- "One is not judged as righteous until he cares for his brother as much as he cares for himself." (Bukhari)
- If any one does not have compassion towards others he does not get any compassion from God. (Mutafaq Alaihi)
- Each one of you has a responsibility and each one of you is responsible towards those under your responsibility (Mutafaq Alaihi)

In fact, the feeling of responsibility towards one another is the foundation of solidarity of Islamic community. In order to perform our responsibilities, we need to cooperate and we need to protect the property and life of the members of the society.

Philosophical basis

Islamic Insurance or Takaful is a concept of mutual cooperation to guarantee mutual protection of the members. It is a response to what Allah wants Muslims to do on a cooperative basis to achieve the Ummah's interest. It fulfills the social obligations towards financial assistance. Takaful is a service to Muslim Ummah. It is basically a

welfare scheme. Takaful mechanism is an example as to how the principles of Islamic Shariah can help to create new socio-economic mechanism based on equity, justice and fair play.

By ensuring financial assistance in times of need and providing indemnity against accidental loss of property, Takaful serves public interest and, therefore, can play an important role in the society. The family Takaful system facilitates capital formation of individual households. The collective surplus funds can be invested for the social welfare projects and economic development of the community. General Takaful schemes can facilitate trade, commerce and best utilization of resources. Takaful mechanism also encourages Mudarabah as mode of investment and can play a key role for the betterment of the Muslim society throughout the world.

Some western thinkers opine that Takaful is an innovative financial instrument. This is not the whole truth. It is basically a socio-economic device which is being practiced on the basis of the principles of Shariah, where human aspect is more important than the material one. It relies more on moral, ethical and human aspect than on the material aspects. Takaful is a system where people are encouraged to contribute money for mutual help in times of need. This unique mechanism ensures cooperation and mutual help.

Operational System

Islamic insurance is based on principles of cooperation, and mutuality. It encompasses the elements of shared responsibility, joint indemnity, and solidarity, whereby the policyholders cooperate among themselves for their common good. Every policyholder pays his subscription to help those who need assistance. It does not derive advantage at the cost of others but at the same time ensures financial protection or indemnity against loss. The main purpose of this system is not profit but to uphold the principle of "bear ye another's burden". The role of this practice indicates that the Takaful operators are in fact the managers or trustees of the policyholders' fund.

Presently, apart from the purely cooperative concept of Takaful system, different commercial models have evolved and are being practised. The Mudaraba model is most common in South Asian countries. Under this model the surplus is shared between the policyholders and Takaful operator. Under this model, Takaful operators take share in the underwriting surplus as well as on the returns of invested premiums. On the other hand under the wakala model, the Takaful operators do not take part in any profit sharing rather charge fees for services provided. Whatever is the mode of operation, Takaful is perceived as cooperation for the good cause of the people, for the betterment of the Ummah.

In Takaful, the participants are virtually the insured and the insurer. The participants jointly cooperate to compensate the risks incurred by one of the participants from their contribution. The element of cooperation in takaful is between the participants themselves. The relation of the company and the participant is governed by the principles of business and or exchange contract. When we say that Islamic insurance is based on donation and not for profit making, we do not mean that the operator is not aiming at profit. The takaful operator manages the underwriting and investment activities in pure business and trade basis.

The Mudaraba concept is relevant to takaful system because it governs the relationship between the participants as capital provider and the takaful operator as an entrepreneur. The main aim of participants is not mudaraba. It is their secondary objective. Therefore, the family takaful operators divide the contributions into two sets, namely participants, special account (taburru) and participants, account (Mudaraba).

As an alternative to Mudaraba system, Wakala system is being practised in the Middle Eastern countries. The basic concept of this system is that the takaful operator acts as wakil for the participants. The wakala fee transferred to the shareholders account. Under this model, 100% of the operating surplus is distributed among the participants. In case of deficit, the shareholders are required to provide karze hasana to the participants to pay for the deficit, which will be returned from future surplus. In a typical waqala contract, the tabarru is conditional as it is used to pay claims. But if and when there is surplus in tabarru fund, this will be given back to the participants.

Some of the Shariah scholars have critically analyzed the Wakala system and have suggested to incorporate the concept of Waqf into the Wakala model. Under this revised model, the operator would initially make a donation to establish a benevolent fund called the Waqf Fund. When this Waqf is created, the shareholders will lose their ownership rights on the waqf. However, this fund will be administered by the operator. The donations received from the participants, seeking takaful protection, will also be deposited into this fund and the combined amount will be used for investment. Profits earned will be deposited into the same fund. Participants will be given benefit from this Waqf fund. The Waqf fund would be allowed to form contingency reserve fund apart from usual technical reserves. The Waqf fund rules would define the basis for compensation and financial help, and rules for sharing surplus between the members and operators.

Takaful Practices

Many Islamic scholars suggest that purely cooperative or mutual form of insurance can be the basis of Islamic Insurance. In cooperative model, the management and control are in the hands of the members, who are also the policy holders. The insured and the insurers are the same people. The only purpose of such a model is mutual protection and security. There is no element of profit. Surplus, if any, needs to be ploughed back into the insurance fund. Contributions of the participants may also be increased or decreased as per experience of the operation of the scheme. However in Malaysia and other ASEAN countries, Islamic Insurance is being practised as Tejari Model, i.e., commercial in nature. The operators under the Tejari model are supposed to make profit. Under the Tejari Model, contractual relationship between the operator and the participant is on the basis of Mudaraba mechanism. In many of the middle eastern countries where Tejari model is being followed, the contractual relationship between the operator and the participants is that of wakala.

Co-operative and mutual model of insurance can be operated in a society, where the participants are conscious and capable of running the technical aspects of insurance operation. Moreover, funds should be available to start the venture. Therefore, the commercial model is being practised. In most cases, mudaraba system is being followed for sharing the surplus. At present, there are three different systems of Mudaraba mechanism. Some of the companies follow a pure mudaraba system, where the participants and the operator share direct investment income. Underwriting surplus, if any, is distributed entirely to the participants only. Some companies follow a practice of sharing surplus of the fund, and profit from investment is ploughed back to the fund. A third practice is to share both the surplus and the investment income between the operator and the participants.

With regard to the eligibility of participants in the share of the surplus, there are two different approaches. Some are of the opinion that participants will be eligible to participate in the distributable surplus, provided they have not made any claims or received any takaful benefits from the operator, or if they have surrendered/terminated policies. Others feel that the participants are eligible to the share of surplus if the claim is less than the contribution.

In a majority of the middle eastern countries the concept of wakala is being followed. The basic concept is that the takaful operators act as Wakeel (agent) for the participants. Under this system the operator should get a fee out of the contributions made by the participants. However, we observe several different systems of remunerating the operators. Under the pure wakala system, the operator charges a fixed amount of fee for services rendered. Some follow a modified approach where a percentage share of the underwriting surplus is paid as a performance incentive for the operator. Another approach of wakala system is on the basis of the concept of wakala as well as waqf. Under this approach the operator would initially make a donation to establish the waqf fund. In this modified approach of the wakala system the relationship of the participants and of the operator is directly with the Waqf fund, and the participant donates to the fund unconditionally and becomes a member. The rate of donation would be appropriate to the risk of the participants/assets as per underwriting principles. The Waqf fund rules would define the basis for compensation of losses to its members. All operational costs that would be incurred for providing takaful services be met from Waqf Fund. For performing the services, the operator would be eligible for taking a defined remuneration, which would be paid from the Waqf fund. The operator is also entitled to share in the surplus either as wakeel or as mudareeb. The relationship between the operator and the participants is based on three concepts, Wakala, Waqf and Mudaraba. This appears to be more easy to implement and may contribute further to the growth of the Islamic Insurance as opposed to conventional Insurance.

Need for Ijtihad

Insurance is an economic necessity. But Shariah concept of Takaful is absent in the conventional insurance mechanism. Therefore, there is an urgent need to introduce Shariah based principles and mechanism. This is why the Shariah scholars of the modern age have studied insurance mechanism in depth in order to reach a Shariah ruling that could encourage the Muslims throughout the world to avail of the services of insurance for their own benefit.

The objective of insurance is to protect individuals against risks of life, health and wealth. The concept of insurance is acceptable within the framework of Islamic principles. While most of the members of Muslim community are financially handicapped, the establishment and operation of Takaful is the need of the time. The Shariah requires that takaful mechanism should ensure benefit for all the contracting parties. In Islamic law, contracts must serve the interest of both parties equally. An Islamic Insurance company, therefore, should endeavor to meet the objective of cooperation and solidarity among the participants. The contributions made by the participants belong to them and not to the operators as being practised by conventional insurance companies.

In conventional insurance the contract is based on the principles of exchange of interest. The relationship is designed in such a way that the insured buys protection by payment of premiums and the insurer provides protection against the insured risk. Under Islamic law, insurance transactions can not be concluded on this basis of buy and sale contract. Takaful mechanism requires that the mutual assistance of the participants should be the prime objective and should be operated mainly by virtue of the donation (tabarru) contract.

Need is the mother of invention. Like any other product or service, innovation takes place when there is a demand. There is a demand for Shariah compliant services for covering risks of life, property and liability. Therefore, takaful companies have been established to meet the demand of the Muslim Ummah throughout the world. However, Takaful system is still in the process of evolution. Present developments are very encouraging in terms of demand. There is a growing interest in this area both in Muslim and Non-Muslim countries. The ultimate goal of the professionals and Shariah

scholars is to evolve an ideal system commensurating with Shariah principles and thus to gain a greater confidence of the consumers.

Under the present circumstances, it appears, that cooperative or mutual insurance would be ideal as a substitute of conventional social insurance. There is an absence of social insurance system in the Muslim world. However, when Islamic Insurance is being offered as a substitute of conventional commercial insurance, “Tejari” system seems to be better for us to adopt.

Which system to be followed depends upon the perception of the professionals responsible for running the operation. What is clear to us that either of the two models (Mutual or Tejari) can be used on Sharia principles and a combination of various systems can also be used under the Shariah guidelines. What is most important for us is to understand that insurance in its present form did not exist during the Prophet's time. Therefore, Ijtihad need to be used to decide the legal position. Here lies the crucial role of our Shariah scholars. Ijtihad must be based on the Quran and the Sunnah. First of all, we shall have to be guided by the Book of Allah- the Quran. If we do not find any clear guidance, we shall be following the Sunnah of the Prophet of Allah. If we do not find any specific guideline in the Quran or Sunnah, we will exert our own judgments if and when there is no clear indication from these sources.

Commercial transactions are constantly developing from one generation to another to meet the needs of a society. It also varies from country to country. Market practices are different. There are also differences in rules, regulations and laws of commercial and financial transactions. Variations and changes are unavoidable and Islamic law does not resist to whatever changes taking place on this earth. Therefore, various models and systems under the Shariah framework ought to respond to these changes to sustain the relevancy of Islamic Law, throughout the centuries. Ijtihad is an everlasting tool for Islamic dynamism. Modern Islamic jurists need to exercise their independent legal reasoning to formulate new ideas and alternatives for the growth and survival of Islamic Insurance system in the contemporary world.

If you would like more information on ICMIF and its services to the takaful sector, please contact Sabbir Patel (sabbir@icmif.org), or visit www.takaful.coop.

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